IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
Norfolk Division

In re:

ZETIA (EZETIMIBE) ANTITRUST LITIGATION

MDL NO. 2:18md2836

THIS DOCUMENT RELATES TO:

2:18cv23; 2:18cv39; and 2:18cv71

REPORT AND RECOMMENDATION

In this antitrust action Plaintiffs' claims arise from Defendant Merck's alleged efforts to delay generic competition for its cholesterol drug Zetia. Merck has moved to compel certain Plaintiffs to arbitrate the claims under the terms of a written Distributorship Agreement. The arbitration clause in the agreement does not unambiguously delegate preliminary questions of enforceability to the arbitrator. It also contains a clear, prospective waiver of certain statutory remedies, including Plaintiffs' claims for treble damages and attorney's fees under Section Four of the Clayton Act. 15 U.S.C. § 15(a). Because federal law directs the court to determine this preliminary issue, and the waivers render the clause unenforceable as to Plaintiffs' antitrust claims, this report recommends that the court deny Merck's Motion to Compel Arbitration.

I. FACTUAL AND PROCEDURAL HISTORY

The three named Plaintiffs presently before the court, FWK Holdings, LLC, Cesar Castillo, Inc., and Rochester Drug Cooperative, Inc., are drug wholesalers which directly purchased Zetia from Merck[1] during the period 2006 to 2016 ("Direct Purchasers" or "Plaintiffs"). Zetia, generically known as ezetimibe, is a cholesterol-lowering medication formerly subject to patent protection. For purposes of the present motion, it is sufficient to summarize Plaintiffs' 90-page Complaint as alleging a scheme by Merck to extend patent protection for Zetia by obtaining a reissued patent, Patent No. RE 37,721 ("RE '721 patent") for compounds which were "inherent metabolites" of compounds disclosed in earlier patents. Compl. ¶ 153 (ECF No. 1 at 43-44).[2] Plaintiffs allege this inherency rendered the RE '721 patent invalid as anticipated by the earlier patents. Id. They also allege Merck withheld references during the reissue

[1] The complaints name five related Merck entities, collectively referred to in this Report as Merck.

[2] ECF numbers referenced in this Report and Recommendation correspond to case number 2:18cv23, FWK Holdings, LLC v. Merck & Co., Inc. et al.. Merck filed substantially identical motions prior to consolidation of the direct purchaser actions in MDL No. 2836. See Mots., Case Nos. 2:18cv23 (ECF No. 92); 2:18cv39 (ECF No. 69); and 2:18cv71 (ECF No. 80). As stated in this court's August 15, 2018 order, the motions and responsive briefing are construed to apply to the forthcoming Direct Purchasers' consolidated complaint in Case No. 2:18md2836, presently due no later than September 13, 2018. Pretrial Order No. 4, at 2 n.1 (ECF No. 141 at 2).

prosecution, amounting to inequitable conduct which would also void the RE '721 patent. Compl. ¶¶ 156-58 (ECF No. 1 at 45-47).

Co-Defendant Glenmark, a generic drug maker, challenged the reissued patent and first filed an Abbreviated New Drug Application (ANDA) asserting rights to market a generic version of the drug in 2006. Compl. ¶ 144 (ECF No. 1 at 41). Merck sued Glenmark, alleging infringement of the RE '721 patent, and Glenmark counterclaimed alleging the patent was invalid under several theories. Plaintiffs allege that Glenmark's challenges to the RE '721 patent's validity for inequitable conduct and, as anticipated by Merck's prior patents, were clearly meritorious. Compl. ¶ 176 (ECF No. 1 at 50). But instead of pursuing them to finally obtain a declaration of invalidity, Glenmark settled with Merck, agreeing to drop its claims in exchange for Merck's promise not to compete with Glenmark, by refraining from producing its own authorized generic version of the drug during Glenmark's 180-day period of exclusivity after it entered the market. Compl. ¶ 181 (ECF No. 1 at 51). Plaintiffs allege this *quid pro quo* agreement not to compete amounted to an improper reverse payment to delay generic entry of the type proscribed under federal antitrust law as interpreted by the Supreme Court. F.T.C. v. Actavis, Inc., 570 U.S. 136 (2013).

The three named Direct Purchasers before the court on these motions each brought putative class action complaints seeking to

recover from Merck and Glenmark for overcharges they claim to have paid during the delay in generic competition and during the period after Glenmark entered the market when Merck agreed not to compete with its own generic version of the drug. All three complaints were subject to a Transfer Order by the Judicial Panel on Multidistrict Litigation (JPML) consolidating these cases for all pretrial purposes in this MDL proceeding. Transfer Order, MDL No. 2836 (ECF No. 123). In addition to these Plaintiffs, the MDL includes putative class action claims by End Payor Plaintiffs as well as individual claims filed by various large Retailer Plaintiffs, including Walgreens, Rite Aid and CVS. All of the consolidated claims allege antitrust or anticompetitive injuries arising from the same course of conduct and all name Merck and Glenmark as Defendants.[3]

The Merck Defendants filed motions to dismiss, or in the alternative to stay the cases filed by the Direct Purchasers pending arbitration. Merck alleges that all three named Direct Purchasers, as well as the other putative Direct Purchaser class members, were parties to Merck's Authorized Distributorship (MAD) Agreement governing the terms of their relationship. The MAD Agreements for the three named Direct Purchaser parties are nearly

[3] The MDL presently consists of 18 cases, including five cases transferred here from three other jurisdictions.

identical and define the parties' obligations with respect to the purchase of Merck products. For example, the MAD Agreements require that distributors purchase Merck products only from Merck; not resell Merck products in foreign markets; and abide by certain credit and charge-back policies. Decl. of Jennifer L. Greenblatt, Ex. A ("MAD Agmt.") (ECF No. 96-1). The MAD Agreements contain no pricing or product information, nor do they obligate any party to purchase or sell any particular quantity of Merck product. Instead, they specify certain terms under which such sales would, and apparently did, take place. Id.

Executed in 2012, the MAD Agreements presently before the court contain identical language reflecting the parties' agreement to arbitrate.[4] The relevant paragraph provides:

> Arbitration. Any controversy, claim or dispute ("Dispute") that may arise out of or be related to the performance, construction, interpretation or enforcement of this Agreement (including disputes as to the scope, applicability and meaning of this arbitration clause) shall be submitted to mandatory, binding, confidential arbitration pursuant to the Federal Arbitration Act, 9 U.S.C. § 1 et seq., under the auspices

[4] The operative agreements for two named Plaintiffs were signed in 2012. Earlier agreements covering the same subject matter did not contain arbitration clauses. The Plaintiffs have argued that the 2012 agreements do not have retroactive effect, as the events giving rise to their claims occurred almost entirely before 2012. In light of the recommendation set forth in this report, the undersigned does not reach the issue of whether the arbitration language is sufficiently broad to be given retroactive effect. See Wachovia Bank, Nat'l Ass'n v. Schmidt, 445 F.3d 762, 767 (4th Cir. 2006) (observing that arbitration clause encompassing claims relating to "any aspect of the relationship between the parties" is far broader than one encompassing those relating to the agreement itself).

> and Commercial Rules of the American Arbitration Association.
>
> . . .
>
> The arbitrator(s) is empowered to award equitable relief but not empowered to award damages in excess of compensatory damages and each Party hereby irrevocably waives any right to recover such damages with respect to any dispute within the scope of this clause. Each party shall pay for all attorney's fees and costs it incurs in connection with the arbitration.

Id. ¶ 7(A) (ECF No. 96-1 at 4-5).

Merck argues that the clause requires all the Direct Purchasers to arbitrate their claims. Its motion seeks to dismiss the Direct Purchasers' claims, or alternatively to stay them until the arbitration proceedings are concluded. Plaintiffs disagree, and assert several challenges to arbitrability. Specifically, Plaintiffs claim the clause does not apply to their antitrust claims because those claims do not relate to the performance or enforcement of the MAD Agreements. They note that the Agreements impose no obligation on either party to buy or sell Merck products, and that the antitrust damages they allege flow, not from any contractual duty, but from a market allocation scheme that increased prices by keeping competitors - including Glenmark and various non-parties - from selling generic ezetimibe. The Direct Purchasers also raise administrative challenges to the clause, noting that only one of the Merck entities is a signatory and that the arbitration language appeared in the Agreements only in 2012,

two years after the conduct underlying the antitrust claims occurred. Finally, the Plaintiffs claim the clause is invalid as it contains prospective waivers of statutory antitrust remedies which Congress deemed nonwaivable.

Merck contends that all of these arbitrability challenges are reserved to the arbitrator to decide under the language of the parties' agreement. However, to the extent the court undertakes to decide them, Merck argues that none are sufficient to preclude arbitration.

For the reasons set forth in greater detail below, the undersigned agrees with the Direct Purchasers that the prospective waiver of statutory remedies contained in the arbitration clause renders it unenforceable. Because the parties' agreement did not delegate this preliminary question of arbitrability to the arbitrator to decide, the court retains jurisdiction to resolve it. Accordingly, this report recommends that the court deny Merck's Motions to Dismiss or Compel Arbitration (2:18cv23, ECF No. 92; 2:18cv39, ECF No. 69; 2:18cv71, ECF No. 80).

II. ANALYSIS

The Federal Arbitration Act (FAA) reflects the "overarching principle that arbitration is a matter of contract." Am. Express Co. v. Italian Colors Rest., 570 U.S. 228, 232 (2013). It is a congressional command that courts "vigorously enforce" arbitration agreements, including those which may require arbitration of

claims arising under federal law. In re Cotton Yarn Antitrust Litigation, 505 F.3d 274, 282 (4th Cir. 2007). The FAA explicitly provides that arbitration agreements are "valid, irrevocable, and enforceable, save upon such grounds as exists at law or in equity for the revocation of any contract." 9 U.S.C. § 2. State law contract defenses which do not "rely on the uniqueness of an agreement to arbitrate" may still prevent enforcement of the agreement to arbitrate. Dillon v. BMO Harris Bank, N.A., 856 F.3d 330, 334 (4th Cir. 2017) (quoting AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 341 (2011)).

Among these contract defenses, an arbitration agreement may be invalid as against public policy where it contains a "prospective waiver of a party's right to pursue statutory remedies." Id. (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 637 n.19 (1985)). Thus, even when an arbitration clause is sufficiently broad to encompass antitrust claims, "arbitration of the claim will not be compelled if the prospective litigant cannot effectively vindicate statutory rights in the arbitral form." Cotton Yarn, 505 F.3d at 282 (citing Green Tree Fin. Corp. - Ala. v. Randolph, 531 U.S. 79, 90 (2000)).

The Plaintiffs raise a number of challenges to Merck's claim that this dispute is subject to arbitration under the arbitration clause in the MAD Agreements. Such "question[s] of arbitrability" are in the normal course "undeniably an issue for judicial

determination." Hayes v. Delbert Servs. Corp., 811 F.3d 666, 671 (4th Cir. 2016) (quoting Peabody Holding Co. v. United Mine Workers of Am., Int'l Union, 665 F.3d 96, 102 (4th Cir. 2012)). The parties may, however, agree to assign questions of arbitrability to the arbitrator to decide. Because such delegation would depart from the norm, a court must find the assignment in "clear and unmistakable" evidence of the parties' agreement. Rent-A-Ctr., W., Inc. v. Jackson, 561 U.S. 63, 69 n.1 (2010).

This court's contract interpretation function encompasses the initial inquiry into whether the parties agreed to arbitrate the particular arbitrability questions raised. See Peabody Holding Co., 665 F.3d at 101. The interpretative rule, which presumes that the parties intended for such gateway questions of arbitrability to be decided by the court, does not apply to every type of objection to arbitration which might be raised. Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79, 83-84 (2002). Instead the presumption applies to certain gateway matters, such as whether the parties have a valid arbitration agreement at all, or whether a concededly binding arbitration clause applies to a certain type of controversy. Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444, 452 (2003). Other arbitrability challenges are not subject to the presumption of judicial resolution, as they involve questions of arbitration procedure better left to the arbitrator to decide. Howsam, 537 U.S. at 84. And consistent with its contractual nature,

an arbitration agreement may expressly assign responsibility for resolving gateway arbitrability challenges. Simply Wireless, Inc. v. T-Mobile US, Inc., 877 F.3d 522, 526 (4th Cir. 2017).

Thus, the question of which decisionmaker - court or arbitrator - resolves a particular challenge to arbitrability depends upon the nature of the challenge presented, whether the interpretive rule presuming judicial resolution applies, and finally whether the parties have obviated the need for an interpretive rule by clearly and unmistakably delegating authority to decide the preliminary question to the arbitrator. See Kristian v. Comcast Corp., 446 F.3d 25, 39-48 (1st Cir. 2006) (applying a "trilogy" of Supreme Court precedent to assess whether the court or an arbitrator should decide enforceability of an arbitration clause containing a prospective waiver of antitrust remedies). Applying that analysis to the Direct Purchasers' claims, the undersigned concludes that the MAD Agreement did not clearly and unmistakably delegate to the arbitrator resolution of all preliminary questions of arbitrability. Under established Fourth Circuit precedent, questions regarding the enforceability of clauses purporting to limit Plaintiffs' claims to vindicate statutory protections are for the court to determine. Finally, because the clause in this case contains an unenforceable prospective waiver of important antitrust safeguards, the court should deny Merck's Motion to Compel Arbitration.

A. The enforceability challenge raised by the Arbitration Agreement's prospective waiver of statutory rights should be decided by this court.

Merck's first argument is that all matters related to the arbitrability of the Direct Purchasers' claims must be decided in the first instance by the arbitrator. The company points to parenthetical language delegating certain jurisdictional questions to the arbitrator, and to the Agreement's incorporation of the Commercial Rules of the American Arbitration Association. It contends these terms comprise the parties' agreement to delegate all questions of arbitrability to the arbitrator.

But as the Direct Purchasers point out, the word "arbitrability" does not appear in the parenthetical language Merck relies upon. The word also did not appear in the Commercial Rules until 2012, after two of the operative MAD Agreements in this case were executed. And the language the parties did use in the MAD Agreement's delegation clause does not clearly and unmistakably encompass the type of challenge to arbitrability posed by the prospective waiver of statutory rights.

As noted, under the FAA, certain preliminary questions of arbitrability are ordinarily for the court to determine, absent "clear and unmistakable" evidence that the parties intended for an arbitrator to resolve them. Simply Wireless, Inc., 877 F.3d at 526. "The 'clear and unmistakable' standard is exacting, and the

presence of an expansive arbitration clause, without more, will not suffice." Peabody Holding Co., 665 F.3d at 102. As a result, the language of the MAD Agreement vesting the arbitrator with the power to resolve disputes "related to the performance, construction, interpretation or enforcement of [the] Agreement" is insufficient to delegate arbitrability questions to the arbitrator. See id.; Carson v. Giant Food, Inc., 175 F.3d 325, 330 (4th Cir. 1999).

Recognizing this, Merck mainly relies on the much narrower parenthetical language in the clause, identifying a subset of disputes also reserved to the arbitrator. The MAD Agreement describes this as "including disputes as to the scope, applicability and meaning of this arbitration clause." MAD Agmt. ¶ 7(A) (ECF No. 96-1). This parenthetical delegation, Merck argues, is sufficient to meet the clear and unmistakable evidence standard and requires that this court defer to the arbitrator resolution of all the Direct Purchasers' preliminary challenges.

The Direct Purchasers attack the parenthetical delegation clause on multiple fronts. They first argue that the parenthetical, which begins with the word "including," indicates that the clause is nothing more than a subset of the broad arbitration language rejected as an insufficient delegation under Carson and Peabody. But such a reading would render the parenthetical clause meaningless, which the Pennsylvania law of contract construction

seeks to avoid. Friestad v. Travelers Indemnity Co., 393 A.2d 1212, 1217 (Pa. Super. Ct. 1978).[5]

Plaintiffs next argue that, considering the parenthetical language as a separate delegation of gateway questions to the arbitrator, it is clear the delegation does not encompass every arbitrability challenge the Direct Purchasers raise. They note that the word "arbitrability" does not appear in the clause. Instead, the delegation is limited to questions regarding the "scope, applicability and meaning" of the arbitration language. MAD Agmt. ¶ 7(A) (ECF No. 96-1 at 4). While the use of the exact word "arbitrability" is not required to delegate preliminary questions to the arbitrator, the language used in the parenthetical delegation is significantly narrower than Merck claims.

Some of the challenges raised by the present motion likely fall within this delegation and would be for the arbitrator to decide. For example, Direct Purchasers' arguments regarding whether the antitrust claims alleged are sufficiently related to the performance or enforcement of the MAD Agreement relate to the scope and applicability of the arbitration clause. These would be for the arbitrator to determine under the parties' agreement.

But the delegation clause does not encompass Plaintiffs' claim that prospective waivers of certain statutory remedies

[5] The MAD Agreement provides that it is to be construed under Pennsylvania law. MAD Agmt. ¶ 7(Q) (ECF No. 96-1 at 8).

render the clause invalid or unenforceable. This is especially so given the presumption that such questions are for the court to resolve, and the unambiguous nature of the statutory rights waiver in the clause.

The Fourth Circuit has twice examined similar waivers and concluded that the enforceability questions they presented required judicial resolution. See Dillon, 856 F.3d at 334-35; Hayes, 811 F.3d at 671 n.1. Both cases involved choice of law provisions which purported to limit or prohibit the enforcement of federal statutory protections. In refusing to compel arbitration of the disputes, the court noted that where there is uncertainty regarding the terms of the agreement and whether those terms would preclude enforcement of statutory claims, the arbitrator should determine in the first instance whether those terms would deprive a party of those remedies. Dillon, 856 F.3d at 334. But where clear language takes the "plainly forbidden step" of prospectively waiving federal rights, the court may conclude that it is unenforceable as a matter of law. Hayes, 811 F.3d at 675.

Both Hayes and Dillon are consistent with the United States Supreme Court's view. In PacifiCare Health Systems, Inc. v. Book, 538 U.S. 401 (2003), the Court considered an arbitration provision with "too much legal ambiguity" for the court to determine whether the challenge presented a question of arbitrability for the court to decide. See Kristian, 446 F.3d at 40 (citing PacifiCare, 538

U.S. at 407). Because the Court did "not know how the arbitrator [would] construe the remedial limitations, the question whether they rendered the parties' agreements unenforceable and whether it [was] for courts or arbitrators to decide in the first instance [were] unusually abstract." PacifiCare, 538 U.S. at 407. As a result, the Court directed arbitration to resolve those ambiguities, and answer "the preliminary question whether the remedial limitations at issue [ ] prohibit an award of RICO treble damages." Id. at 407 n.2.

Merck argues that PacifiCare is directly analogous to matters pending in this court and that this court should likewise defer the enforceability challenge posed by the waiver to the arbitrator to decide. But as the First Circuit has noted, in an even more closely analogous case, where the statutory waivers are clear, the questions posed by the enforceability challenge are for the court to resolve. See Kristian, 446 F.3d at 46. In that case, the court also interpreted an arbitration clause purporting to bar antitrust remedies, including treble damages. In deciding the preliminary question of whether the court or an arbitrator should address such claims, the court conducted a detailed analysis of Supreme Court precedent and concluded that PacifiCare teaches such matters are for the court to decide, absent ambiguous language. Summarizing its conclusion, the court wrote:

> Implicit in the PacifiCare analysis is the proposition that if the remedies limitation in the arbitration agreement posed a clear conflict with the remedies available in the RICO statute, that clear conflict would pose a question of arbitrability. In other words, in the face of a vindication of statutory rights claim based on such a clear conflict, the court would decide the question of the enforceability of the arbitration clause in the first instance.

Id. at 46.

Thus, at a minimum, this court must examine the prospective waiver to determine whether it is ambiguous, or whether it clearly takes the "plainly forbidden" step of precluding substantive remedies. Hayes, 811 F.3d at 675.

Nothing in the MAD Agreement's parenthetical delegation suggests the parties agreed to modify this presumptive rule. Certain preliminary questions of arbitrability - namely scope questions related to the applicability of the clause - were delegated to the arbitrator under the language of the parties' contract. But that language says nothing about challenges to the validity or enforceability of the arbitration clause. This omission is particularly significant in light of the broader language concerning the types of contract disputes subject to arbitration under the clause. It is also significant that the arbitration clause expressly incorporates the FAA, under which such enforceability challenges are decided by the court. See Simply Wireless, 877 F.3d at 530 (Floyd, J., dissenting)(noting

arbitration agreement's incorporation of FAA, which contemplates judicial resolution of arbitrability disputes).

Likewise, the clause's incorporation of the AAA Commercial Rules does not clearly and unmistakably demonstrate that the parties intended for the arbitrator to resolve the enforceability challenge posed by the prospective waiver. This is primarily because the delegation clause in the parenthetical specifically addresses a narrower set of gateway questions than the Commercial Rules purport to address. When two provisions of a contract purport to address the same subject matter, the more specific language controls. Trombetta v. Raymond James Fin. Servs., Inc., 907 A.2d 550, 560 (Pa. Super. Ct. 2006) ("[t]he specific controls the general when interpreting a contract."). Moreover, the Commercial Rules in effect at the time the 2012 MAD Agreements were executed did not use the term "arbitrability," and even after that word was added in 2013, the provision merely confers power on the arbitrator to resolve such disputes, but does not expressly direct that she do so. See Commercial Arbitration Rules and Mediation Procedures R.7 (Am. Arbitration Ass'n 2013) (adding arbitrability language to 2009 rules, available at www.adr.org/ArchiveRules).

In Simply Wireless, the Fourth Circuit ruled that incorporation of the JAMS Comprehensive Rules and Procedures in the parties' arbitration clause was sufficient to delegate

preliminary questions of arbitrability to the arbitrator. 877 F.3d at 528. The case is distinguishable on two fronts. First, the arbitration agreement in Simply Wireless did not contain a more specific and limited delegation of preliminary questions. Id. at 525. Second, the JAMS Rules then in effect phrased the delegation in mandatory terms, specifically providing that "jurisdictional and arbitrability disputes … shall be submitted to and ruled on by the Arbitrator." JAMS Comprehensive Arbitration Rules and Procedures R. 11(b) (July 2014) (emphasis added). By contrast, the MAD Agreement contains an express delegation of only a subset of arbitrability challenges to the arbitrator. And Rule 7 of the AAA Commercial Rules incorporated in the MAD Agreements is permissive, not mandatory, providing "the arbitrator shall have the power to rule on his or her own jurisdiction, including any objections to the existence, scope, or validity of the arbitration agreement." Commercial Rules, supra. Although the jurisdictional clause in the Commercial Rules was extended to disputes regarding "the arbitrability of any claim or counterclaim" in 2014, the language of Rule 7 is still permissive, conferring jurisdiction on the arbitrator, but not requiring submission of such disputes by the parties. Id. As a result, even considering the incorporation of the Commercial Rules, the parties' explicit language delegating only scope and meaning questions to the arbitrator is not superseded by their incorporation. Therefore, the court should

enforce the parties' express delegation, and defer arbitrability challenges involving the scope of the clause, but examine the Direct Purchasers' enforceability challenge based on the prospective waiver of statutory rights.

B. The unambiguous prospective waiver of statutory rights in the Arbitration Agreement would prevent Direct Purchasers from effectively vindicating their claims in the arbitral forum.

The FAA requires the court enforce an agreement to arbitrate "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. A court will not compel arbitration "if the prospective litigant cannot effectively vindicate his statutory rights in the arbitral forum." Cotton Yarn, 505 F.3d at 282. This so-called "effective vindication" exception can arise where an arbitration agreement is alleged to "operate[] ... as a prospective waiver of a party's right to pursue statutory remedies." Mitsubishi Motors Corp., 473 U.S. at 637 n.19. The Supreme Court has acknowledged that restrictive arbitration provisions could trigger this exception. See Italian Colors, 570 U.S. at 236 (stating the exception "would certainly cover a provision in an arbitration agreement forbidding the assertion of certain statutory rights").

Because the text of the antitrust laws speaks in mandatory terms, the Supreme Court has implied, and the lower courts have routinely held, that the prescribed statutory remedies are

nonwaivable. See, e.g., Mitsubishi Motors Corp., 473 U.S. at 637 n.19; Kristian, 446 F.3d at 48. Therefore, if an arbitration agreement operates to preclude assertion of those remedies, courts will refuse to enforce it as against public policy.[6] See, e.g., Dillon, 856 F.3d at 334; Hayes, 811 F.3d at 674-75; Gaines v. Carrollton Tobacco Bd. of Trade, Inc., 386 F.2d 757, 759 (3d Cir. 1967) ("[I]t seems clear as a matter of law that such an agreement, if executed in a fashion calculated to waive damages arising from future violations of the antitrust laws, would be invalid on public policy grounds."). For present purposes, this means that if the arbitration provisions of the MAD Agreement operate as a prospective waiver of the right to assert an antitrust claim for treble damages and/or attorney's fees in the arbitral forum, those provisions may not be enforced.

The operative language of the arbitration provision states:

> The arbitrator(s) is empowered to award equitable relief but not empowered to award damages in excess of compensatory damages and each Party hereby irrevocably waives any right to recover such damages with respect to

[6] In his Italian Colors opinion for the majority, Justice Scalia characterized the effective vindication exception as a "judge-made exception to the FAA." 570 U.S. at 235. Though judges undoubtedly apply the exception, it should fairly be noted that it exists solely to vindicate those explicit policies which Congress saw fit to place beyond the reach of private contract. The Court itself has emphasized the importance of Congress's chosen remedies in the antitrust laws. See, e.g., Hawaii v. Standard Oil Co. of Cal., 405 U.S. 251, 262 (1972).

> any dispute within the scope of this clause. Each party shall pay for all attorney fees it incurs in connection with the arbitration. The costs of the arbitration proceeding shall be shared equally between the Parties.

MAD Agmt. ¶ 7(A) (ECF No. 96-1 at 4-5.). Thus, the first issue is whether antitrust treble damages under 15 U.S.C. § 15(a) constitute damages "in excess of compensatory damages." Merck argues that they may not, and urges the court to defer to the arbitrator to resolve this preliminary question. The undersigned concludes that treble damages are unambiguously "in excess of compensatory damages" and that by requiring the Direct Purchasers to "irrevocably waive any right to recover such damages" the arbitration provision would operate to preclude such an award. Furthermore, the MAD Agreement precludes a recovery of attorney's fees, another mandatory remedy under § 15(a), by a successful plaintiff seeking antitrust damages. Those provisions therefore constitute unenforceable prospective waivers of statutory rights.

The Supreme Court has not been perfectly clear as to the exact nature of statutory treble damages, but its cases at minimum demonstrate that such damages are something "in excess of" compensatory damages. In Texas Industries, Inc. v. Radcliff Materials, Inc., 451 U.S. 630, 639 (1981), the Court noted that "[t]he very idea of treble damages reveals an intent to punish past, and to deter future, unlawful conduct." In Vermont Agency of Natural Resources v. United States ex rel. Stevens, 529 U.S. 765,

784 (2000), the Court described the treble damages provision in the False Claims Act as "essentially punitive in nature." Regardless of the intent for which a statute prescribes them, "it is important to realize that treble damages have a compensatory side ... in addition to punitive objectives." Cook County, Ill. v. United States ex rel. Chandler, 538 U.S. 119, 130 (2003); see also Comm'r v. Glenshaw Glass Co., 348 U.S. 426, 427 (1955) (recognizing "the punitive two-thirds portion of a treble-damage antitrust recovery"). Thus, while the Clayton Act's treble damages provision may indeed serve a partially remedial function, there is no doubt the provision's full measure of damages is "in excess of compensatory damages." See, e.g., ZF Meritor, LLC v. Eaton Corp., 696 F.3d 254, 300 (3d Cir. 2012) ("[I]n the antitrust context, a damages award not only benefits the plaintiff, it also fosters competition and furthers the interests of the public by imposing a severe penalty (treble damages) for violation of the antitrust laws.").

Despite this authority, Merck claims that an arbitrator might construe the term "compensatory damages" as used in the MAD Agreement as co-extensive with treble damages under the Clayton Act. But the plain language of § 15(a) mandates recovery by a successful plaintiff of "threefold the damages by him sustained." Using the ordinary definition of compensatory damages, the damages provision in § 15(a) could be translated as "three times

compensatory damages." See Compensatory Damages, Black's Law Dictionary (10th ed. 2014) ("Damages sufficient in amount to indemnify the injured person for the loss suffered."). However, if "compensatory damages" might also *include* treble damages, as Merck contends, then § 15(a) would seemingly permit trebling a second time. Continually substituting the ordinary meaning of compensatory damages with that offered by Merck would result in successive threefold multipliers *ad infinitum*. A common sense reading of § 15, whereby a plaintiff establishes its damages and then recovers three times that fixed amount, avoids this problem.

Merck primarily relies on PacifiCare, 538 U.S. 401, which refused to invalidate arbitration agreements that imposed a limitation on damages in the context of alleged violations of the RICO statute. It bears mention that the Supreme Court did not determine that the arbitration clause in PacifiCare was enforceable. Instead it remanded for the arbitrator to determine questions of arbitrability which were "unusually abstract." Id. at 407. Moreover, the contract provisions considered in PacifiCare are distinguishable. The four agreements under review in that case variously prohibited an arbitrator from awarding "punitive," "exemplary," or "extra contractual damages."[7] Id. at 405. The lower

[7] Only one of the four agreements used the term "extra-contractual damages," and the context in which it was used suggests it may have been interpreted to exclude only punitive, exemplary or mental-anguish damages. See PacifiCare, 538 U.S. at 407 n.2.

courts had refused to compel arbitration, holding that the damages restriction precluded an award of treble damages under RICO. Id. at 403. The Supreme Court reversed, citing uncertainty about whether an arbitrator would in fact construe the various contracts to preclude a treble damages award. Id. at 406-07. That uncertainty made it "premature" for the Court to address the question of enforceability, and therefore "the proper course [was] to compel arbitration" under the contract. Id. at 404, 407.

No such uncertainty exists in this case. The MAD Agreement does not *exclude* a specific type of damages. Rather, it permits only one type of damages, and prevents Direct Purchasers from even asserting their rights under federal law. In so doing it prevents the arbitrator from awarding *any* damages *except* compensatory damages.[8] MAD Agmt. ¶ 7(A) (ECF No. 96-1 at 4.). Invalidating the contract in PacifiCare would have required finding that statutory treble damages *are* punitive damages; by contrast, invalidating the provision here requires finding only that such damages *are not* purely compensatory.[9] No ambiguity prevents the latter conclusion.

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[8] In light of the above discussion, it is clear that the MAD Agreement must permit recovery of antitrust treble damages to be enforceable. It is perhaps telling, then, that counsel for Merck was reluctant to concede at argument that the Direct Purchasers would be entitled to treble damages if successful, regardless of the forum.

[9] PacifiCare uses the terms "remedial" and "compensatory" somewhat interchangeably, but never suggests that statutory treble damages

See Kristian, 446 F.3d at 44-47 (concluding that PacifiCare impliedly recognized that a clear conflict between an arbitration provision and a statutory remedy would raise a question of arbitrability for the court).

The attorney fees prohibition in the arbitration agreement is plainer still. If the court enforced this provision and compelled arbitration, the Direct Purchasers would be precluded from recovering attorney's fees even if they succeeded on their antitrust claims, contravening a key purpose of § 15. See Alyeska Pipeline Serv. Co. v. Wilderness Soc'y, 421 U.S. 240, 263 (1975) (offering antitrust law as a "prime example" of Congress's policy of incentivizing private enforcement by means of fee-shifting). Merck suggests that the provision, on its face, simply prohibits fee shifting "in connection with the arbitration," MAD Agmt. ¶ 7(A) (ECF No. 96-1 at 5), and therefore does not interfere with a litigant's "right to pursue statutory remedies" in the courts. See Italian Colors, 570 U.S. at 235. But Merck may not avoid the question of the arbitration provision's enforceability by pointing to the remedies that would be available if the provision was not enforced. Nor will the court read any saving exception into the

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are purely either. See 538 U.S. at 405-06. Suffice it to say that the Court's treatment of these terms permits a conclusion that treble damages could be entirely remedial but only partially compensatory, a conclusion that would still run aground of the MAD Agreement's arbitration provision.

parties' contract language. See Whitman v. Legal Helpers Debt Resolution, LLC, No. 4:12-cv-00144-RBH, 2012 WL 6210591, at *4 (D.S.C. Dec. 13, 2012) (refusing to interpret a contract provision prohibiting fee-shifting by an arbitrator as including an exception for statutory claims providing for an award of fees).

Having concluded that the remedy limitations in the MAD Agreement arbitration provisions are unenforceable, the court must decide "whether severance of the [limiting] provisions, rather than invalidation of the arbitration agreements, would be the appropriate remedy." Cotton Yarn, 505 F.3d at 292. Because the challenged provisions are central elements of the arbitration agreement as a whole, and because the MAD Agreement itself does not provide for severability, the undersigned recommends invalidation of the entire arbitration agreement.

"[W]hether an enforceable arbitration agreement exists ... is a matter of contract interpretation governed by state law." Rota-McLarty v. Santander Consumer USA, Inc., 700 F.3d 690, 699 (4th Cir. 2012). The MAD Agreement contains a choice-of-law clause dictating that Pennsylvania law shall apply, MAD Agmt. ¶ 7(Q) (ECF No. 96-1 at 8), to which Virginia law gives effect, Colgan Air, Inc. v. Raytheon Aircraft Co., 507 F.3d 270, 275 (4th Cir. 2007). Unlawful contract provisions may not be severed if the provision is "central or essential to the parties' agreement." Dillon, 856

F.3d at 336; see also Huber v. Huber, 470 A.2d 1385, 1389 (Pa. Super. Ct. 1984) (reciting same principle).

In Hayes, the court refused to sever choice-of-law provisions in an agreement that would have entirely displaced the application of state and federal law to a dispute over a payday loan, concluding that they went "to the core of the arbitration agreement." 811 F.3d at 675-76. In a subsequent case examining nearly identical provisions, the court again rejected a proposal to sever the offending provisions and allow arbitration under other contract language. See Dillon, 856 F.3d at 336.

Although the arbitration provisions in the MAD Agreement are not as extreme as those in Hayes and Dillon, their limitations represent central components of the overall arbitration scheme. The provisions purport to completely immunize Merck from the majority of any potential liability under the antitrust laws and numerous other federal statutes which impose penalties for noncompliance, or damages beyond those actually incurred by the injured party.[10] In this way, the arbitration agreement, as applied to Plaintiffs' antitrust claims, resembles "an attempt by [Merck]

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[10] See, e.g., 15 U.S.C. § 1117 (statutory and treble damages provisions of Lanham Act); 15 U.S.C. § 1681n (punitive damages provision of Fair Credit Reporting Act); 18 U.S.C. § 1964(c) (treble damages provision of RICO statute); 35 U.S.C. § 284 (treble damages provision of Patent Act); 35 U.S.C. § 3729(a)(1) (civil penalty provision of False Claims Act).

to achieve through arbitration what Congress has expressly forbidden." Graham Oil Co. v. ARCO Prods. Co., 43 F.3d 1244, 1249 (9th Cir. 1994). As Hayes and Dillon make clear, an arbitration agreement's "central" or "essential" terms can encompass more than simply the agreement to arbitrate itself. Moreover, consistently severing unenforceable provisions while leaving the base agreement intact "creates an incentive to get away with as many 'bad' arbitration provisions as possible, knowing that the worst case scenario is a court sending the case to arbitration with some of them stripped out." Winston v. Academi Training Ctr., Inc., No. 1:12-cv-767, 2013 WL 989999, at *3 (E.D. Va. Mar. 13, 2013); see also Murray v. United Food & Commercial Workers Int'l Union, 289 F.3d 297, 304 (4th Cir. 2002) (refusing to allow union to rewrite arbitration clause "on a case-by-case basis in order to claim that it is an acceptable one").

The structure of the MAD Agreement reinforces the conclusion that severability is not the appropriate remedy in this case. The arbitration agreement falls under a single heading and contains just six sentences, half of which would be excised by Merck's proposed severance. See Carll v. Terminix Int'l Co., 793 A.2d 921, 925-26 (Pa. Super. Ct. 2002) (refusing to sever damages limitation from an arbitration provision, because "[t]he same contractual provision that directs arbitration limits the authority of the individual conducting that arbitration"; cf. Fellerman v. PECO

Energy Co., 159 A.3d 22, 29 (Pa. Super. Ct. 2017) (distinguishing Carll and allowing severance of a damage limitation in part because it was "separate and distinct" from arbitration clause, "both location-wise and functionally"). In addition, the MAD Agreement lacks a severability clause and contains an express integration clause. See MAD Agmt. (ECF No. 96-1.); cf. Kristian, 446 F.3d at 53 (relying on savings clause in contract to sever limitation on recovery of attorney's fees in arbitration agreement). Because the offending provisions are central to the arbitration agreement, and because the MAD Agreement itself does not suggest severance is appropriate, the undersigned recommends the court invalidate the entire arbitration agreement and deny Merck's motion.

III. RECOMMENDATION

For the foregoing reasons the undersigned recommends that Merck's Motions to Dismiss or Compel Arbitration (2:18cv23, ECF No. 92; 2:18cv39, ECF No. 69; 2:18cv71, ECF No. 80) be DENIED.

IV. REVIEW PROCEDURE

By copy of this report and recommendation, the parties are notified that pursuant to 28 U.S.C. § 636(b)(1)(C):

1. Any party may serve upon the other party and file with the Clerk written objections to the foregoing findings and recommendations within fourteen (14) days from the date of mailing of this report to the objecting party, see 28 U.S.C. § 636(b)(1), computed pursuant to Rule 6(a) of the Federal Rules of Civil

Procedure. Rule 6(d) of the Federal Rules of Civil Procedure permits an extra three (3) days, if service occurs by mail. A party may respond to any other party's objections within fourteen (14) days after being served with a copy thereof. See Fed. R. Civ. P. 72(b)(2) (also computed pursuant to Rule 6(a) and (d) of the Federal Rules of Civil Procedure).

2. A district judge shall make a de novo determination of those portions of this report or specified findings or recommendations to which objection is made.

The parties are further notified that failure to file timely objections to the findings and recommendations set forth above will result in a waiver of appeal from a judgment of this Court based on such findings and recommendations. Thomas v. Arn, 474 U.S. 140 (1985); Carr v. Hutto, 737 F.2d 433 (4th Cir. 1984); United States v. Schronce, 727 F.2d 91 (4th Cir. 1984).

/s/
Douglas E. Miller
United States Magistrate Judge

DOUGLAS E. MILLER
UNITED STATES MAGISTRATE JUDGE

September 6, 2018