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U.S. Supreme Court Ruling Paves the Way for Companies to Enforce Class Action Waivers in Arbitration Agreements

On April 27, 2011, the United States Supreme Court issued a decision in *AT&T Mobility LLC v. Concepcion* that ensures that companies will be able to enforce well-drafted class action waiver clauses in consumer contracts containing arbitration agreements – rejecting lower court decisions finding such waiver clauses to be unconscionable. Specifically, the Court held that the Federal Arbitration Act (“FAA”) preempts a California rule that held class action waivers in consumer arbitration agreements to be unconscionable and therefore unenforceable. The Court’s 5-4 decision, authored by Justice Scalia, rested on the conclusion that “[r]equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA.” Given that class treatment likely will be precluded in the arbitration context, one can expect that many businesses will include arbitration agreements and class waiver provisions in their consumer contracts, resulting in a decline in consumer class action litigation.

Background

In 2002, Vincent and Liza Concepcion contracted to purchase AT&T cellular telephone service. By signing up for the service, the Concepcions received free telephones, but AT&T charged them \$30.22 in sales taxes based on the retail price of the phones. The consumer contract between the Concepcions and AT&T required arbitration for all disputes and permitted the parties to bring only individual claims. The contract specifically provided that the parties could not bring claims “as a plaintiff or class member in any purported class or representative proceeding.”

The Concepcions sued AT&T in 2006 in federal court in California for false advertising and fraud for charging sales tax on phones that had been advertised as free. The Concepcions’ complaint was consolidated with a putative class action, and AT&T then moved to compel arbitration under the contract. The district court denied AT&T’s motion, agreeing with the Concepcions that the arbitration agreement was unconscionable under California Supreme Court precedent because it prohibited class procedures. The Ninth Circuit Court of Appeals affirmed and also held that the FAA did not preempt California’s unconscionability rule. In the Ninth Circuit’s analysis, since California law prohibited class action waivers in both the litigation and arbitration contexts, it did not disfavor arbitration. Accordingly, California’s rule fell within the scope of 9 U.S.C. § 2, a section of the FAA providing that arbitration agreements are “valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”

The Supreme Court’s Opinion

The Court reversed the Ninth Circuit and held that the FAA preempts California’s rule that class waiver provisions in arbitration agreements are unconscionable. The Court emphasized that the FAA was intended to instill a federal policy favoring arbitration and to ensure that courts enforce arbitration agreements according to their terms. The FAA requires courts to place arbitration agreements on equal footing with other kinds of contracts. While California’s rule theoretically did not run afoul of the FAA because it prohibited class waivers in litigation as well as in arbitration, the Court noted that California courts tended to find arbitration agreements unconscionable much more often than they found other contracts unconscionable.

The core of the Court's reasoning was that the FAA preempts California's rule because requiring the availability of class arbitration proceedings is inconsistent with certain fundamental attributes of arbitration. Noting that informality is the "principal advantage" of arbitration, the Court found that class proceedings sacrifice this advantage in several ways:

- Class procedures make the dispute-resolution process slower, more complex and more costly. For example, asking an arbitrator to decide threshold issues as to whether a class may be certified greatly increase the complexity and costs of an arbitration proceeding.
- The rights of absent class members require that any class arbitration proceedings be conducted with a substantial level of formality. To be bound by an arbitrator's decision, absent class members would have to be adequately represented, have notice, and have the opportunity to opt out of the class. The Court was concerned about placing absent class members' due process rights in the hands of an arbitrator.
- Class arbitration increases risks for defendants to an unacceptable level. Company defendants are willing to enter into arbitration agreements with individual consumers because the costs to the company of an incorrect arbitrator decision are low. In class arbitration, however, companies face extremely high risks of incorrect decisions because of the absence of appellate review. As a result of these risks, the Court expressed skepticism that potential defendants would continue to be willing to enter into arbitration agreements if courts do not enforce class waivers.

The *AT&T Mobility* decision follows closely on the heels of the Supreme Court's decision in *Stolt-Nielsen S.A. v. Animalfeeds Int'l Corp.*, 130 S. Ct. 1758 (Apr. 27, 2010), another case in which the Court signaled an aversion to class arbitration. In that case, the Court went out of its way to strike down an arbitration panel's ruling that class arbitration was available where the agreement at issue was silent on this question.

Implications of the Decision

In the aftermath of *AT&T Mobility*, class action waiver provisions in arbitration agreements will almost always be found enforceable, unless they contain other terms that foreclose individual adjudication. Companies—even those relying on adhesive contracts to do business with large numbers of consumers—most likely will be able to require all consumer disputes to be resolved individually. Companies preferring to resolve disputes in individual arbitrations rather than in class arbitration or class litigation should consider including class action waiver clauses in their standard arbitration agreements.

If you would like more information on the *AT&T Mobility* decision or on the firm's Appellate and Consumer Class Action practices, please contact one of the attorneys below:

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