In re *American Express Merchants' Litigation*[*]

I. INTRODUCTION

In May 2010 the United States Supreme Court vacated the Second Circuit's decision holding that a mandatory class action waiver contained in the American Express Company's card acceptance agreement with its merchants was unenforceable,[1] and remanded for further consideration in light of the Supreme Court's holding in *Stolt-Nielsen*.[2] On remand, the Second Circuit found that its original analysis and conclusion were unaffected by *Stolt-Nielsen*, and once again held that the mandatory class action waiver was unenforceable against Amex's merchants because the waiver "effectively strip[ped] plaintiffs of their ability to prosecute alleged antitrust violations."[3] More important, the Court found that *Stolt-Nielsen* does not stand for the proposition "that a contractual clause barring class arbitration is *per se* enforceable."[4] Thus, despite the Court's careful reconsideration, there remains uncertainty regarding the enforceability of class action waivers—it is still determined on a case-by-case basis in which courts balance the benefits of class actions with a federal policy favoring arbitration.[5] As Amex has petitioned the Supreme Court for certiorari, close attention should be paid to whether the Supreme Court will affirm the Second Circuit's decision or set new precedent on class action waivers.

II. FACTS AND PROCEDURAL HISTORY

A. *Facts*

The named plaintiffs in this class are divided into two groups: (1) California and New York corporations that operate businesses that have contracted with American Express ("Amex") to accept their payment card products; and (2) the National Supermarkets Association, Inc. ("NSA").[6] The class itself is comprised of "all merchants that have accepted American

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[*] *In re* American Express Merchants' Litigation, 634 F.3d 187 (2d Cir. 2011).

[1] *In re* American Express Litigation, 554 F.3d 300, 304 (2d Cir. 2009).

[2] Stolt-Nielson S.A. v. AnimalFeeds Int'l Corp., 599 U.S. ---, 130 S. Ct. 1758 (2010).

[3] *Amex*, 634 F.3d at 194.

[4] *Amex*, 634 F.3d at 193.

[5] *Id.* at 199.

[6] *Amex*, 554 F.3d at 305.

Express charge cards (including the American Express corporate card), and have thus been forced to agree to accept American Express credit and debit cards, during the longest period of time permitted by the applicable statute of limitations ... throughout the United States."[7] The basic contractual relationship between Amex and the plaintiffs is set forth in the Card Acceptance Agreement ("the Agreement").[8] Since 1999, the Agreement has contained a mandatory arbitration clause.[9]

The plaintiffs' substantive dispute with Amex centers on the "Honor All Cards" provision in the Agreement.[10] Amex charged merchants higher "merchant discount fees" for its traditional charge cards. Over the past decade, Amex developed a variety of new debit and credit card products—and although these products produced a lower sale-per-transaction rate, Amex nevertheless charged its merchants the same high discount rate as it did for its traditional charge cards. The merchants were obligated to accept these new card products because of the "Honor All Cards" provision. Thus, the plaintiffs assert that due to this provision, they are forced either to pay "supracompetitive" merchant discount fees or to stop accepting Amex products, which would significantly decrease their sales.[11] As a result, the plaintiffss brought suit claiming that the Agreement amounts to an "illegal tying arrangement" in violation of Section 1 of the Sherman Act.[12]

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[7] *Id.*

[8] *Id.*

[9] *Id.* at 306.

[10] "[The Agreement applies] to your acceptance of American Express© Cards ... *American Express Card(s)* ... shall mean any card or other account access device issued by American Express Travel Related Services Company, Inc., or its subsidiaries or affiliates or its or their licensees bearing the American Express name or an American Express trademark, service mark or logo." *Id.* at 308.

[11] *Amex*, 554 F.3d at 308.

[12] "The Supreme Court has defined a tying arrangement as 'an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.' A tying arrangement will violate Section 1 of the Sherman Act if 'the seller has appreciable economic power in the tying product market and if the arrangement affects a substantial volume of commerce in the tied market.' (internal quotation marks omitted)." *Id.* at 308 n.6 (quoting Northern Pacific Ry. Co. v. United States, 356 U.S. 1, 5–6 (1958); Eastman Kodak Co. v. Image Technical Servs., 504 U.S. 451, 462 (1992)).

B. *Procedural History*

After the plaintiff merchants filed their class action antitrust suit, Amex filed a motion to compel arbitration pursuant to the mandatory arbitration provision in the Agreement.[13] The district court granted Amex's motion, finding that because the mandatory arbitration provision was "paradigmatically broad" it applied to the dispute between the parties.[14] The district court also found that the enforceability of the arbitration clause was for the arbitrator to decide. As a result, plaintiff's substantive antitrust claim was dismissed.[15]

The plaintiffs appealed to the Second Circuit, which reversed the district court on both grounds, finding that (a) the enforceability of the arbitration provision was a matter for the court, not the arbitrator, to decide, and (b) the arbitration provision in the Agreement was unenforceable under *Green Tree Financial Corp.-Alabama v. Randolph*.[16]

Amex subsequently appealed to the Supreme Court, which vacated the Second Circuit's decision, and remanded the case for further consideration in light of its holding in *Stolt-Nielsen*.[17] The Second Circuit was then tasked with determining whether *Stolt-Nielsen* altered the Court's original analysis regarding the enforceability of the arbitration clause in the Agreement.[18]

III. THE *STOLT-NIELSEN* PRECEDENT

In *Stolt-Nielsen*, shipping company customers, including AnimalFeeds, brought suit against Stolt-Nielsen for illegal price fixing.[19] Although the parties were required to arbitrate their antitrust dispute, AnimalFeeds demanded class arbitration.[20] Because the arbitration clause was silent on the

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[13] *Amex*, 554 F.3d at 308.

[14] *Amex*, 634 F.3d at 191.

[15] *Id.*

[16] *Id.* ("[W]hen a party seeks to invalidate an arbitration agreement on the ground that arbitration would be prohibitively expensive, that party bears the burden of showing the likelihood of incurring such costs.") (quoting Green Tree Financial Corp.-Alabama v. Randolph, 531 U.S. 79, 92 (2d Cir. 2000)).

[17] *Amex*, 634 F.3d at 192.

[18] *Id.*

[19] *See Stolt-Nielsen*, 130 S. Ct. at 1764–65.

[20] *Id.* at 1765.

issue of class arbitration, the parties submitted AnimalFeed's demand to the arbitration panel to decide whether class arbitration was permitted.[21] The panel concluded that in light of expert testimony, the Supreme Court's decision in *Green Tree*, and policy considerations, the arbitration clause permitted class arbitration.[22]

Stolt-Nielsen appealed the panel's decision to the district court, which vacated the decision and concluded that the clause precluded class arbitration.[23] The Second Circuit then reversed on the narrow grounds that the panel's decision was not made in "manifest disregard" of the law, and thus the district court should have affirmed the decision.[24]

The Supreme Court later reversed, finding that "a party may not be compelled under the FAA to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so."[25] Since the parties had stipulated that there was no agreement on the issue of class arbitration, the Court held that "it follows that the parties cannot be compelled to submit their dispute to class arbitration."[26]

IV. THE SECOND CIRCUIT'S HOLDING AND REASONING

The Second Circuit on reconsideration held that *Stolt-Nielsen* did not affect its original analysis in which it found the class action waiver contained in the agreement between Amex and its merchants unenforceable.[27] Specifically, the Court found that where *Stolt-Nielsen* held that parties cannot be forced into class arbitration absent a contractual agreement, the appropriate focus in this case was "not on whether the plaintiffs' contract provides for class arbitration, but on whether the class action waiver is enforceable when it would effectively strip plaintiffs of their ability to prosecute alleged antitrust violations."[28]

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[21] *Id.* at 1765–66.

[22] *Amex*, 634 F.3d at 192–93.

[23] *Id.* at 193.

[24] *Id.*

[25] *Stolt-Nielsen*, 130 S. Ct. at 1775 (emphasis in original).

[26] *Id.* at 1776.

[27] *Amex*, 634 F.3d at 189.

[28] *Id.* at 193–94.

A. Stolt-Nielsen *Did Not Hold That Contractual Clauses Barring Class Arbitration Are* Per Se *Enforceable*

As the Supreme Court explained in *Stolt-Nielsen*, "the foundational FAA principle [is] that arbitration is a matter of consent."[29] Hence, a party could not be compelled to submit to arbitration unless there was a contractual basis upon which a court could conclude that the party agreed to arbitration.[30] In light of *Stolt-Nielsen*, Amex claimed that the opposite was true: its merchants must be compelled to submit to individual arbitration because the Agreement specifically waived class action lawsuits.[31] Additionally, Amex argued that *Stolt-Nielsen* rejected the use of public policy as a basis for finding arbitration agreement language void.[32]

The Second Circuit rejected both of Amex's arguments. First, the court noted that *Stolt-Nielsen* simply stands for the principle that parties cannot be forced to arbitrate unless they contractually agreed to do so.[33] Second, the court found that although *Stolt-Nielsen* "plainly rejects using public policy as a means for divining the parties' intent," the case did not bar courts from "using public policy to find contractual language void."[34] Thus, the Second Circuit's reconsideration of the effect of *Stolt-Nielsen* on its original analysis was simple and straightforward: it had no effect.[35]

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[29] *Stolt-Nielsen*, 130 S. Ct. at 1775.

[30] *Id.*

[31] *Amex*, 634 F.3d at 190–91.

[32] *Id.* at 199. Interestingly, Amex's argument here ignored the plain language of the savings clause of Section 2 of the FAA which provides that an agreement to arbitrate "shall be valid, irrevocable, and enforceable, *save upon such grounds as exist at law or in equity for the revocation of any contract.*" 9 U.S.C. § 2 (emphasis added). A contractual term is unenforceable on grounds of public policy if the interest in its enforcement is clearly outweighed by a public policy against enforcement of the term. *See* RESTATEMENT (SECOND) OF CONTRACTS § 178 (1981).

[33] *Amex*, 634 F.3d at 193.

[34] *Id.* at 199.

[35] *Id.* at 199. According to the Second Circuit the only effect *Stolt-Nielsen* had on the case was in the type of relief the the Court could have ordered because *Stolt-Nielsen* "plainly preclude[d] [the Court] from ordering class-wide arbitration." *Id.* at 200. As the court noted, however, it did not order class-wide arbitration in its original decision; hence, the type of relief ordered was a non-issue on reconsideration. *Id.*

B. *Amex's Class Action Waiver Provision Is Unenforceable Because It Precludes Merchant-Plaintiffs From Enforcing Their Statutory Rights*

Once the Second Circuit determined that *Stolt-Nielsen* had no effect on its original analysis, the court proceeded to rearticulate its reasons for finding the class action waiver at issue unenforceable. As the court explained, its evaluation of the enforceability of class action waivers is done "under the federal substantive law of arbitrability."[36] Part of that substantive law is a "vindication of statutory rights" analysis, which is the test the Second Circuit applied to the class action waiver contained in the Agreement.[37]

Under the statutory rights analysis, the Second Circuit first explained the unique role of the class action as a "vehicle" for vindicating statutory rights:

> [T]he class action device is the only economically rational alternative when a large group of individuals or entities has suffered an alleged wrong, but the damages due to any single individual or entity are too small to justify brining an individual action.[38]

The Second Circuit then focused on the issue of whether the mandatory class action waiver contained in the Agreement had the practical effect of precluding the Plaintiffs from bringing their antitrust claims in either an individual or collective capacity.[39] Thus, for example, if the costs of arbitration were prohibitively expensive for an individual party, a class action waiver may be unenforceable under the statutory rights analysis.[40]

However, the burden of proving prohibitive costs is on the party seeking to invalidate an arbitration agreement, and to carry that burden it must do more than speculate that it will incur prohibitive costs.[41] The most effective way for a party to invalidate an arbitration agreement on prohibitive-cost grounds is to produce expert testimony on the economic feasibility of

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[36] *Amex*, 634 F.3d at 194.

[37] *Id. See also* Kristian v. Comcast Corp., 446 F.3d 25, 63 (1st Cir. 2006).

[38] *Amex*, 634 F.3d at 194 (quoting Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 161 (1974)).

[39] *Amex*, 634 F.3d at 196.

[40] *Id.* at 196–97.

[41] *Id.* at 196.

pursuing a statutory claim individually or collectively—which is precisely what the merchant-plaintiffs did in this case.

Based on plaintiffs' expert report, the Second Circuit concluded that "the only economically feasible means for enforcing their statutory rights is via a class action."[42] Furthermore, Amex offered no challenge to plaintiffs' feasibility claim. Thus, the court held as a matter of law that "the cost of plaintiffs individually arbitrating their dispute with Amex would be prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws."[43]

V. CONCLUSION AND IMPACT OF THE SECOND CIRCUIT'S RULING

The Second Circuit's holding has made one thing very clear: courts deciding whether a class action waiver is enforceable will be faced with the difficult task of balancing the necessity of class actions with the "liberal federal policy favoring arbitration agreements."[44] It follows, therefore, that courts can only proceed on a case-by-case basis in evaluating the enforceability of class action waivers when a statutory right is asserted, which in turn can only lead to greater uncertainty.

For example, the Second Circuit held that the class action waiver was unenforceable because it prevented plaintiffs from vindicating their statutory rights under the antitrust statutes—a result Congress could not have intended when it included "strong private enforcement mechanisms" in those statutes.[45] However, the court explicitly stated that it did not conclude that class action waivers in arbitration agreements were per se unenforceable, nor did it conclude that such waivers were "per se unenforceable in the context of antitrust actions."[46]

Is then the key factor in evaluating the enforceability of class action waivers persuasive expert testimony on the prohibitiveness of the costs of pursuing individual arbitration? Clearly, Amex erred in its decision not to

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[42] *Id.* at 198.

[43] *Id.* at 197–98. The Second Circuit went on to explain that "[e]radicating the private enforcement component from our antitrust law scheme cannot be what Congress intended when it included strong private enforcement mechanisms and incentives in the antitrust statutes." Id. at 199. See also Reiter v. Sonotone Corp., 442 U.S. 330, 344 (1979).

[44] *Amex*, 634 F.3d at 199 (quoting Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983)).

[45] *Amex*, 634 F.3d at 199.

[46] *Id.*

challenge plaintiffs' demonstration that their claims could not "reasonably be pursued" as individual actions.[47] If it did, however, this case would have turned into a "battle of the experts" to determine whether plaintiffs could cost-effectively vindicate their statutory rights through individual arbitration—law and economics at its finest.[48]

Going forward, the most important question that remains is how can companies like American Express structure contractual arbitration clauses so that courts will enforce the agreement as written? In light of this case, *Stolt-Nielsen*, and Section 2 of the FAA, parties simply cannot rely on courts to enforce their arbitration agreements as written, especially when one party, such as Amex, uses the same class action waiver in each and every Agreement with its merchants. Nevertheless, parties committed to having their class action waivers enforced must now be prepared to spend more money and other necessary resources on financial and economic experts to withstand a statutory rights analysis—all in the name of arbitration.

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[47] *Id.*

[48] It might be worth noting here that the only option Amex's merchants had was individual arbitration or litigation, which means it is possible that the Second Circuit's analysis could have been different had the merchant-plaintiffs at least been afforded the possibility to arbitrate their claims as a class. However, the last thing large corporations want to do is submit to class-wide arbitration where FED. R. CIV. P. 23 does not exist—not to mention the standard of review courts apply to an arbitrator's decision.