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Stolt-Nielsen's Effect On Consolidation Of Arbitrations

Law360, New York (July 07, 2010) -- Courts and commentators agree that consolidation of arbitrations is an issue for arbitrators, not courts, to decide. But is that about to change? The U.S. Supreme Court's recent decision in Stolt-Nielsen SA v. Animalfeeds International Corp., 130 S. Ct. 1758 (2010), indicates that it might be.

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Although the Supreme Court did not directly address the court versus arbitrator issue, the holding — that consent to class treatment of claims cannot be presumed by the parties' agreement to arbitrate alone — and the reasoning behind it, suggest that courts, not arbitrators, should decide the issue of consolidation.

Stolt-Nielsen: the Supreme Court's Ruling

Stolt-Nielsen began as an antitrust lawsuit filed on behalf of a class of liquid chemical product manufacturers who purchased shipping services from Stolt-Nielsen. Following a series of orders by various courts, the case was referred to arbitration. Stolt-Nielsen objected to class action arbitration, arguing that the parties' arbitration agreement did not extend to class actions.

The parties agreed to submit the issue of whether the arbitration clause covered class claims to the arbitration panel. The arbitration panel ruled that the arbitration could proceed as a class action. The U.S. Court of Appeals for the Second Circuit upheld the arbitration panel. Stolt-Nielsen appealed and the Supreme Court agreed to hear the case.

On April 27, 2010, the Supreme Court reversed. The court held that the arbitration panel had no authority under the Federal Arbitration Act to order class action arbitration where the parties' agreement to arbitrate was silent as to arbitration on behalf of a class.

The court clarified that its 2003 decision in GreenTree Financial Corp. v. Bazzle was not dispositive on the authority of arbitrators to order class arbitration. In Bazzle, a plurality of the court had ruled that the issue of class arbitration, where not specifically provided for in the contract, should be decided by an arbitrator, not the court.

The court emphasized that “no single rationale commanded a majority in Bazzle” and that Bazzle therefore “did not establish the rule to be applied in deciding whether class arbitration is permitted.” Rather, the court stated, “[t]he decision in Bazzle left that question open, and we turn to it now.”

The court first noted that the “primary purpose of the FAA” is to ensure that “private agreements to arbitrate are enforced according to their terms.” The court went on to say, “it follows 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.”

The court found that the arbitration panel had not attempted to determine the parties’ intent: “Rather than inquiring whether the FAA, maritime law, or New York law contains a ‘default rule’ under which an arbitration clause is construed as allowing class arbitration in the absence of express consent, the panel proceeded as if it had the authority of a common law court to develop what it viewed as the best rule to be applied in such a situation.”

The court rejected the proposition that the parties’ agreement to submit class claims to arbitration is a “procedural question” that can be inferred from the mere existence of an agreement to arbitrate. The court stated that class arbitrations change the nature of arbitration “to such a degree” that the parties’ agreement to arbitrate class claims cannot be presumed from the mere fact that arbitration was agreed.

The court recognized that “procedural questions which grow out of the dispute and bear on its final disposition are presumptively not for the judge, but for an arbitrator to decide.” The court declined to state, however, whether the issue of the parties’ intent to arbitrate class claims was for the arbitrators or the courts to decide, because the parties in Stolt-Nielsen had agreed to submit that issue to the arbitration panel.

Does Stolt-Nielsen Put the Issue of Consolidation Back in the Courts?

Prior to 2002, courts, not arbitrators, routinely decided whether arbitrations could be consolidated. In 2002, the Supreme Court held in Howsam v. Dean Witter Reynolds Inc. that whether a claim was barred by a time limit for filing securities arbitrations was an issue for an arbitrator and not the court to decide. The court distinguished such “procedural questions,” which are implicit in an agreement to arbitrate and thus are for arbitrators to decide, from “questions of arbitrability,” which are for courts to decide.

After Howsam was decided in 2002, and Bazzle in 2003, the law changed. Relying on one or both of these decisions, all of the United States Circuit Courts of Appeal that subsequently considered the issue ruled that whether arbitrations should be consolidated was a matter for arbitrators, not courts, to decide.

Typical of these courts’ reasoning was the Third Circuit’s decision in Certain Underwriters at Lloyd’s London v. Westchester Fire Ins. Co. Referring the issue of consolidation, to arbitration, the court stated:

"Howsam and [Bazzle] together explain why no 'question of arbitrability,' as the Supreme Court has recently — and narrowly — defined that phrase, has been raised here. ... [F]ederal courts, 'upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue,' are authorized to 'make an order summarily directing the parties to proceed to arbitration in accordance with the terms thereof.'"

Following the court’s decision in Stolt-Nielsen, the Howsam/Bazzle rationale that has been the basis for deferring the issue of consolidation to arbitration appears to be in doubt. Not only did the court seem to undercut the precedential effect of Bazzle, it also held that consent to class action arbitration cannot be presumed from the parties' agreement to arbitrate, and thus cannot not be considered a mere "procedural question," per Howsam.

In considering whether class action arbitration is a "procedural question" that can be inferred from the agreement to arbitrate itself, the court, despite its statement that it was declining to "revisit" the court versus arbitrator issue, appears in effect to have decided that the issue is for the courts.

The procedural/substantive arbitrability distinction derives from Howsam, which as noted, has been the basis on which courts have referred the issues of class arbitration and consolidated arbitrations to an arbitrator for decision. Having found that class action arbitration is not the type of procedural question for which consent can be presumed from the fact that the parties agreed to arbitrate, it is difficult to see how it could be classified a matter for an arbitrator to decide under Howsam.

The same can be said of consolidated arbitration if, like class arbitrations, the parties' consent cannot be presumed from the agreement to arbitrate itself. Whether courts will apply the reasoning of Stolt-Nielsen to consolidation will likely depend on whether and to what extent the factors that the court relied on to reach its conclusion that consent to class arbitration could not be inferred from the agreement to arbitrate can be applied to the issue of consolidation.

The court noted four "fundamental changes brought about by the shift from 'bilateral' to class arbitration":

— An arbitrator chosen to resolve one dispute resolves many disputes involving hundreds, or perhaps thousands, of parties.

— Breaches of privacy and confidentiality, which are common features of bilateral arbitration.

— The arbitration binds the rights of parties who are not parties to the agreement.

— The commercial stakes are much higher.

The court concluded "that the differences between bilateral and class action arbitration are too great for arbitrators to presume, consistent with their limited powers under the FAA, that the parties' mere silence on the issue of class action arbitration constitutes consent to resolve their disputes in class proceedings."

These "fundamental changes" from bilateral arbitration to class arbitration are the likely battleground on which fight over consolidation will be fought. Parties seeking consolidation will claim that consolidation changes the arbitration process to a much lesser degree than does class action arbitration, and thus fall within the category of procedural issues for which consent can be presumed, even where the agreement is silent.

The argument that consolidation of arbitrations is distinct from class arbitrations and thus can still be characterized as procedural has some appeal, on the surface, at least. Unlike class arbitrations, consolidated arbitrations can be bilateral, involving the same parties. In such instances, there would be no breach of confidentiality and no involvement of third parties.

Consolidated arbitrations also involve far fewer than the hundreds or thousands of claims that the court noted could be involved in class arbitrations. Likewise, they would not involve absent parties and the financial stakes may not increase as much as in class arbitration.

On the other hand, consolidated arbitrations can be quite different from the typical bilateral arbitration. Consolidated arbitrations do not involve hundreds of disputes, but they do involve more than one. Consolidated arbitrations can involve third parties, thus raising the same breach of confidentiality concerns that are present in class arbitrations. The financial stakes can also increase greatly with consolidation. A single, bilateral arbitration

can involve tens or even hundreds of millions of dollars. Joining it with another large claim, or joining a large claim with a small claim, would likewise greatly increase the financial stakes.

The actual degree to which an agreement to arbitrate would be changed by consolidation would require factual findings and would have to be assessed on a case-by-case basis. The court in Stolt-Nielsen, however, did not find it necessary to inquire into the facts surrounding the proposed class action that was before the arbitration panel. The actual number of class members, whether the class members had agreed to arbitrate and if so, the terms on which they agreed to do so, the dollar amounts at stake, whether a bilateral arbitration between Stolt-Nielsen and AnimalFeeds would in fact be confidential — none of these factual matters was considered by the court. Rather, the court looked at potentials — what class action arbitration could entail — and on that basis, concluded that the parties' silence did not amount to consent to the fundamental changes that could be brought about by class arbitration.

The same reasoning can be applied to the consolidation of arbitration. Consolidating arbitrations could fundamentally change the parties' bilateral agreement by bringing in third parties, increasing the number of disputes, breaching confidentiality and significantly raising the financial stakes. It can be credibly argued, therefore, that these potential differences are likewise too great to presume the parties' consent to consolidation by their mere silence and thus do not fall within the category of "procedural questions" that are presumptively for an arbitrator to decide.

Conclusion

The Supreme Court's reasoning in Stolt-Nielsen supports the conclusion that the law on consolidation of arbitration has come full circle. Under the logic of Stolt-Nielsen, consolidation of arbitrations is not authorized in the absence of an agreement by the parties. Implicit in the court's reasoning is the conclusion that the issue of class action arbitration — and by extension, consolidated arbitration — is for a court, not an arbitrator, to decide.

A final conclusion, of course, will have to await further rulings on consolidation by lower courts and perhaps, by the Supreme Court itself. But there is good reason to believe that Stolt-Nielsen has indeed significantly changed the landscape on consolidation of arbitrations.

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