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Second Circuit Finds Class Action Waiver Deprived Plaintiffs of Antitrust Protections

by Christine A. Scheuneman, Brian D. Martin, Roxane A. Polidora, C. Douglas Floyd, Amy L. Pierce and Nathaniel R. Smith

Declining to enforce an arbitration clause on the grounds that the class action waiver effectively would preclude plaintiffs from enforcing their rights under the Sherman and Clayton Acts, the Second Circuit distinguished the U.S. Supreme Court's recent pro-arbitration decisions in Stolt-Nielsen, Concepcion *and* CompuCredit, *and instead relied on* Green Tree Financial Corp. *and other earlier U.S. Supreme Court decisions.*

Since 2010, the U.S. Supreme Court has handed down three pro-arbitration decisions—*Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758 (2010), *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011) and *CompuCredit Corp. v. Greenwood*, No. 10-948 (Jan. 10, 2012). Notwithstanding this trend, the Second Circuit Court of Appeals, on February 1, 2012, for the third time declined to enforce an arbitration clause with a class action waiver on the grounds that individual arbitration would effectively deprive plaintiffs of federal statutory antitrust protections under the Sherman and Clayton Acts. For the time being, the decision leaves the door open for plaintiffs to pursue antitrust claims as a class action in federal court in circumstances where the plaintiff can demonstrate that enforcement of a class action waiver would result in *de facto* antitrust immunity.

The Underlying Action and District Court's Decision

The named plaintiffs in *Italian Colors Rest. v. Am. Express Travel Related Serv. Co.* (aka *In re: American Express Merchants' Litigation*) are California and New York corporations that operate businesses which have contracted with the defendant, as well as the National Supermarkets Association, Inc., a trade association that represented the interests of independently owned supermarkets. The contractual relationship between the parties is a card acceptance agreement that includes a mandatory arbitration clause. The arbitration clause precluded a merchant from having any claim arbitrated on anything other than an individual basis. After litigation commenced, the district court granted the defendant's motion to compel arbitration, holding that the arbitration clause applied to the parties' disputes and that the enforceability of the class action waiver was for the arbitrator to resolve. The plaintiffs appealed.

The Second Circuit's Original Decision

The Second Circuit first decided that the class action waiver's enforceability was a matter for the court, not the arbitrator. Turning to the question of whether the class action waiver was enforceable, it found that *Green Tree Financial Corp.-Alabama v. Randolph*, 531 U.S. 79 (2000), controlled its analysis. Pursuant to *Green Tree*, a plaintiff can challenge a class action waiver clause on the grounds that it would be a cost-prohibitive method of enforcing a statutory right, provided that the plaintiff set forth sufficient proof to support such a finding. Plaintiffs had submitted evidence that an antitrust study and expert fees would approach $1 million, and the defendant had "brought no serious challenge" to that evidence. In an affidavit, the plaintiffs' expert stated that out-of-pocket expert costs for "individual plaintiff antitrust cases ha[ve] ranged from about $300 thousand to more than $2 million. However, after reviewing the complaint and doing some preliminary research in this case, it is my opinion that . . . the cost for this case will fall in the middle of th[is] range…" The Second Circuit considered that "while the Clayton Act does provide for treble awards along with the recovery of attorneys' fees and expenses, that was unlikely to assist plaintiffs where, as here, 'the trebling of a small individual damages award is not going to pay for the expert fees [plaintiffs' expert] has estimated will be necessary to make an individual plaintiff's case.'" The Second Circuit agreed that the clause "flatly ensures that no small merchant may challenge [the defendant's] tying arrangements under the federal antitrust laws." It then held that the class action waiver cannot be enforced because to do so would grant the defendant *de facto* immunity from federal antitrust liability.

The defendant filed a petition for writ of certiorari, which the U.S. Supreme Court granted. It vacated the Second Circuit's decision, and remanded for further consideration in light of its holding in *Stolt-Nielsen* that class arbitration could not be ordered unless there is a contractual basis for finding the parties agreed to class arbitration.

The Second Circuit's Decision on Remand After *Stolt-Nielsen*

On remand from the U.S. Supreme Court, the Second Circuit found *Stolt-Nielsen* did not require it to depart from its original analysis. The key issue it determined was whether the mandatory class action waiver is enforceable even if the plaintiffs are able to demonstrate that the practical effect of enforcement of the waiver would be to preclude their bringing Sherman and Clayton Act claims against the defendant. It concluded enforcement of the class action waiver would bar plaintiffs from pursuing their statutory claims because the "record evidence before us establishe[d], as a matter of law, that the cost of plaintiffs' individually arbitrating their dispute with [the defendant] would be prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws."

The Second Circuit's Reconsideration of Its Decision Post-*Concepcion*

The Second Circuit Distinguishes *Concepcion*

Shortly after the Second Circuit issued its post-*Stolt-Nielsen* decision, the U.S. Supreme Court held in *Concepcion* that California's Discover Bank rule—a rule that largely invalidated class action waivers in arbitration provisions in consumer contracts—is preempted by the Federal Arbitration Act (FAA) because it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Thereafter, in supplemental briefing, the defendant argued that *Concepcion* required reversal of the Second Circuit's second decision. The Second Circuit rejected this contention, finding that "a careful reading of [*Stolt-Nielsen* and *Concepcion*], demonstrates that neither one addresses the issue presented here." For a third time, the Second Circuit declined to enforce the class action waiver and to compel arbitration.

It first noted that whereas *Concepcion* analyzed whether a state contract law is preempted by the FAA, this case involved "the federal substantive law of arbitrability." It then noted that *Concepcion* and *Stolt-Nielsen*, taken together, clearly precluded the court from ordering the parties to participate in class arbitration. But it found that *Stolt-Nielsen* and *Concepcion* do not require that all class action waivers be deemed per se enforceable, and left open the question presented—whether a mandatory class action waiver clause is enforceable even if the plaintiffs are able to demonstrate that the practical effect of enforcement would be to preclude their ability to bring federal antitrust claims. It found useful guidance in other U.S. Supreme Court decisions addressing the issue of vindicating federal statutory rights via arbitration, and again found *Green Tree* to be controlling.[1] According to the Second Circuit, plaintiffs' evidence established "that the cost of plaintiffs' individually arbitrating their dispute with [the defendant] would be prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws." This evidence demonstrated "that the only economically feasible means for plaintiffs enforcing their statutory rights is via a class action." The Second Circuit confirmed that this is not a per se rule of unenforceability and that plaintiffs carry a heavy burden on a case-by-case basis to establish that arbitration is not economically feasible.

The Second Circuit Distinguishes *CompuCredit Corp.*

The Second Circuit also briefly touched on *CompuCredit Corp.*, in which the U.S. Supreme Court held that the Credit Repair Organizations Act did not preclude enforcement of an arbitration agreement. Unlike *CompuCredit*, the plaintiffs do not allege that the Sherman or Clayton Acts expressly preclude arbitration or that they expressly provide a right to bring collective or class actions. But the Second Circuit reasoned that "[a]lthough the Sherman Act does not provide plaintiffs with an express right to bring their claims as a class in court, forcing plaintiffs to bring their claims individually here would make it impossible to enforce their rights under the Sherman Act and thus conflict with congressional purposes manifested in the provision of a private right of action in the statute."

The Takeaway from the Second Circuit's Decisions

At first blush, *In re American Express Merchants Litigation* arguably appears to involve refusal by the Second Circuit to give effect to the *Concepcion* decision. But it is important to note the key distinction between those two cases: the Second Circuit's decision was based on a conflict between the purposes of two federal statutes—the FAA and the Sherman Act—whereas *Concepcion* involved a conflict between state law and the FAA. Although the FAA preempts conflicting state laws, the Second Circuit apparently concluded that the FAA stands on equal footing with federal statutes such as the Sherman and Clayton Acts. These distinctions should be kept in mind when assessing the enforceability of arbitration provisions that contain class waivers.

[1] The Second Circuit cited *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 161 (1974) ("Economic reality dictates that petitioner's suit proceed as a class action or not at all."), *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997) ("'The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights.'"), *Deposit Guar. Nat'l Bank v. Roper*, 445 U.S. 326, 338 (1980) ("[A class action] may motivate [plaintiffs] to bring cases that for economic reasons might not be brought otherwise… [, thereby] vindicating the rights of individuals who otherwise might not consider it worth the candle to embark on litigation in which the optimum result might be more than consumed by the cost."), *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 632 (1985) ("Arbitration is also recognized as an effective vehicle for vindicating statutory rights, but only 'so long as the prospective litigant may effectively vindicate its statutory cause of action in the arbitral forum'"), *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (the Court concluded that the plaintiff in that case could effectively vindicate his Age Discrimination in Employment Act claim in the arbitral forum), and *Green Tree Financial Corp.-Alabama v. Randolph*, 531 U.S. 79 (2000) (the Court acknowledged in dicta "that the existence of large arbitration costs could preclude a litigant… from effectively vindicating her federal statutory rights in the arbitral forum").

Nevertheless, one might question whether the Second Circuit's distinction between the state unconscionability doctrines at issue in Concepcion and the "vindication of federal statutory rights" analysis employed by it will ultimately prevail in other circuits and in the U.S. Supreme Court in view of the similarities between the two. In its previous decision in *Kristian v. Comcast*, 446 F. 3d 25 (1st Cir. 2006), for example, the First Circuit emphasized the close line between the two doctrines, noting that "[a]s a practical matter, there are striking similarities between the vindication of statutory rights analysis and the unconscionability analysis. In fact, many of the plaintiffs' unconscionability arguments were merely reiterations of their vindication of statutory rights arguments."

Finally, it is important to recognize that, in view of *Stolt-Nielsen*, the effect of the Second Circuit's decision is not to authorize judicially compelled class arbitration, but rather to avoid the arbitration clause entirely and to permit plaintiffs to litigate their claims as a class action in federal court.

Click here to read the *In re: American Express Merchants' Litigation opinion* (2d Cir. Feb. 1, 2012)

If you have questions, please contact the Pillsbury attorney with whom you regularly work or the authors or attorneys identified below:

Christine A. Scheuneman (bio)
Los Angeles
+1.213.488.7487
christine.scheuneman@pillsburylaw.com

Roxane A. Polidora (bio)
San Francisco
+1.415.983.1976
roxane.polidora@pillsburylaw.com

Amy L. Pierce (bio)
Sacramento
+1.916.329.4765
amy.pierce@pillsburylaw.com

Michael L. Sibarium (bio)
Washington D.C.
+1.202.663.9202
michael.sibarium@pillsburylaw.com

Brian D. Martin (bio)
San Diego
+1.619.544.3204
brian.martin@pillsburylaw.com

C. Douglas Floyd (bio)
San Francisco
+1.415.983.1438
douglas.floyd@pillsburylaw.com

Nathaniel R. Smith (bio)
San Diego
+1.619.544.3210
nathan.smith@pillsburylaw.com

Eric Fishman (bio)
New York
+1.212.858.1745
eric.fishman@pillsburylaw.com

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