
# Class Arbitration – Can It Even Work?

**By Jay Bogan***

Courts continue to devote a lot of attention to class arbitration. The U.S. Supreme Court has a case on its docket, the Eleventh Circuit just decided an issue of first impression, and another important case is teed up before the Second Circuit.

But the most important question underlying all of this jurisprudential activity remains: Can class arbitration even work?

Think about your typical consumer fraud class action. The class representative files the class action in a trial court, such as an Article III federal district court, where it will be governed by rules of procedure constituting, essentially, legislative enactment, often Federal Rule of Civil Procedure 23. Most of these cases seek damages, such as under Federal Rule 23(b)(3), with the result that all class members receive notice and an opportunity to opt out if the court grants certification or approves a class settlement. In other words, your typical class action (as opposed to a collective action under the federal Fair Labor Standards Act) will not be structured as an ***opt-in*** class. If the class member receives notice and fails to opt out, the class member ultimately will be bound by the judgment entered by the trial court, whether favorable or unfavorable to the class.

How do you bind absent class members through an arbitration process, where the arbitrator's power derives solely from the parties' private contractual framework, and without the recognized authority of a court acting pursuant to procedural rules that have the force of law?

Justice Alito raised the issue of whether a class arbitration can effectively bind absent class members in his concurring opinion in *Oxford Health Plans LLC v. Sutter*, 569 U.S. 564, 573 (2013) (Alito, J., concurring), and the issue has been ruled on by the Southern District of New York in a case now pending on appeal before the Second Circuit.

In his concurrence, Justice Alito reasoned that where an arbitration agreement does not explicitly authorize class arbitration, the distribution of opt-out notices to the putative members of an arbitration class would not be sufficient to bind them to a class arbitration award. *Sutter*, 569 U.S. at 574. "'[A]rbitration is simply a matter of contract between the parties,' and an offeree's silence does not normally modify the terms of a contract." *Id.* (quoting *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995), and citing 1 *Restatement (Second) of Contracts* § 69(1) (1979)). According to Justice Alito, "at least where absent class members have not been required to opt *in*, it is difficult to see how an arbitrator's decision to conduct class proceedings could bind absent class members who have not authorized the arbitrator to decide on a classwide basis which arbitration procedures are to be used." *Id.* (emphasis in original).

In the recent Southern District of New York case, Judge Jed Rakoff held the arbitrator could *not* bind absent class members to class procedures under an arbitration agreement that did not explicitly authorize class arbitration, even if the named parties had agreed to submit the class issue to the arbitrator. *Jock*

*v. Sterling Jewelers Inc.*, 284 F. Supp. 3d 566 (S.D.N.Y. 2018), *appeal filed*, No. 18-153 (2d Cir. Jan. 18, 2018). According to Judge Rakoff, who relied in important respects on Justice Alito's concurrence in *Sutter*, only the named parties to the arbitration proceeding and specific class members who agreed to *opt in* could be bound by the arbitrator's decision. And he recognized that the question of whether absent class members could be bound where the parties' arbitration agreement explicitly authorized class arbitration remained unresolved. *Id*. at 570 n.2 (stating that he "need not reach the question of whether, had the RESOLVE agreement, in fact, permitted class procedures, the Arbitrator would have had the authority to bind absent class members based on the fact that each absent class member agreed to such procedures by virtue of having signed the agreement").

As class action waivers continue to proliferate in consumer and employment contracts, the question of whether class members can be bound where an arbitration agreement expressly authorized class arbitration may never be answered. But even assuming every member of a putative class had agreed to a clause authorizing class arbitration, an absent class member might still later object to a class arbitration award, arguing, for example, that he or she did not have an opportunity to select the arbitrator, an opportunity always afforded under arbitration agreements and rules.

The Supreme Court recently heard a class arbitration case out of the Ninth Circuit. In that case, a 2-1 Ninth Circuit panel affirmed the district court's ruling that class arbitration claims could proceed, because ambiguous language in the contract regarding class arbitration had to be construed against the drafter of the contract under the state law contractual interpretation doctrine of *contra proferentem*. *See Varela v. Lamps Plus, Inc.*, 701 F. App'x 670, 672-73 (9th Cir. 2017), *cert. granted*, 138 S.Ct. 1697 (U.S. 2018). If the Supreme Court will address the deeper question of whether opt-out class arbitration can ever work – or address only whether the Ninth Circuit's ruling can be squared with *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010) – remains to be seen.

In *JPay, Inc. v. Kobel*, 904 F.3d 923 (11th Cir. 2018), a 2-1 Eleventh Circuit panel decided, as matter of first impression, that the availability of class arbitration constitutes a substantive, gateway question of arbitrability that is presumptively for a court (rather than an arbitrator) to decide. But the Eleventh Circuit went on to hold that the parties had "clearly and unmistakably" assigned that question to a private arbitrator in their arbitration agreement (*i.e.*, the parties' contractual language overcame the presumption). The arbitration agreement in *JPay* said nothing specifically about class arbitration, prompting a strong dissent to the majority's interpretation of the contract. And the dissent noted the Supreme Court soon will be addressing the contractual interpretation issue in *Lamps Plus, Inc. v. Varela*, 138 S.Ct. 1697 (U.S. 2018) (cert. granted).

As the dissent in *JPay* notes, a Supreme Court ruling in *Lamps Plus* that the Federal Arbitration Act displaces contractual interpretation rules such as *contra proferentem* likely would require vacatur of the *JPay* majority's ruling. But the Supreme Court (or one or more concurring justices) may take the occasion to address the deeper question of whether a class arbitration can ever work. If an arbitrator could never bind absent class members to an "opt out" class arbitration award, questions about whether an ambiguous arbitration agreement assigns the class arbitration issue to the arbitrator in the first instance would become purely academic. And even if *Lamps Plus* does not provide the vehicle to address this question of arbitrator power, the Second Circuit's forthcoming decision in *Jock v. Sterling Jewelers* may constitute the first federal appellate court decision to address the issue directly.

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# Class Arbitration – Can It Even Work?
# Update

**Shortly after oral arguments were heard in *Lamps Plus*, discussed above, the author composed the following blog post.**

As I explored in the above article ("*Class Arbitration – Can it Even Work?*"), conducting a class arbitration like most class actions – that is, giving absent class members notice and an opportunity to opt-out – may not be sufficient to bind absent class members to a class arbitration award. This problem arises from the purely contractual nature of arbitration and the fact the arbitrator does not have the authority of a court to enforce procedural rules that have the force of law.

The U.S. Supreme Court recently explored this threshold question of viability during oral argument in *Lamps Plus, Inc. v. Varela*, No. 17-988 (U.S. argued Oct. 29, 2018). As noted above, in *Lamps Plus*, a 2-1 Ninth Circuit panel affirmed the district court's ruling allowing class arbitration claims to proceed, agreeing with the lower court that ambiguous language in the contract regarding class arbitration had to be construed against the drafter of the contract under the state law contractual interpretation doctrine of *contra proferentem*. In a two-sentence dissenting opinion, Judge Fernandez concluded that the arbitration agreement – which did not expressly refer to class arbitration – was "not ambiguous" and "[w]e should not allow Varela to enlist us in this palpable evasion of *Stolt-Nielsen*."

Judge Fernandez's dissent focused on *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010). In *Stolt-Nielsen*, the Supreme Court held that, because of the vast differences between bilateral and class arbitration, a party's consent to class arbitration cannot be inferred solely from the fact that the party agreed to arbitrate in the first place. In Judge Fernandez's view, inferring consent to class arbitration based on *contra proferentem* could not be reconciled with *Stolt-Nielsen*.

During oral argument before the Supreme Court, questions from several Justices indicated interest in the deeper question of viability of any opt-out class arbitration, as opposed to addressing only the *Stolt-Nielsen* issue. Several of these questions reflected the concerns articulated by Justice Alito in 2013, when he raised the issue of whether a class arbitration can effectively bind absent class members in his concurring opinion in *Oxford Health Plans LLC v. Sutter*, 569 U.S. 564, 573 (2013) (Alito, J., concurring). During the *Lamps Plus* argument, Justice Gorsuch asked: "[W]hat do we do with the due process problem that Justice Alito pointed out in Oxford Health?" and "What do we do about those absent class members in opt-out class classes permitted by whatever arbitrable forum's rules prevail?" Transcript of Oral Argument, at 37-38. Justice Gorsuch then tied this "due process" issue to the issue of contractual interpretation: "[S]hould we ignore [the due process issues] in considering the impact here of the Arbitration Act and normal contract principles and whether normal contract principles would abide due process, for example?" *Id*. at 38.

Picking up on his own concurrence in *Oxford Health*, Justice Alito asked: "But do you think that … absent class members who didn't agree to arbitration could be bound by the decision of the arbitrator? … if [absent class members] have a legal claim, how can they be deprived of their legal claim pursuant to an arbitration award if they never agreed to arbitration? I thought arbitration was a matter of contract." *Id*. at 39-40.

Earlier comments by Justice Kavanaugh and Chief Justice Roberts indicate the Supreme Court might find a way to tie the due process issue to the contractual interpretation issue. According to Justice Kavanaugh, if "*Stolt-Nielsen* said that you needed something on the order of express language" to authorize class arbitration, then "the ship has sailed" on the contractual interpretation issue before the Court *Id*. at 20. Chief Justice Roberts, discussing the supposedly "neutral" contractual interpretation rule of *contra proferentem*, remarked: "[T]he question really is whether they're neutral principles. … the argument is that applying these principles has a peculiar impact on arbitration agreements since it authorizes a type of arbitration that is – is like a poison pill that basically [we] said in prior cases is fundamentally inconsistent

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with arbitration." *Id*. at 32-33. He later remarked: "So, if the [Federal Arbitration Act] says enforce the contract[] according to its terms, but one of the terms, as our prior precedents say, is fundamentally inconsistent with arbitration itself, then, presumably, the FAA would preclude that term." *Id*. at 35.

Based on these comments, it is possible the U.S. Supreme Court will require that an arbitration agreement contain (borrowing the words of Justice Kavanaugh) "express language" authorizing class arbitration, before a district court or arbitrator can rule that class arbitration may proceed. Otherwise, it cannot be presumed from an arbitration agreement that the parties agreed to a process with inherent due process problems and therefore dubious finality.

But the Court also could address the deeper issue, addressing an arbitrator's power to bind absent parties to any type of representative ruling. The Court could rule that the interpretation issue relates to the underlying contractual basis for arbitration and thus requires, as a matter of due process, a basis for finding express consent by the absent parties to having a single arbitrator or panel of arbitrators decide all of the class members' claims. In other words, unless every class member's arbitration agreement unambiguously authorized an arbitrator selected by a different class member to adjudicate the claims of absent class members, then the absent class members could not be said to have agreed to class arbitration (unless they separately "opted in" to the class arbitration). Such an arbitration agreement almost certainly does not exist.

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Ultimately, the *Stolt-Nielsen* issue may become purely academic, as more and more arbitration agreements will include an unambiguous class action waiver. In the meantime, it will be interesting to see if *Lamps Plus* merely extends the *Stolt-Nielsen* rule or takes on Justice Alito's threshold question of an arbitrator's power to bind absent class members.