New York Law Journal

SERVING THE BENCH AND BAR SINCE 1888

WWW.NYLJ.COM

An ALM Publication

VOLUME 243—NO. 94

TUESDAY, MAY 18, 2010

Outside Counsel

Expert Analysis

Supreme Court: No Class Arbitration Where Agreement Is Silent

By **Samuel Estreicher**

And **Elena J. Voss**

On April 27, 2010, in *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*,[1] the U.S. Supreme Court held that where an arbitration agreement is "silent" on whether the parties have authorized classwide arbitration, neither the arbitrator nor the court may require that the action proceed on a class basis. The arbitration panel below exceeded its authority in violation of the Federal Arbitration Act (FAA)[2] when it found that the agreement permitted class arbitration. The decision essentially reverses the presumption that many thought the Court previously had endorsed in *Green Tree Financial Corp. v. Bazzle*,[3] that silence in an arbitration agreement allows the arbitrator to find authority to proceed on a class basis.

The underlying dispute in *Stolt-Nielsen* involved antitrust price-fixing claims by AnimalFeeds, an animal feed supplier, against several maritime shipping companies with whom it contracted to ship materials. AnimalFeeds sought to represent a class of customers of the shippers, initially in court and later in arbitration, after the court claims were dismissed pursuant to an arbitration clause in the standard shipping agreement.

The parties agreed to submit the issue of whether the agreement permitted class arbitration to a panel of arbitrators. The parties stipulated that the agreement was "silent" on the issue of class arbitration. The arbitration panel issued a "Partial Final Clause Construction Award" ruling that the arbitration agreement permitted class proceedings. It agreed to stay the arbitration, however, pending judicial review of the clause-construction award.

The shipping companies then filed an application in the District Court for the Southern District of New York to vacate the award under the FAA §10. The trial court vacated the award, finding that award was in "manifest disregard" of the law because the panel did not conduct a choice-of-law analysis, which would have required application of maritime law, and which, in turn, would have required interpretation of the agreement in light of custom and usage.[4] The U.S. Court of Appeals for the Second Circuit reversed.[5]

The appellate court first explained that the "manifest disregard" standard remained viable even after the Supreme Court's decision in *Hall Street Assoc. v. Mattel Inc.*[6] that the FAA did not authorize grounds for judicial review other than those enumerated in §10. The "manifest disregard" standard, the court explained, was a "judicial gloss" on the enumerated grounds. The appeals court then upheld the award because no authority had been offered by the shipping companies of a maritime law rule or New York rule against class arbitration.

> Class arbitration 'changes the nature of arbitration to such a degree' that consent to class arbitration cannot be presumed.

Evidence of Consent

The Supreme Court granted certiorari on the issue of whether the FAA permits class arbitration where the agreement is silent on the issue. The Court reversed (5-3), holding that the arbitration panel exceeded its authority under the FAA when it ruled that the agreement permitted class arbitration. Justice Samuel Alito, writing for the majority, found that the arbitrators had acted according to their own sense of public policy, rather than the scope of the authority provided by the agreement.

Because the parties stipulated that the agreement was "silent" and there had been "no agreement" on class arbitration, the Court reasoned, there was no need to ascertain the parties' intent on the subject. Instead, the arbitrators' proper task was to determine whether, in the face of that silence, class arbitration was permitted by an underlying default rule of law—be it maritime law, New York law, or the FAA.

The Court rejected the arbitrators' view that its prior decision in *Bazzle* "controlled" the issue of authority to proceed on a class basis. *Bazzle*, we are told, involved three separate questions: (1) "which decision maker (court or arbitrator) should decide whether the contracts in question were 'silent' on the issue of class arbitration"; (2) what is the appropriate standard in deciding whether the contract allows class arbitration; and (3) was class arbitration properly ordered in the case at hand. The plurality opinion decided only the first question—that this was the arbitrator's province.

However, Justice John Paul Stevens' concurrence in the judgment "did not endorse the plurality rationale;" rather, "his analysis bypassed the first question…and rested instead on the resolution of the second and third questions. Thus, *Bazzle* did not yield a majority decision on any of the three questions."

In the instant case, *Bazzle*'s first question did not have to be reached because the parties' supplemental agreement had assigned the "who decides" question to the arbitration panel. The second question—the standard for determining whether class proceedings are permitted under a "silent" agreement—did have to be decided.

SAMUEL ESTREICHER *is the Dwight D. Opperman Professor at New York University School of Law and counsel to Jones Day.* ELENA J. VOSS *is an associate in the labor and employment group at Jones Day.*

Although state law ordinarily would govern the interpretation of an arbitration agreement, "the FAA imposes certain rules of fundamental importance, including the basic precept that arbitration is a matter of consent, not coercion,"—requiring, in effect, resort to an FAA-based default rule.

The Court then considered the appropriate default rule under the FAA. Arbitration, the Court explained, has always been considered a matter of consent. Class arbitration "changes the nature of arbitration to such a degree" that consent to class arbitration cannot be presumed. Commonly touted benefits of arbitration such as speed, cost savings, efficiency, and privacy may be lost in a class setting, and new concerns added related to the greater potential for a multiplicity of claims, absent parties, and high stakes.

Thus, the Court ruled, "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." Because the parties here conceded that there was no such agreement, there could be no class arbitration.

The Court remanded the case, but ruled that rehearing by the arbitration panel on the class issue was not warranted, given the parties stipulation on "silence."

Dissent: Issue Not Ripe

Justice Ruth Bader Ginsburg dissented, joined by Justices Stevens and Stephen Breyer.[7] Justice Ginsburg believed that certiorari had been granted improvidently, because the issue was not ripe for adjudication. The panel's clause construction award was a preliminary ruling, determining only arbitration was permitted by the agreement, but not reaching the issue of whether it was appropriate to certify a class or on what terms a class should be certified. Justice Ginsburg opined that majority ruling ran contrary to the traditional "final judgment" principle for appellate review, and the panel's ruling was not the type of "partial award" meant to be subject to judicial review under the FAA.

On the merits, Justice Ginsburg disagreed with the majority that the arbitration panel exceeded its authority. Justice Ginsburg noted that the parties had agreed to submit to the panel the issue of whether the agreement authorized arbitration, and thus the panel acted within its conferred authority in issuing its award. Justice Ginsburg also disagreed with the majority's characterization of the basis for the panel's award as resting on policy, and questioned whether AnimalFeeds really had conceded that there was "no agreement" on class arbitration. Finally, Justice Ginsburg disagreed with the Court's decision not to remand the issue to the arbitration panel to clarify the basis for its award.

Unanswered Questions

Stolt-Nielsen leaves open a number of important issues. First, the Court did not resolve the question raised in *Bazzle* of whether the court or the arbitrator should decide, in the first instance, whether the agreement permits class arbitration. The Court maintains that *Bazzle* represents no more than a four-justice plurality opinion on the allocation of the "who decides" issue to the arbitrator; Justice Stevens, who concurred in order to create a clear judgment, "did not take a definitive position" on that question.

The Court in the instant case found no need to take up the issue, because the parties had agreed, in a supplemental undertaking, to submit the question to the arbitrators. Even though the "who decides" issue is formally open, the majority's FAA-based default rule suggests that leading arbitration services organizations like the AAA and JAMS may wish to review their class arbitration rules to see if arbitral authority is improperly presumed or directed.

> The arbitrators' proper task was to determine whether, in the face of that silence, class arbitration was permitted by an underlying default rule of law—be it maritime law, New York law, or the FAA.

The Court also explicitly left open the issue of the continued viability of the "manifest disregard of the law" ground for vacatur of an arbitration award. Some courts have suggested that this doctrine may not have survived the Supreme Court's decision *Hall Street Associates*,[8] which held that the parties could not expand on the grounds for judicial review of an arbitration award contained in the FAA. The Second Circuit in *Stolt-Nielsen* ruled that the manifest disregard standard remains viable as a "judicial gloss" on the grounds enumerated in the FAA, but the Supreme Court found that it need not reach the issue because the instant case could be resolved under the express "exceeded their powers" ground in FAA §10.

Companies utilizing arbitration agreements will need to reevaluate whether an express class action waiver clause is necessary or useful after *Stolt-Nielsen*. Some prior court decisions like *In re American Express Merchants' Litigation and Discover Bank v. Superior Court*[9] have ruled, at least in the consumer credit card context, that certain contractual class waiver provisions are unconscionable under state law. It is unclear whether unconscionability analysis under state law would be applied in the same way even in the absence of an express class action waiver provision because the agreement itself might effect such a waiver. Justice Ginsburg in her dissent suggested that a different default rule—one more receptive to class arbitration than the majority's—might be applied with respect to "take-it-or-leave-it" contracts of adhesion.

The majority's rejection of the lack of ripeness consideration might also open the door to increased review of preliminary awards issued by arbitrators—not only so-called "clause construction awards" construing agreements to permit or prohibit class arbitration, but also a variety of other types of initial rulings. The decision also raises the question of whether a party's failure to seek review of an early award by an arbitrator waives its right to challenge that ruling at a later stage.

The outcome in *Stolt-Nielsen* results from the relatively unusual circumstance of the parties agreeing that there was "no agreement" on the issue of class arbitration. As the majority recognized, its decision leaves for future development by lower courts and/or arbitrators what types of contract language can be construed as evincing an intent to permit class arbitration.

It also remains to be seen whether such decisions, when reached by arbitrators, will receive heightened review by courts to determine whether the agreement is silent versus ambiguous, or whether they will be subject to the traditional minimal level of review accorded arbitration awards that construe contract language. Pending additional development in the case law, contract drafters should remain cautious in deciding between express class waivers and remaining "silent," and particularly in assuming that their agreement truly is "silent" on class arbitration.

1. No. 08-1198, 559 U.S.__ (2010).

2. 9 U.S.C. §1 et seq.

3. 539 U.S. 444 (2003).

4. 435 F.Supp.2d 382, 385-86 (SDNY 2006).

5. 548 F.3d 85 (2d Cir. 2008).

6. 552 U.S. 576 (2008).

7. Justice Sonia Sotomayor did not participate in the decision.

8. *Hall Street Associates, L.L.C. v. Mattel Inc.*, 552 U.S. 576 (2008). See, e.g., *Citigroup Global Mkts. Inc. v. Bacon*, 562 F.3d 349, 358 (5th Cir. 2009); *Ramos-Santiago v. United Parcel Service*, 524 F.3d 120, 124 n.3 (1st Cir. 2008) (dicta).

9. *In re American Express Merchants' Litigation*, 554 F.3d 300 (2d Cir. 2009); *Discover Bank v. Superior Court*, 36 Cal. 4th 148 (2005).