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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

The Current State Of 'Class Arbitration' Law

By **Gilbert Samberg**


Gilbert Samberg

Law360, New York (June 12, 2017, 12:02 PM EDT) -- We recently began a series of articles in which we ask whether "class arbitration" — meaning the utilization of a Federal Rule of Civil Procedure 23 class action protocol in an arbitration proceeding — is ultimately viable, considering arbitration's essential nature, or is it an oxymoron? Here, we examine several elements of the current law, muddled as it is, regarding class arbitration.

Thus far the U.S. Supreme Court has addressed a few issues concerning "class arbitration," including (1) the fundamental significance of the arbitration agreement; (2) the enforceability of a purported contractual waiver of class arbitration; and (3) the extent of and criteria for judicial review of an arbitrator's award concerning the permissibility of class arbitration.

On the other hand, the Supreme Court has not yet focused on the ultimate viability and enforceability, or the res judicata effects, of a class arbitration award (a) vis-à-vis a noncontracting, nonparticipating "class" member, or (b) vis-à-vis a party to an arbitration agreement who made no bilateral agreement with such a class member to arbitrate. Thus, the ultimate viability of class arbitration has not been addressed squarely by the Supreme Court.

1. FAA Neither Authorizes Nor Prohibits Class Arbitration

The Federal Arbitration Act (FAA), 9 U.S.C. §§1, et seq., says nothing about class arbitration. It does not permit or prohibit such a procedure, nor does any other statute expressly prohibit or create a right to employ such a procedure.

2. The Arbitration Agreement is King

Contracting parties are "generally free to structure their arbitration agreements as they see fit," and to "specify with whom they choose to arbitrate their disputes." Stolt- Nielsen S. v. AnimalFeeds International Corp., 559 U.S. 662, 130 S. Ct. 1758, 1774 (2010). Therefore, "a party may not be compelled under the FAA to submit to a class arbitration unless there is a contractual basis for concluding that the party agreed to do so." Id. at 1775. Generally, class arbitration is effectively prohibited unless (a) it is clearly and unmistakably permitted by an arbitration agreement, or (b) some governing rule of law or decision under which the parties are arbitrating creates a default rule permitting it. Oxford Health Plans v. Sutter, 133 S. Ct. 2064, 2066 (2013).

Regarding the first basis, the parties' incorporation by reference in an arbitration agreement of rules that permit class arbitration could suffice. In that regard, there has been significant litigation concerning the incorporation by reference of the American Arbitration Association's Supplementary Rules for Class Arbitration (eff. Oct. 8, 2003) (SRCA). Those rules provide procedures for determining (a) who will decide whether class arbitration is permitted (the arbitrator); and (b) whether the arbitration agreement permits class arbitration (incorporation of the SRCA is not to be a factor in that regard, however, see SRCA 3).

Incorporation of the SRCA "by reference" does not require much, nor is it determinative. The

AAA's announced policy is that it will administer a class arbitration if the arbitration agreement (a) is silent concerning "class claims," consolidation or joinder of claims; (b) adopts any arbitration rules of the AAA; and (c) does not (expressly or implicitly) exclude the SRCA. Thus, parties who expressly agree to any of the sets of arbitration rules of the AAA, including its Commercial Arbitration Rules, and are otherwise silent regarding class arbitration, are deemed to have consented to the AAA's SRCA. See, e.g., Reed v. Florida Metropolitan University, 681 F.3d 630, 635 (5th Circuit 2012), citing 1 Oehmke, Commercial Arbitration § 16:16 (April 2012). However, that consent and incorporation does not constitute an agreement to class arbitration, which is a matter to be adjudicated by the arbitrator. See SRCA § 3.

As to the second basis (a governing rule of law), the Supreme Court has rejected the argument that "federal law secures a non-waivable opportunity to vindicate federal policies" by class arbitration using the procedures in Federal Rule of Civil Procedure 23 or "some other informal class mechanism in arbitration." American Express Co. v. Italian Colors Restaurant., 133 S.Ct. 2304, 2310 (2013), citing AT&T Mobility v. Concepcion, 563 U.S. 333, 131 S.Ct. 1740 (2011). Thus, the fact that the parties would be able to litigate via class action in the absence of an arbitration agreement is not a basis to conclude that they agreed to class arbitration when they entered into an arbitration agreement. See, e.g., Reed v. Florida Metropolitan Uniersity., 681 F.3d 630, 641-43 (5th Cir. 2012). Moreover, "class arbitration, to the extent it is manufactured by [state law] rather than consensual, is inconsistent with the FAA." Concepcion, 131 S.Ct. at 1751-52.

Nevertheless, as a possible example of that second basis (a governing rule of law), the Fair Labor Standards Act provides that an action to recover unpaid minimum wages or overtime may be maintained against an employer by any one or more employees "for and on behalf of himself or themselves and other employees similarly situated." 29 U.S.C. § 216 (2012). Many employee-claimants arbitrating FLSA disputes have contended on this basis that they have a right to conduct a class arbitration, whether the arbitration clause in question is silent concerning class arbitration or even if it prohibits or purports to waive it. The federal circuit courts are split on this issue, but U.S. Supreme Court appears set to address it during its current term, when it takes up three consolidated cases concerning this matter.

3. Courts Must Enforce Arbitration Agreements According to Their Terms

The FAA requires courts to enforce arbitration agreements in accordance with their terms. See, e.g., 9 U.S.C. § 4. The interpretation of such clauses is typically a matter of state contract law. See Stolt-Nielsen, 559 U.S. at 681 ("interpretation of an arbitration agreement is generally a matter of state law"); Greentree Financial Corp. v. Bazzle, 529 U.S. 444 (2003) (where class arbitration is not clearly prohibited in an arbitration clause, whether it is permissible in a particular arbitral proceeding is a matter of contract interpretation applying state law); 2 Domke on Commercial Arbitration § 32:32 (June 2016); see also, FAA § 2.

That is, however, subject to the condition that state law must treat an arbitration agreement no differently than any other agreement. See, e.g., Kindred Nursing Centers LP v. Clark, 2017 U.S. LEXIS 2948 (May 15, 2017).

4. Silence is Not a Basis For Finding Agreement to Class Arbitration

One takeaway from Stolt-Nielsen has been that under the FAA, a party may not be compelled to submit to class arbitration unless "there is a contractual basis for concluding that the party agreed to do so ..." 559 U.S. at 648-85, and the parties' mere agreement to arbitrate is not a basis upon which to infer that they authorized class arbitration, id. Therefore, silence in an arbitration clause about class arbitration cannot be construed to indicate an agreement to it.

> The U.S. Supreme Court ... held that the differences between bilateral and class-action arbitration are too great for arbitrators to presume that the parties' mere silence on the issue of class-action arbitration constitutes a consent to class-action arbitration ...

1 Oehmke, Commercial Arbitration §16:1; see also, 2 Domke, Commercial Arbitration § 32:32. Put another way, it is not enough under Stolt-Nielsen that the terms of an arbitration agreement could support a finding that the parties did not preclude class arbitration. E.g., Reed v. Florida Metropolitan University, 681 F.3d 630, 644 (5th Cir. 2012).

5. Parties Can Agree to Class Arbitration

A few years after Stolt-Nielsen, the Supreme Court reviewed a similar but crucially distinguishable situation in Oxford Health Plans v. Sutter, 133 S. Ct. 2064 (2013). As in Stolt-Nielsen, the parties in Oxford Health had agreed to have an arbitrator decide whether their arbitration agreement permitted class arbitration notwithstanding that it was silent in that regard. Id. at 2067. In Oxford Health, however, the arbitrator indicated that he was interpreting the arbitration clause in deciding that class arbitration was indeed permitted. The Supreme Court refrained from second guessing the arbitrator, in accordance with established jurisprudence concerning such judicial review, and thus affirmed the confirmation of the award, which determined that the parties' agreement authorized class arbitration. See, id. at 2071. (Both the Oxford Health and Stolt-Nielsen decisions could also be said to support the proposition that class arbitration is permitted if an arbitrator interprets the governing arbitration agreement as allowing it.)

Thus, as evidenced by the Stolt-Nielsen and Oxford Health opinions, the Supreme Court has focused more on maintaining the integrity of the analytical framework for judicial review of arbitral awards (in the context of a petition to vacate or confirm an award) than on addressing the question of the fundamental legal viability of a class arbitration award.

6. Class Arbitration Waiver

A class arbitration waiver in an arbitration agreement is generally enforceable under the FAA. American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304, 2312 (2013).

7. Who Decides if Class Arbitration is Permitted? It Depends.

The basic rules are as follows. Questions of arbitral procedure are presumptively for an arbitrator, not for the court to decide. Howsom v. Dean Witter Reynolds Inc., 537 U.S. 79, 84, 123 S. Ct. 588 (2002). On the other hand, "arbitrability" questions — including "certain gateway matters, such as whether parties have a valid arbitration agreement … or whether a concededly binding arbitration clause applies to a certain type of controversy — are presumptively for the courts" to decide. Oxford Health, 133 S. Ct. at 2068 n. 2.

However, even gateway questions of arbitrability are for the arbitrator, rather than for the court, where the parties "clearly and unmistakably [so] provide" in their arbitration agreement. AT&T Technologies Inc. v. Comm'ns Workers of Am., 475 U.S. 643, 649, 106 S. Ct. 1415 (1986). "The agreement to arbitrate a gateway issue is simply an additional, antecedent agreement the party seeking arbitration asks the federal court to enforce, and the FAA operates on this additional arbitration agreement just as it does on any other." Rent-A-Center, West Inc. v. Jackson, 561 U.S. 63, 130 S. Ct. 2772, 2778 (2010). Thus, the parties could agree that the class arbitration issue should be decided by an arbitrator, see Oxford Health, 133 S. Ct. at 2070-71, and that would be binding.

Such a "clear and unmistakable" agreement might include, for example, the effective adoption of the AAA's Supplementary Rules for Class Arbitration, as previously described.

Furthermore, in at least the Eleventh Circuit, the parties are deemed to have clearly and unmistakably agreed that an arbitrator should determine whether class arbitration is permitted based merely on the parties' adoption of the Commercial Arbitration Rules (CAR) of the AAA without more. The reasoning is that CAR 8(a) is a sufficient basis for that. Rule 8(a) provides that:

> The arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope or validity of

arbitration agreement.

See Terminix International Co. v. Palmer Ranch Ltd. Partnership, 432 F.3d 1327, 1332 (11th Cir. 2005); CFL Pizza LLC v. Hammack, 2017 U.S. Dist. LEXIS 14081 at *8 (M.D. Fla. Feb. 1, 2017).

The question of whether class arbitration is permitted in effect determines the parties to an arbitration proceeding — a gateway issue. It is therefore arguable that, in the absence of an agreement otherwise, the court, rather than an arbitrator, should decide that question of party arbitrability in the first instance. Howsam v. Dean Witter Reynolds Inc., 537 U.S. 79, 83 (2002); First Options of Chicago Inc. v. Kaplan, 514 U.S. 938, 943-46 (1995).

That would, however, be contrary to the 2003 plurality decision in Greentree Financial Corp. v. Bazzle, 529 U.S. 444 (2003), that the permissibility of class arbitration is a procedural (nongateway) issue for the arbitrator. Bazzle, 539 U.S. at 454 (Breyer, J. for a plurality of four justices). Thus in Bazzle, the Supreme Court vacated the arbitral award in question and sent the matter back to the arbitrator to decide whether a "class arbitration" had been permitted by the pertinent arbitration agreement. The dissent in Bazzle (Chief Justice William Rehnquist, joined by Justices Anthony Kennedy and Sandra Day O'Connor), on the other hand, considered that threshold question to be for the court, rather than for an arbitrator. Id. at 455. (Furthermore, they opined that the arbitration clause language was clear enough so that a court could determine that class arbitration was not permitted, id. at 458-59.)

Subsequently, the court in Stolt-Nielsen confirmed that Bazzle "did not yield a majority decision" on this issue. Stolt-Nielsen, 130 S.Ct. at 1772. Thus, it arguably remained open at the Supreme Court level, Reed v. Florida Metropolitan University, 681 F.3d 630, 634 (5th Cir. 2012), whether, in the absence of agreement by the parties regarding who should decide, the relevant issue is a gateway matter for courts to decide or a procedural matter for the arbitrator to decide. See Stolt-Nielsen, 559 U.S. at 679; Oxford, 133 S. Ct. at 2068 n. 2; In re A2P SMS Antitrust Litigation, No. 12-CV-2656 (AJN), 2014 U.S. Dist. LEXIS 74062 (S.D.N.Y. May 29, 2014)(analyzing precedent).

After Stolt-Nielsen, lower federal courts split on this issue and then seemed to gravitate toward a recognition that the determination is one of party arbitrability — i.e., whether a person (for example, a nonsignatory "class" member) is bound by an arbitration agreement — which is for the court in the first instance. See, e.g., DiMartino v. Dooley, No. 08 CIV 4606, 2009, at *4, *3 (S.D.N.Y. Jan. 6, 2009); see also, Sarhank Group v. Oracle Corp., 404 F3d 657, 661 (2d Cir. 2005) ("arbitrability is not arbitrable in the absence of the parties' agreement"). This is consistent with the requirement of Section 4 of the FAA (9 U.S.C. § 4) — that is, "[t]he question [of] whether a person is a party to [an] arbitration agreement ... is included within the statutory issue of the making of the arbitration agreement." McAllister Bros. Inc. v. A&S Transportation Co., 621 F2d 519, 524 (2d Cir. 1980) (citation and internal quotation marks omitted).

8. Persons Who May Be Compelled to Arbitrate

A court is not authorized by the FAA to compel arbitration by parties who are not bound by an arbitration agreement. EEOC v. Waffle House Inc., 534 U.S. 279, 289 (2002); see 9 U.S.C. § 4. If parties have not agreed to arbitrate, the courts have no authority to mandate that they do so. Cf., United Steel Workers of America v. Warrior & Gulf Navigation Co., 363 U.S. 574, 582 (1960).

Conversely, a person who may have a claim against "X," but who is not party to a relevant arbitration agreement with "X," generally may not arbitrate that claim, notwithstanding that another person with a similar claim and an arbitration agreement with "X" may do so. See, Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 19-20 (1983).

Persons who are bound by an arbitration agreement are (1) the party-signatories to the agreement and (2) those deemed bound by it in accordance with contract and/or agency law principles. Among the legal bases for compelling (or enabling) a nonsignatory of an arbitration agreement to arbitrate against a signatory are veil piercing, estoppel, incorporation of an arbitration agreement by reference, assumption, agency, etc. E.g., Thomson-CSF SA v. American Arbitration Association, 64 F.3d 773, 776-778 (2d Cir. 1995).

9. Parties Bound By a Class Arbitration Award

The Supreme Court indicated in Concepcion that noncontracting, nonparticipating class members are not bound by a purported class arbitration award unless they had had notice, an opportunity to opt out, and adequate representation. Concepcion, 131 S.Ct. at 1751. The Supreme Court subsequently indicated that class members who have not opted into a class arbitration proceeding are not bound by a purported class arbitration award. See, Oxford Health Plans LLC v. Sutter, 133 S. Ct. 2064, 2072 (2013).

However, the Supreme Court does not appear to have identified precisely when a noncontracting, nonparticipating class member is bound by a class arbitration award. Nor has the Supreme Court indicated when a party to an arbitration agreement is bound by an award in favor of (or against) a noncontracting, nonparticipating class member. Currently, therefore, we cannot infer that a class arbitration award adjudicates not just the rights of parties to a bilateral arbitration agreement, "but … the rights of the absent parties as well." Stolt-Nielsen v. AnimalFeeds International Corp., 559 U.S. 662, 686 (2010).

10. Vacatur of Award If Arbitrator's Powers Exceeded

The FAA provides that a court must confirm an arbitral award "unless the award is vacated, modified, or corrected as prescribed in Sections 10 and 11 [of the FAA]." See FAA § 9 (9 U.S.C. §9). One of the specified grounds for vacatur of an award is "where the arbitrators exceeded their powers." FAA § 10(a)(4).

Arbitration is a creature of contract, and the scope of an arbitrator's powers are generally set by the terms of the arbitration agreement, on which his jurisdiction is founded. The parties' bilateral agreement effectively identifies the parties, the dispute(s) and the procedures in the arbitration.

Logically, if an arbitrator goes beyond the authority given him by the arbitration agreement, he has exceeded his powers. And an arbitration award that reflects that overstepping may in principle be vacated under FAA § 10(a)(4).

Arguably, an arbitrator exceeds his powers if his award purports to bind — i.e., to burden or benefit, and to have a preclusive effect on — (a) any person who has not agreed to arbitrate or (b) a contracting party relative to a person with whom that party is not bound by agreement to arbitrate.

One might expect, therefore, that "[a]n arbitrator may exceed his powers by ordering class arbitration without authorization." Sutter v. Oxford Health Plans, 675 F.3d 2125, 220 (3d Cir. 2012), affirmed on other grounds, Oxford Health Plans v. Sutter, 133 S. Ct. 2064 (2013); see, Reed v. Florida Metropolitan University 681 F.3rd 630 (5th Cir. 2012) (Clause Construction Award under SCRA). But, as noted earlier, the U.S. Supreme Court has not yet made an analysis in such terms. Rather, it has focused on the limits of judicial review of an arbitrator's award. For example, Stolt-Nielsen concerned vacatur of an award where the arbitrators had ordered class arbitration notwithstanding that there was no evidence that parties had agreed to it. Stolt-Nielsen, 130 S. Ct. at 1770.

However, the Stolt-Nielsen court did not address the implications of an arbitrator's potential auto-expansion of his jurisdiction by issuing an award that binds noncontracting persons, but rather focused on the mode of analysis by the arbitrator. So did the court in Oxford Health. There, the Supreme Court determined that the arbitrator's decision that the arbitration agreement permitted class arbitration survived the limited judicial review permitted under FAA § 10(a)(4) because the question for a judge on review is not whether the arbitrator construed the parties' contract correctly, but whether he construed it at all. In Oxford Health, the court determined that the arbitrator's method of analysis met that test, and therefore affirmed the Third Circuit's affirmance of the district court's refusal to vacate an arbitration award that authorized class arbitration.

Gilbert A. Samberg is a member of Mintz Levin Cohn Ferris Glovsky and Popeo PC based in the firm's New York office. He is a commercial litigator and arbitration practitioner who focuses on

international financial, commercial and technology-related disputes.

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