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When Would It Violate Public Policy to Require a Party to Arbitrate a RICO Claim?

by Jay E. Grenig

PREVIEW of *United States Supreme Court Cases*, pages 266–269. © 2003 American Bar Association.

Case at a Glance

This case presents the question of whether it would violate public policy to require a party to arbitrate a RICO claim under an arbitration agreement that arguably does not allow the arbitrators to grant all the remedies provided by RICO for such a claim.

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ISSUE

Does the Federal Arbitration Act require federal and state courts to enforce arbitration clauses that prohibit arbitrators from awarding full statutory remedies to plaintiffs?

FACTS

This case arises from a massive nationwide class action filed in August 2000 on behalf of more than 600,000 physicians against 10 of the largest managed care organizations (MCOs) in the United States. The physicians provided treatment to individuals who receive health care under employee benefit plans insured or administered by the MCOs. Among other things, the physicians accused the MCOs of not properly paying claims they had submitted, in violation of the Racketeer Influenced and Corrupt Organizations Act (RICO) (18 U.S.C. § 1961 et seq.). Specifically, they alleged that the MCOs, on their own and as part of a conspiracy with every other defendant MCO, implemented a plan to “deny, delay, and diminish” the reimbursement

payments due the physicians. The complaint alleged, among other things, that the MCOs delayed payment on claims in order to obtain a “float” on the monies due.

The terms of the contracts were negotiated and varied from physician to physician and from physician group to physician group. The parties negotiated such terms as covered services, claim submission provisions, claim payment time-frame requirements, and fee schedules. The contracts at issue here contain arbitration clauses. Some of the arbitration clauses provided that “any disputes about their business relationship” must be resolved through arbitration. Others provided that all matters arising from the agreement must be arbitrated. Some limited the arbitrators’ authority by preventing the arbitrator from awarding extra contractual damages of any kind, including punitive or exemplary damages. Others only prohibited the arbitrator from

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FROM: THE ELEVENTH CIRCUIT

awarding punitive or exemplary damages.

In September 2000, some of the MCOs moved in district court to compel arbitration of the claims covered by contracts with arbitration clauses. The physicians opposed arbitration, contending that the limitations on punitive and extracontractual damages rendered those arbitration agreements unenforceable, because those provisions purportedly deprived them of the ability to obtain treble damages on their RICO claims.

Finding that the respondents were “sophisticated” commercial actors, the district court held that the agreements were generally enforceable. *In re Managed Care Litigation*, 132 F.Supp.2d 989 (S.D.Fla. 2000). See also *In re Managed Care Litigation*, 143 F.Supp.2d 1311, 1375 (S.D.Fla. 2001). However, the court refused to compel arbitration of the physicians’ RICO claims because the waiver of punitive damages would prevent the physicians from recovering treble damages for a RICO violation. The court then concluded that, even though the physicians had freely agreed to arbitrate all disputes, the physicians were not required to arbitrate their RICO claims because they could not obtain “meaningful relief in arbitration.” The Eleventh Circuit affirmed the district’s court’s ruling. *In re Humana Managed Care Litigation*, 285 F.3d 971 (11th Cir. 2002).

The Supreme Court thereafter granted the MCOs’ petition requesting review of the Eleventh Circuit’s decision.

CASE ANALYSIS

Congress enacted RICO as Title IX of the Organized Crime Control Act of 1970. The purpose of RICO is “to seek the eradication of organized

crime in the United States by strengthening the legal tools in the evidence-gathering process, by establishing new penal prohibitions, and by providing enhanced sanctions and new remedies to deal with the unlawful activities of those engaged in crime.” Pub.L. 91-452, 84 Stat. 922, 923.

Both criminal and civil actions may be based on RICO. A civil RICO action may be brought by a private plaintiff “injured in his business or property.” Civil remedies for a successful private RICO action include the recovery of treble damages, costs, and attorney fees. In *Humana, Inc. v. Forsyth*, 525 U.S. 299 (1999), the Supreme Court held that group health insurers could be sued under RICO.

Claims based on RICO statutory violations are generally arbitrable under broad arbitration clauses. *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987). According to the Supreme Court, the burden is on the party opposing arbitration to show the legislature clearly and unmistakably intended to exclude arbitration. However, courts will not enforce arbitration agreements when the agreement is unconscionable. *Doctor’s Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996).

The MCOs argue that arbitrators, not courts, should address the validity of arbitral limitations on remedies. They claim that Congress wanted arbitrators, not courts, to determine any issues beyond challenges to the making or scope of arbitration agreements. The physicians disagree, arguing that the court, not the arbitrator, must decide arbitrability, including the gateway question of whether a prospective litigant effectively may vindicate his federal statutory cause of action in the arbitral forum.

According to the physicians, the Supreme Court has repeatedly held that the question of arbitrability is an issue for judicial determination unless the parties clearly and unmistakably provide otherwise.

According to the MCOs, Congress did not intend to preclude arbitration of the statutory claims at issue. The MCOs assert that the physicians are inappropriately attempting to extend the Supreme Court’s categorical, statute-level review to specific arbitration procedures or remedies agreed to by the parties. The MCOs argue that permitting pre-arbitration court review of consensual partial restrictions on statutory remedies would dramatically alter the Supreme Court’s established motion-to-compel arbitration analysis and seriously weaken the Court’s long-standing support for arbitration under the Federal Arbitration Act.

The physicians disagree, contending that denying a litigant judicial consideration of the arbitrability of the litigant’s federal right until after arbitration on the merits would be both prejudicial and inefficient. They say that parties would be first subjected to arbitration and then to a judicial determination of the arbitrator’s decision. They assert that post-arbitration review would potentially be more intrusive and less deferential than an initial determination of arbitrability.

The MCOs contend that the damage-limitation provisions could not justify excusing the physicians from arbitrating their RICO claims. First, the MCOs contend that a limitation on punitive damages does not prevent an award of RICO treble damages. They assert that the RICO treble damage provision is not a punitive damages clause because punitive damages are damages independently awarded to punish a defen-

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dant for its conduct. It is the MCOs' position that treble damages are a statutorily created category of damages that serves disparate purposes and whose nature and practice differ significantly from punitive damages.

The physicians contend that an arbitration provision that excludes or severely limits substantive federal statutory rights or remedies is unenforceable. Because the arbitration agreements restrict the physicians' substantive rights and their ability to vindicate their RICO claims, the physicians say that the agreements are unenforceable.

Even if it is determined that the damage limitation provisions in the arbitration agreements must be interpreted by the court, the MCOs say that a limitation on punitive damages does not prevent an award of RICO treble damages. Should the Supreme Court determine that the damage limitation provisions in the arbitration agreements must be interpreted as a bar to RICO treble damages, the MCOs argue that the limitation was valid and enforceable and could not justify releasing the physicians from their obligation to arbitrate their disputes with the MCOs. As "sophisticated actors," the MCOs say, the physicians were free to contract and structure their arbitration agreements according to their business needs, including a mutual waiver of punitive damages.

The physicians respond that they cannot recover treble damages under United Healthcare's agreement limiting the arbitrator's ability to award extracontractual damages. Noting that treble damages have commonly been characterized as punitive or exemplary, they claim that they would be precluded by the prohibition of punitive or exemplary damages under the other arbitration agreements from recovering treble

damages. The physicians say that an arbitrator acting pursuant to these agreements would not have the authority to award treble damages, preventing the physicians from obtaining meaningful relief for their federal RICO claims in the arbitral forum.

Finally, the MCOs claim that, even if the damage limitation provisions are unenforceable, the physicians' RICO claims are still arbitrable. They assert that, if the district court believed that the damage limitation provisions could not be applied to the physicians' RICO claims, the court could have easily enforced the remainder of the arbitration agreements without any limitation on respondents' claims for treble damages under RICO.

The physicians counter that refusing to compel arbitration as to the physicians' RICO claims rather than striking the damages limitation is especially compelling in this case. They assert that limitations on the remedial power of the arbitrator are an integrated component of the arbitration agreement and cannot be severed. Arguing that severance of the damages limitations would not create a disincentive to drafters to avoid such illegal limitations, the physicians contend that those with the power to compel predispute arbitration agreements would benefit from the inclusion of the most restrictive limitations, knowing that the limitations will involve no risk but will deter potential litigants and will be stricken only following judicial review.

SIGNIFICANCE

The Supreme Court initially refused to compel arbitration of statutory causes of action. However, the Court later held that federal statutory claims may be the subject of arbitration agreements that are enforceable under the Federal

Arbitration Act. See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985). Two years later, in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), the Court held that RICO claims are arbitrable.

However, the Supreme Court has cautioned that statutory causes of action, embodying unique public policy concerns, are not automatically subject to arbitration. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985). According to the Court, a federal statutory claim is arbitrable only if a court determines as an initial matter that (1) the parties' agreement to arbitrate reaches the statutory issues and (2) "legal constraints external to the parties' agreement" do not foreclose arbitration of the statutory claims. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985).

Acknowledging that it has held that federal statutory claims that may be the subject of arbitration agreements are enforceable because the agreement only determines the choice of forum, the Supreme Court has stated that, by agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum. *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 295 n.10 (2002). The question presented in this case is whether a court or an arbitrator should determine if an arbitration agreement subjecting statutory claims to arbitration requires a party to forgo substantive rights afforded by the statute.

Several circuits have addressed the question of whether the validity of a limitation on remedies in an arbitra-

tion clause should be addressed by the district court or the arbitrator in the first instance. Several have ruled that the decision should be made by the arbitrator. See, e.g., *Thompson v. Irwin Home Equity Corp.*, 300 F.3d 88, 91-92 (1st Cir. 2002); *Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222, 228, 232 (3d Cir. 1997); *Boomer v. T&T Corp.*, 309 F.3d 404, 419 (7th Cir. 2002); *Arkcom Digital Corp. v. Xerox Corp.*, 289 F.3d 536, 539 (8th Cir. 2002).

In addition to the Eleventh Circuit, two other circuits have held that courts should make the determination in the first instance. *Investment Partners, LLP v. Glamour Shots Licensing, Inc.*, 298 F.3d 314, 316 (5th Cir. 2002); *Graham Oil Co. v. ARCO Prods. Co.*, 43 F.3d 1244, 1247-49 (9th Cir. 1995); *Cf. Brooks v. Travelers Ins. Co.*, 297 F.3d 167 (2d Cir. 2002). The limitations included restrictions on the length of the hearing, damages, and attorney fees and costs.

Because arbitration is created by contract, and the contract defines the arbitrator's authority or jurisdiction, an arbitrator's finding that he or she is not limited by a contract's limitation on the awarding of arbitration fees could result in the decision being vacated as in excess of the arbitrator's jurisdiction. On the other hand, should the arbitrator refuse to award treble damages for violation of RICO, a mere error of law is not grounds for vacating an arbitration award. See 9 U.S.C. § 10. The Federal Arbitration Act provides only limited grounds for vacating an award, and an error of law is not one of them. An arbitrator's decision will be upheld, unless it is completely irrational or constitutes a manifest disregard of the law. *Wilko v. Swan*, 346 U.S. 427 (1953). As long as an honest arbitrator is even arguably construing or

applying the contract and acting within the scope of his or her authority, the fact that a court is convinced the arbitrator committed serious error does not suffice to overturn the arbitrator's decision. *Eastern Associated Coal Corp. v. United Mine Workers of America, Dist. 17*, 531 U.S. 57, 62 (2000).

The impact of the Court's decision in this matter is somewhat difficult to predict. Unlike most of the arbitration cases before the Supreme Court recently, this case does not involve consumers or employees upon whom arbitration agreements were forced. See, e.g., *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 295 n.10 (2002) (employee); *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001) (employee); *Green Tree Financial Corp.-Alabama v. Randolph*, 531 U.S. 79 (2000) (consumer). The physicians here have been found to be "sophisticated" commercial actors, who, unlike most employees and consumers, were able to negotiate the terms of their contracts with the MCOs. Whether this will be determinative in this case remains to be seen. Nonetheless, the Court's decision will provide needed guidance regarding the rapidly increasing number of arbitration agreements requiring the arbitration of statutory claims.

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