An Emphasis on Arbitrator Authority—Arbitration at the Supreme Court (2012 to 2013 Term)

By Sherman Kahn

The United States Supreme Court issued two regular opinions and one *per curiam* opinion on arbitration during its 2012 term (commencing in October 2012 and extending until June 2013). While the Court's two regular opinions continued the Court's recent concern with the intersection between arbitration and class action procedures, an argument can be made that the overriding theme of this year's Supreme Court arbitration jurisprudence is judicial deference to arbitrators' decisions and those of the parties who appoint them. The Court's three opinions are discussed below.

A. *Nitro-Lift Technologies, L.L.C. v. Howard*[1]

Early in the term, the Supreme Court issued a per curiam opinion offering a sharp rebuke to the Oklahoma Supreme Court for declaring non-competition provisions in two employment contracts null and void under an Oklahoma statute when, according to the Court, that decision should have been left to an arbitrator.[2]

The Court's per curiam opinion in *Nitro-Lift Technologies L.L.C. v. Howard* stresses the primacy of the Federal Arbitration Act ("FAA"), including the FAA's policy favoring arbitration, over state law.[3] The dispute in *Nitro-Lift* concerned an employment agreement under which two employees worked for Nitro-Lift on oil wells in Oklahoma, Texas and Arkansas. The employment agreements included confidentiality and noncompetition provisions and an arbitration clause calling for arbitration in Houston, Texas under AAA rules.[4] When the two employees left Nitro-Lift and began working for a competitor, Nitro-Lift served the employees with a demand for arbitration.[5]

The employees filed suit in Oklahoma state court and asked the court to declare the noncompetition agreements null and void pursuant to an Oklahoma statute. The lower Oklahoma Court dismissed the complaint, finding that the contracts contained valid arbitration clauses under which an arbitrator, and not the court, should decide the validity of the noncompetition agreements.[6]

The Oklahoma Supreme Court, on the employees' appeal issued an order to show cause why the matter should not be resolved by the application of Okla. Stat. Tit. 15 §219A, which limits the enforceability of noncompetition agreements in Oklahoma.[7] Nitro-Lift argued that under Supreme Court precedent interpreting the FAA, the decision on whether the noncompetition clauses were valid was for the arbitrator and not the court.[8] The Oklahoma Supreme Court found the noncompetition clauses invalid as against public policy, holding that the "existence of an arbitration agreement in an employment contract does not prohibit judicial review of the underlying agreement."[9]

The United States Supreme Court reversed, holding precisely to the contrary, "when parties commit to arbitrate contractual disputes, it is a mainstay of the [FAA]'s substantive law that attacks on the validity of the contract, as distinct from attacks on the validity of the arbitration clause itself, are to be resolved by the arbitrator in the first instance, not by a federal or state court."[10] Moreover, the Court held that the Oklahoma courts did not have an adequate and independent state ground to review the validity of the contract because to do so would be in conflict with the federal law construing the FAA.[11]

In *Nitro-Lift*, the Supreme Court issued a clear statement that state courts, regardless of the public policy involved, are not to usurp the arbitrator's role to interpret the validity of contracts put into arbitration pursuant to a valid arbitration clause.

B. *Oxford Health Plans LLC v. Sutter*[12]

The Supreme Court further explored judicial deference to arbitral authority in its unanimous decision in *Oxford Health Plans v. Sutter.*[13] *Oxford Health Plans* was a challenge to an arbitrator's finding that a contract provided for class arbitration under FAA Section 10(a)(4) on the ground that the arbitrator had exceeded his powers.[14] The Court held that it must defer to the arbitrator's decision on the class arbitration decision, whether right or wrong, because the parties duly submitted the question to the arbitrator and the arbitrator decided the issue as a matter of contract interpretation.[15]

Sutter, a doctor who had contracted with Oxford to provide medical services to members of Oxford's insurance network, filed suit against Oxford in New Jersey Superior Court on behalf of himself and a putative class of other New Jersey physicians alleging that Oxford had not fully paid the doctors for their services.[16] Oxford moved to compel arbitration pursuant to an arbitration clause in the agreement between Oxford and Sutter and the New Jersey court granted the motion, referring the matter to arbitration.[17]

In the arbitration, "the parties agreed that the arbitrator should decide whether their contract authorized class arbitrations, and he determined that it did."[18] The arbitrator based his finding on language in the arbitration clause stating that "[n]o civil action concerning any dispute arising under this Agreement shall be instituted before any

court, and all such disputes shall be submitted to final and binding arbitration.…"[19] The arbitrator reasoned based on this language that the intent of the clause was to vest in the arbitration process everything that is prohibited from the court process and that a class action is one such prohibited civil action and is therefore encompassed by the arbitration agreement.[20]

Oxford then filed a motion in federal court to vacate the arbitrator's decision on the ground that he had exceeded his powers under Section 10(a)(4) of the FAA.[21] The district court denied Oxford's motion and the Third Circuit affirmed the denial.[22] As the arbitration continued, the Supreme Court issued its opinion in *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp*,[23] holding 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.[24]

Oxford asked the arbitrator to reconsider his decision on class arbitration based on *Stolt-Nielsen* and the arbitrator found that *Stolt-Nielsen* had no effect on the arbitration because the agreement authorized class arbitration.[25] Oxford again moved in federal court to vacate the arbitrators decision under FAA Section 10(a)(4).[26] The district court again denied Oxford's motion and the Third Circuit again affirmed.[27]

The Supreme Court granted certiorari to address the issue of whether FAA Section 10(a)(4) allows a court to vacate an arbitral award in similar circumstances and held it does not.[28] The Court emphasized that to obtain relief under FAA Section 10(a)(4) on the ground that an arbitrator exceeded his powers the challenger bears a heavy burden and an arbitral decision even arguably construing or applying the contract must stand, "regardless of a court's view of its (de)merits."[29] Thus, the Court concluded that the sole question before it was whether the arbitrator (even arguably) interpreted the parties' contract, and not whether he got its meaning right or wrong."[30] As the arbitrator's decisions were "through and through" interpretations of the parties agreement, the Court held that the arbitrator did not exceed his powers.[31]

The Supreme Court rejected Oxford's argument that *Stolt-Nielsen* authorizes a court to vacate an award where an arbitrator imposes class arbitration without a valid contractual basis.[32] The Court found this to be a misreading of *Stolt-Nielsen*, which had overturned an arbitral decision on the ground that it lacked any basis in the contract and not on the ground that it lacked a "sufficient" one.[33] The Court pointed out that in *Stolt-Nielsen*, the parties had entered what the Court describes as "an unusual stipulation" that they had never reached an agreement on class arbitration, which left the arbitral tribunal no room for an inquiry regarding the parties' intent.[34]

A footnote in the *Oxford Health Plans* decision provides what is likely to be a road-map for the next challenge to class arbitration. The Court pointed out that it would face a different issue had Oxford argued that the availability of class arbitration was a matter of arbitrability—which is presumptively for the courts to decide.[35] According to the Court, *Stolt-Nielsen* made clear that the Court has not yet decided whether the availability of class arbitration is a question of arbitrability but that Oxford precluded consideration of that question when it agreed that the arbitrator should decide the question.[36]

C. *American Express Company v. Italian Colors Restaurant*[37]

The Supreme Court again addressed the intersection of arbitration with class actions in *American Express Co. v. Italian Colors Restaurant,* although with considerably less unanimity.[38] Justice Scalia's opinion for the Court found that a contractual waiver of class arbitration is enforceable even where the plaintiff's cost of individually arbitrating a federal statutory claim demonstrably exceeds the potential recovery on the arbitrated claim.[39]

American Express has a protracted procedural history. The case arose as a dispute between merchants who accept American Express charge cards and American Express.[40] The merchants filed a class action for violation of the antitrust laws on the ground that American Express had allegedly used its monopoly power in the market for charge cards to force merchants to accept credit cards at a rate 30% higher than the rate charged for competing credit cards.[41]

American Express moved to compel individual arbitration based upon its agreement with the merchants that provided for arbitration of all disputes between the parties and also provided that "there shall be no right or authority for any Claims to be arbitrated on a class action basis."[42] The merchants submitted a declaration from an economist who estimated that the cost of the expert analysis necessary to determine the antitrust claims would be several hundred thousand to more than one million dollars, while the maximum recovery for the individual plaintiff would be $12,850 or $38,549 if trebled.[43] The district court granted American Express's motion and dismissed the action, but the Second Circuit reversed and remanded because the merchants had established that they would incur prohibitive costs if compelled to arbitrate under the class action waiver, making the waiver unenforceable.[44]

The Supreme Court then granted certiorari, vacated the Second Circuit's judgment and remanded for further consideration in light of *Stolt-Nielsen.*[45] The Second Circuit stood by its original ruling on the ground that its earlier ruling did not compel class arbitration.[46] The Second Circuit then *sua sponte* reconsidered its second opinion in

light of *AT&T Mobility v. Concepcion*,[47] which held that the FAA preempted a state law barring enforcement of a class action waiver, but again reaffirmed its original ruling as there was no issue of preemption.[48] The Supreme Court again granted certiorari and reversed the Second Circuit.

The Supreme Court began its opinion by emphasizing that, under the FAA, courts rigorously enforce arbitration agreements according to their terms including terms that specify with whom parties will arbitrate their disputes and the rules under which the arbitration will be conducted.[49] The Court rejected the merchants' argument that, by requiring arbitration and excluding class arbitration in its adhesion agreement, American Express was, in effect, using its monopoly power to avoid liability under the antitrust laws because no individual merchant would be able to afford to arbitrate the issue.[50]

The Court first argued that nothing in the antitrust laws themselves require the availability of class action procedures.[51] The Court pointed out that Rule 23 of the Federal Rules of Civil Procedure (authorizing class actions) post-dates the enaction of the Sherman and Clayton Acts and argued that, therefore, the availability of class actions cannot be a requirement of those laws.[52] The Court also reasoned that Rule 23 itself does not establish an entitlement to vindicate federal statutory rights, but rather only an opportunity to do so if all the procedural predicates are met.[53]

The Court's opinion then goes on to reject the merchants' argument that American Express's ban on class arbitration should be invalidated because it prevents the effective vindication of a federal statutory right.[54] This argument is based on the Supreme Court's opinion in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,[55] in which the Court approved arbitration of a federal statutory claim "so long as the prospective litigant effectively may vindicate its statutory cause of action in the arbitral forum."[56] The *American Express* Court, while acknowledging that subsequent Supreme Court cases have recognized an effective vindication exception, took the position that the discussion of effective vindication in *Mitsubishi Motors* was dictum.[57]

Although the majority opinion called the effective vindication exception dictum, it did not eliminate it entirely—rather the Court stated that the exception applies where arbitration might prevent "prospective waiver of a party's *right to pursue* statutory remedies."[58] This the court differentiated from whether it is worth the expense to *prove* the statutory remedy.[59] Thus, the Court reasons, the remedy can still be pursued on an individual basis just as antitrust remedies could be pursued before Rule 23 was enacted.[60]

The majority ends its opinion by rejecting the characterization of *AT&T Mobility v. Concepcion*,[61] which invalidated a California law on the ground that it was preempted by the FAA, as limited to preemption. In a footnote, the Court characterizes *AT&T Mobility* expansively, stating that it established "that the FAA's command to enforce arbitration agreements trumps any interest in ensuring the prosecution of low value claims."[62]

Justice Kagan's dissent, joined by Justices Ginsburg and Breyer, not surprisingly, disagrees with the majority opinion's application of the effective vindication exception, stating that "as applied here, the [effective vindication] rule would ensure that Amex's arbitration clause does not foreclose Italian Colors from vindicating its right to redress antitrust harm."[63] In the dissent's view, if it is not permissible to obtain absolution from antitrust liability through a direct exculpatory clause, it should not be permissible to achieve the same result through the erection of procedural hurdles.[64]

Perhaps the most provocative and interesting argument raised by the *American Express* dissent is that to allow arbitration clauses that effectively strip parties of the economic incentive to enforce their federal statutory rights *frustrates*, rather than advances, the goals of the FAA.[65] This is because the FAA promotes arbitration, but arbitration clauses such as the one at issue in *American Express*, which limit claimants to individual actions but contain no procedural safeguards to ensure such actions can be economically brought, result in no arbitrations being initiated.[66] Such clauses, according to the dissent, act not as arbitration clauses, but rather as *de facto* waivers of liability for the clause-drafter.[67]

Justice Kagan's point is an important one. If the FAA begins to be perceived as a tool to limit substantive rights, legislative efforts to remedy that situation could create problems for commercial and international arbitration. It remains to be seen whether the Court's aggressive approach to enforcing class action waivers will lead to such legislative action.[68]

D. The Upcoming Term

The upcoming Supreme Court term, to commence in October 2013, already promises to be an interesting one. The Court has granted certiorari in *BG Group PLC v. Republic of Argentina,* an investment treaty arbitration matter.[69] The question presented, not explicitly limited in scope to investment arbitration, is "[i]n disputes involving a multi-staged dispute resolution process, does a court or instead the arbitrator determine whether a precondition to arbitrate has been satisfied."[70] This case, for obvious reasons, has been the subject of great interest in the arbitration community and the Court has granted permission to the American Arbitration Association and the United States Counsel for International Business (the U.S. arm of the ICC) to submit briefs as *amici curiae.*[71]

Endnotes

1. 133 S. Ct. 500 (2012).
2. 133 S. Ct. at 501.
3. *Id.*
4. 133 S. Ct. at 501-502.
5. 133 S. Ct. at 502.
6. *Id.*
7. *Id.*
8. *Id.*
9. *Id.*
10. 133 S. Ct. at 503.
11. 133 S. Ct. at 502-503.
12. 133 S. Ct. 2064 (2012).
13. Justice Kagan delivered the opinion of the Court and Justice Alito filed a concurring opinion in which Justice Thomas joined.
14. 13 S. Ct. at 2066.
15. 13 S. Ct. at 2071.
16. 13 S. Ct. at 2067.
17. *Id*.
18. *Id.*
19. *Id.*
20. *Id*.
21. *Id*.
22. *Id.*
23. 559 U.S. 662, 130 S. Ct. 1758 (2010).
24. *Id*., *quoting Stolt-Nielsen*, 559 U.S. at 684.
25. 13 S. Ct. at 2067.
26. 13 S. Ct. at 2068.
27. *Id.*
28. *Id*.
29. *Id*.
30. *Id*.
31. 13 S. Ct. at 2069.
32. *Id*.
33. *Id.*
34. *Id*. It remains unclear why the *Stolt-Nielsen* parties' later agreement to submit the class arbitration issue to the arbitrators did not confer upon them the specific authority to decide the class arbitration issue.
35. 13 S. Ct. at 2068, n. 2.
36. *Id.* Justice Alito's concurrence, joined by Justice Thomas, echoes this point and goes on to say that because the absent class members, unlike Oxford, did not consent to determination by the arbitrator, difficult procedural issues arise with respect to the conduct of class arbitrations.
37. 133 S. Ct. 2304 (2013).
38. 133 S. Ct. at 2307. Justice Scalia delivered the opinion of the Court joined by Chief Justice Roberts and Justices Kennedy, Thomas and Alito. Justice Thomas filed a concurring opinion. Justice Kagan filed a dissenting opinion joined by Justices Ginsburg and Breyer. Justice Sotomayor did not take part in consideration of the case.
39. 133 S. Ct. at 2307.
40. 133 S. Ct. at 2308.
41. *Id*.
42. *Id*.
43. *Id*.
44. *Id.*
45. *Id*.
46. *Id.*, *citing In re American Express Merchants' Litigation*, 634 F.3d 187 (2d Cir. 2011).
47. 131 S. Ct. 1740 (2011).
48. *Id.*, *citing In re American Express Merchants' Litigation*, 681 F.3d 139 (2d Cir. 2012).
49. 133 S. Ct. at 2309.
50. *Id*.
51. *Id*.
52. *Id.*
53. *Id*.
54. *Id*.
55. 473 U.S. 614, 637 n. 19.
56. 113 S. Ct. at 2310.
57. 133 S. Ct. at 2310 and n. 2. Justice Kagan's dissent calls this reduction to dictum of *Mitsubishi's* effective vindication exception "dead wrong." 113 S. Ct. at 2317, n. 3.
58. 113 S. Ct. at 2310 (emphasis in the original).
59. 113 S. Ct. at 2310.
60. 113 S. Ct. at 2311.
61. 131 S. Ct. 1740.
62. 113 S. Ct. at 2312, n. 5. Justice Thomas follows the majority opinion with a concurrence in which he states that because the merchants had not furnished grounds for the revocation of any contract, but instead argued only that to proceed would be economically infeasible, the arbitration clause must be upheld under the FAA. 2013 113 S. Ct. at 2312-13.
63. 113 S. Ct. at 2313.
64. 113 S. Ct. at 2313-14.
65. 113 S. Ct. at 2315.
66. *Id.*
67. *Id.*
68. The possibility of legislative action is not purely speculative. The latest iteration of the Arbitration Fairness Act, HR 1844 and S. 878 introduced on May 7, 2013, would if enacted invalidate any predispute arbitration agreement if it requires arbitration of an employment dispute, consumer dispute, antitrust dispute, or civil rights dispute.
69. 2013 U.S. LEXIS 4532.
70. 2012 U.S. S. Ct. Briefs LEXIS 3231.
71. 2013 U.S. LEXIS 4532.

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