

# THE FUTURE OF CONSUMER ARBITRATION IN LIGHT OF *STOLT- NIELSEN*

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## *I. Overview - The Underlying Policy Issues*

In *Concepcion*,<sup>1</sup> the Supreme Court is poised to decide whether a judicially crafted California rule that serves to invalidate an arbitration class-action waiver as unconscionable is in conflict with the Federal Arbitration Act and therefore ineffective.<sup>2</sup> In deciding this case, the Court is presented with several significant policy conflicts, as is evidenced by the filing of fifteen *Amicus Curiae* briefs for the Respondent and eleven *Amicus Curiae* briefs for the Petitioner. Collectively, the *Amici* represent a broad spectrum of academic, economic, and social interests. At its core, the case presents the question of whether consumers and the businesses that serve them will continue to have access to arbitration in order to resolve individual disputes arising out of the numerous services that businesses provide consumers under standard form consumer agreements. Many of these contracts are designed to resolve individual disputes between business enterprises and consumers through arbitration. However, the contracts explicitly exclude, or require the waiver of, the consumer's participation in class action arbitrations. These

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<sup>1</sup> *Laster v. AT&T Mobility LLC*, 584 F.3d 849 (9th Cir. 2009), *cert. granted, sub nom. AT&T Mobility LLC v. Concepcion*, 130 S. Ct. 3322 (2010).

<sup>2</sup> If a class-waiver is held to be unconscionable, then it is severed from the arbitration agreement, leaving an arbitration agreement silent as to class-arbitration. If the class waiver is struck down and the arbitration agreement has a blow-out clause in place, then the blow-out clause will operate to invalidate the entire arbitration agreement.

agreements by design preclude the use of class actions to resolve consumer disputes under contracts that utilize arbitration to resolve such disputes.

Several *Amici* for the Petitioner summarize the fundamental policy considerations:

Many of the Chamber [of Commerce of the United States of America's] members and affiliates regularly employ agreements to arbitrate in their business contracts with their customers and employees. By agreeing to arbitrate with their counterparties, they avoid costly and time-consuming litigation when disputes arise. In its place, they adopt a dispute resolution mechanism that is speedy, fair, inexpensive, and effective. Based on the legislative policy reflected in the Federal Arbitration Act (FAA) and this Court's consistent endorsement of arbitration over the past several decades, Chamber members have structured millions of contractual relationships around arbitration agreements.

A class-arbitration waiver is a key component of many Chamber members' arbitration agreements. Decisions like the opinion below, which invalidated a class-arbitration waiver, frustrate the parties' intent, undermine their existing agreements, and erode the benefits offered by arbitration as an alternative to litigation.<sup>3</sup>

Also writing in support of the Petitioner as *Amici*, the Center for Class Action Fairness asserts:

*First*, class treatment is neither the only means nor necessarily the best means of providing aggrieved consumers with meaningful relief. In fact, class action litigation suffers from several pathologies which often make it a poor vehicle for the vindication of consumer rights: it is expensive, raising costs to consumers in the long-run; it is slow-moving, bringing relief, if at all, long after class members have been harmed; even when class

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<sup>3</sup> Brief for the Chamber of Commerce of the United States of America as Amicus Curiae Supporting Petitioner at 1-2, *AT&T Mobility LLC v. Concepcion*, 130 S. Ct. 3322 (2010) (No. 09-893).

plaintiffs do succeed, class members face significant barriers to obtaining recovery; and class settlements often are a boon for class action attorneys but a bust for class members who recover little or nothing of value.

*Second*, arbitration is superior in many cases to class actions in vindicating consumer rights. Individual arbitration provides swift resolution of disputes; allows for easy and complete recovery; and does not pit the interests of consumers against an attorney tasked with representing their interests. Indeed, consumers consistently report that they prefer pursuing their claims in arbitration to class action litigation. Therefore, both for the individual complainant and for aggrieved individuals in the aggregate, a contract selecting individual arbitration often will afford consumers a better mechanism for obtaining meaningful relief than class action litigation.<sup>4</sup>

The equally compelling counterpoint is made by the *Amici* States of Illinois, Maryland, Minnesota, Montana, New Mexico, Tennessee, and Vermont, and the District of Columbia:

States have long declined to enforce contracts that are unconscionable or offensive to public policy. These and other state law contract defenses are an important means of protecting consumers against predatory or unfair treatment. In urging FAA preemption of a state-law determination that an adhesive class-action waiver is unconscionable, petitioner asks federal courts to second-guess decades of state contract law, without any administrable standard to guide them. Because the decision below preserves States' historical ability to develop and enforce contract law, the *Amici* States have a significant interest in the outcome of this appeal. Moreover, preempting state law here would effectively eliminate consumer class actions, an important complement to government efforts at safeguarding consumers against fraudulent and deceitful practices.<sup>5</sup>

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<sup>4</sup> Brief of the Center for Class Action Fairness as Amicus Curiae Supporting Petitioner at 3-4, *AT&T Mobility LLC v. Concepcion*, 130 S. Ct. 3322 (2010) (No. 09-893).

<sup>5</sup> Brief for the States of Illinois Supporting Respondents, et al. at 1, *AT&T*

The Court will decide *Concepcion* in the context of these policy considerations. This article will explore the Court's recent decisions dealing with class actions in an arbitration setting and the possible outcomes those decisions forecast. Regardless of the Court's decision, however, the outcome will have a significant impact on arbitration as a means of settling consumer disputes.

## *II. The Federal Arbitration Act*

### A. The principles that have developed and govern arbitration in the United States

The Federal Arbitration Act ("FAA") allows for enforceable arbitration agreements in contracts involving interstate commerce or maritime transactions.<sup>6</sup> Under the FAA, courts must enforce arbitration contracts according to their terms.<sup>7</sup> Agreements to arbitrate are "a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit. Just as parties may limit by contract the issues which they will arbitrate, so too may they specify by contract the rules under which that arbitration will be conducted."<sup>8</sup> Doubts about the scope of arbitrable issues or the meaning of arbitration clauses should be resolved in favor of arbitration.<sup>9</sup> Congress enacted the FAA to overcome judicial hostility toward arbitration,<sup>10</sup> and in doing so it utilized the full extent of its Commerce Clause power.<sup>11</sup>

An arbitration agreement under the FAA is "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."<sup>12</sup> The FAA's Section 2 savings clause "embodies the national policy favoring arbitration and places arbitration agreements on equal footing with all other contracts..."<sup>13</sup> Contract defenses of general

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Mobility LLC v. Concepcion, 130 S. Ct. 3322 (2010) (No. 09-893).

<sup>6</sup> Federal Arbitration Act, 9 U.S.C. § 1 et seq. (2009).

<sup>7</sup> Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Univ., 489 U.S. 468, 478 (1988).

<sup>8</sup> *Id.* at 479 (1989) (citations omitted).

<sup>9</sup> Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24-25 (1983).

<sup>10</sup> Buckeye Check Cashing v. Cardegna, 546 U.S. 440, 443 (2006).

<sup>11</sup> See Allied-Bruce Terminix Cos., Inc. v. Dobson, 513 U.S. 265, 265-66 (1995).

<sup>12</sup> Federal Arbitration Act, 9 U.S.C. § 2 (2009).

<sup>13</sup> *Buckeye Check Cashing*, 546 U.S. at 443.

applicability, such as unconscionability, may be applied to invalidate arbitration agreements without contravening the FAA.<sup>14</sup> A challenge to the validity of the entire contract, as opposed to a challenge to the validity of the arbitration clause itself, is a question for the arbitrator, not a court.<sup>15</sup>

The FAA supplants state laws that discriminate against arbitration.<sup>16</sup> States cannot require that a dispute be resolved in a judicial forum where the parties have agreed to arbitration.<sup>17</sup> Moreover, the FAA preempts state law that undermines a primary objective of an arbitration agreement, such as achieving “streamlined proceedings and expeditious results.”<sup>18</sup> Under the FAA, pre-dispute arbitration agreements are valid even if the governing state law provides that arbitration agreements are unenforceable.<sup>19</sup>

Review is very limited under the FAA, however, as “the task of an arbitrator is to interpret and enforce a contract, not to make public policy.”<sup>20</sup> “It is only when [an] arbitrator strays from interpretation and application of the agreement and effectively dispense[s] his own brand of industrial justice that his decision may be unenforceable.”<sup>21</sup> At that point, the arbitrator has exceeded his powers under section 10(a)(4) and vacatur is proper.<sup>22</sup> Parties cannot contract for different standards of judicial review of an arbitration decision, governed by the FAA, than are provided in the FAA.<sup>23</sup>

#### B. *Stolt-Nielsen* - A clear pronouncement that class actions would not be inferred under the FAA

In *Stolt-Nielsen*, the Supreme Court held that “a party may not be compelled under the FAA to submit to class

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<sup>14</sup> *Doctor’s Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996); *see also Allied-Bruce Terminix Cos., Inc.*, 513 U.S. at 281.

<sup>15</sup> *Buckeye Check Cashing*, 546 U.S. at 444.

<sup>16</sup> *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984).

<sup>17</sup> *Id.* at 10.

<sup>18</sup> *Preston v. Ferrer*, 552 U.S. 346, 357-358 (2008) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 633 (1985)).

<sup>19</sup> *See Allied-Bruce Terminix Cos.*, 513 U.S. at 268.

<sup>20</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 130 S. Ct. 1758, 1767 (2010).

<sup>21</sup> *Id.* at 1767 (quoting *Major League Baseball Players Ass’n. v. Garvey*, 532 U.S. 504, 509 (2001) (per curiam) (internal quotation marks omitted)).

<sup>22</sup> *Id.* at 1780.

<sup>23</sup> *Hall St. Assocs. LLC v. Mattel, Inc.*, 552 U.S. 576, 581 (2008).

arbitration unless there is a contractual basis for concluding that the party *agreed* to do so.”<sup>24</sup> The Court was confronted with the issue of “whether imposing class arbitration on parties whose arbitration clauses are ‘silent’ on that issue is consistent with the [FAA].”<sup>25</sup> More specifically, the main issue was whether vacatur of the arbitration award was appropriate because the arbitrators “exceeded their powers” under the arbitration agreements. The Court reasoned that the arbitrators violated section 10(a)(4) of the FAA by deciding that class arbitration was permitted under arbitration clauses that were silent to the issue of class arbitration because of a public policy favoring arbitration.<sup>26</sup> The court held that vacatur of the arbitration award was appropriate.<sup>27</sup>

*Stolt-Nielsen* seems to signal the end of inferred class arbitration, at least in a commercial, non-consumer setting. A court cannot compel class arbitration without a contractual basis for concluding that the parties agreed to it; and presumably no potential defendant would agree to it. It is very unlikely that a potential defendant would elect class arbitration because the procedure combines the worst aspects of arbitration and litigation — it is a high cost and high stakes process with an uncertain preclusive effect on class members, lacks confidentiality (and transparency), and imposes extreme limitations on the scope of judicial review.

However, the dissent in *Stolt-Nielsen* suggested that the majority opinion does not extend to situations where a consumer has agreed to a class waiver in an adhesion contract.<sup>28</sup> *Concepcion* is a case currently before the Court that deals with that very issue — class action waivers in a consumer contract setting.<sup>29</sup> If the Court decides that class action waivers are susceptible to state law unconscionability challenges, then companies contracting with consumers may abandon arbitration altogether. *Stolt-Nielsen*, therefore, may mean the end of class arbitration, and *Concepcion* may mean the end of arbitration in consumer settings.

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<sup>24</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1775 (emphasis added).

<sup>25</sup> *Id.* at 1764.

<sup>26</sup> *See id.* at 1776-78.

<sup>27</sup> *Id.* at 1770.

<sup>28</sup> *See id.* at 1783 (Ginsburg, J., dissenting).

<sup>29</sup> *Laster*, 584 F.3d at 852-53.

C. Class arbitration is not precluded by the FAA, but must be shown to have been agreed upon by all parties

While the FAA allows class arbitration,<sup>30</sup> it still remains a voluntary process that cannot be forced onto parties.<sup>31</sup> A party will not be forced into class arbitration under the FAA absent a contractual basis for concluding that the party agreed to it.<sup>32</sup> Whether an arbitration agreement is silent as to class arbitration is an issue of contractual interpretation to be decided by an arbitrator.<sup>33</sup>

Section 2 of the FAA provides that agreements to arbitrate are “valid, irrevocable, and enforceable save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>34</sup> State law may be applied to determine if such grounds exist, but only if such law applies to contracts generally, not just to agreements to arbitrate.<sup>35</sup> Because an arbitration clause is severable from the rest of the contract as a matter of substantive federal arbitration law, the entire contract is not automatically struck down if the arbitration clause is found to be invalid.<sup>36</sup> This is true even where the container contract is itself an arbitration agreement since “[a]pplication of the severability rule does not depend on the substance of the remainder of the contract.”<sup>37</sup> Therefore, an unconscionable class waiver is severable from the rest of the arbitration clause.<sup>38</sup> Still, a court will uphold an “arbitration provision [that] specifically provides that if the class action waiver is found to be void, then the entire arbitration provision is null and void.”<sup>39</sup>

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<sup>30</sup> See *Stolt-Nielsen S.A.*, 130 S. Ct. at 1773-75; *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 445-46 (2003); 1 COMMERCIAL ARBITRATION § 16:1.

<sup>31</sup> *Volt Info. Scis. Inc.*, 489 U.S. at 479.

<sup>32</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1775.

<sup>33</sup> *Bazzle*, 539 U.S. at 445.

<sup>34</sup> Federal Arbitration Act, 9 U.S.C. § 2 (2009).

<sup>35</sup> *Casarotto*, 517 U.S. at 686.

<sup>36</sup> *Buckeye Check Cashing*, 546 U.S. at 445-46.

<sup>37</sup> *Rent-A-Center, West, Inc. v. Jackson*, 130 S. Ct. 2772, 2779 (2010).

<sup>38</sup> *Gatton v. T-Mobile USA, Inc.*, 2003 WL 21530185, at \*13 (C.D. Cal. Apr. 18, 2003).

<sup>39</sup> *Kaltwasser v. Cingular Wireless, LLC*, 350 Fed. App'x. 108, 109 (9th Cir. 2009).

D. Seven years of confusion induced by lower courts' erroneous interpretation of the Court ruling in *Bazzle*

Class arbitrations were uncommon before the Court's decision in *Bazzle*.<sup>40</sup> In *Bazzle*, homeowners obtained home improvement loans from Green Tree Financial.<sup>41</sup> The parties entered into a contract, governed by South Carolina law, which contained a broad arbitration clause.<sup>42</sup> The contract also stated that the FAA applied to the agreement.<sup>43</sup> However, Green Tree Financial failed to provide the borrowers a required form informing them of their rights to counsel and insurance agents; consequently, two sets of borrowers brought separate actions in South Carolina state court.<sup>44</sup>

Ultimately, two classes were certified and compelled arbitration proceedings before the same arbitrator, who found for the class in both cases. After Green Tree Financial appealed the arbitrator's rulings, the South Carolina Supreme Court withdrew both cases from the Court of Appeals and held that the contracts were silent as to class proceedings, that they allowed class proceedings, and that the arbitrations had properly assumed that form.<sup>45</sup>

The issue for the court in *Bazzle* was whether the South Carolina Supreme Court's holding was consistent with the FAA.<sup>46</sup> The Supreme Court plurality found that the holding was inconsistent with the FAA and vacated and remanded the case for an arbitrator to decide the question of contractual interpretation.<sup>47</sup> The Court reasoned that, by the terms of the parties' contracts, the question of whether the agreement allows or prohibits class arbitration was for the arbitrator to decide.<sup>48</sup>

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<sup>40</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1768 n.4.

<sup>41</sup> *Bazzle*, 539 U.S. at 447.

<sup>42</sup> *Id.* at 448. “. . . [a]ll disputes, claims, or controversies arising from or relating to this contract or the relationships which result from this contract . . . shall be resolved by binding arbitration by one arbitrator selected by us with the consent of you.” *Id.*

<sup>43</sup> *See id.* at 455.

<sup>44</sup> *Id.* at 448.

<sup>45</sup> *Id.* at 450.

<sup>46</sup> *See id.* at 450-51.

<sup>47</sup> *Bazzle*, 539 U.S. at 454.

<sup>48</sup> “In certain limited circumstances, courts assume that the parties intended courts, not arbitrators, to decide a particular arbitration-related matter (in the absence of clear and unmistakable evidence to the contrary). These limited instances typically involve matters of a kind that contracting

Several courts read *Bazzle* narrowly, concluding that it had no precedential value whatsoever.<sup>49</sup> Other courts took a different view of *Bazzle* — namely that the ruling clearly placed with the arbitrator the issue of whether an agreement to arbitrate allows for class arbitration.<sup>50</sup> The Fifth Circuit, for example, decided that *Bazzle* created a precedent requiring an arbitrator, rather than a court, to decide whether an agreement to arbitrate allows for class arbitration.<sup>51</sup> The use of class arbitration accelerated following *Bazzle*. In *Stolt-Nielsen*, however, the court revisited *Bazzle*, perhaps to reverse that trend.

E. *Stolt-Nielsen* - The Court takes a sharp tack and class arbitration changes course

1. Proceeding in the courts below

AnimalFeeds and Stolt-Nielsen were parties to parcel tanker shipping services contracts with broad arbitration clauses.<sup>52</sup> AnimalFeeds alleged that Stolt-Nielsen violated federal antitrust laws by engaging in an effort to restrain competition and corner the world market for parcel tanker shipping services.<sup>53</sup>

The parties agreed that the arbitrators would follow and be bound by Rules 3 through 7 of the American Arbitration

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parties would likely have expected a court to decide. They include 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... The question here — of whether the contracts forbid class arbitration — does not fall into this narrow exception.” *Id.* at 452 (internal citations omitted).

<sup>49</sup> See, e.g., *Employers Ins. Co. of Wausau v. Century Indem. Co.*, 443 F.3d 573, 579-82 (7th Cir. 2006) (concluding that *Bazzle* has no precedential value because no single rationale was endorsed by a majority).

<sup>50</sup> “In the absence of a class action waiver, California law authorizes classwide arbitrations and vests jurisdiction in our trial courts to determine whether in a particular case that approach offer[s] a better, more efficient, and fairer solution than the alternatives. Until last year, we applied these rules to arbitrations governed by the Federal Arbitration Act—but no longer. The Supreme Court has spoken, and the foundational issue—whether a particular arbitration agreement prohibits class arbitrations—must (in FAA cases) henceforth be decided by the arbitrators, not the courts.” *Garcia v. DIRECTV, Inc.*, 115 Cal. App. 4th 297, 298 (Cal. Ct. App. 2004) referring to *Bazzle*, 539 U.S. at 451 (citations omitted).

<sup>51</sup> *Pedcor Mgmt. Co., Inc. Welfare Benefits Plan v. Nations Pers. of Tex., Inc.*, 343 F.3d 355, 358-63 (5th Cir. 2003).

<sup>52</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1764-65.

<sup>53</sup> See *id.* at 1765.

Association's Supplementary Rules for Class Arbitrations.<sup>54</sup> Rule 3 provides that the arbitrator decides whether the arbitration clause allows for class arbitration in a particular instance.<sup>55</sup> The arbitration panel looked at the relevant arbitration clauses and determined that they were silent as to the issue of class arbitration.<sup>56</sup> AnimalFeeds and its co-plaintiffs argued that the class arbitration could—and should—proceed, citing Rule 3 and public policy in addition to claiming the contracts would otherwise be unconscionable.<sup>57</sup> Stolt-Nielsen argued that the silence meant the parties did not intend to allow for class arbitration, citing cases and arbitration decisions and purporting to distinguish decisions cited by AnimalFeeds.<sup>58</sup> Stolt-Nielsen contended that those decisions were distinguishable because they were not international maritime agreements where parties expect bilateral instead of class arbitration as a matter of custom and usage.<sup>59</sup>

The arbitration panel issued a clause construction award, concluding that the agreements and the arbitration clauses allowed for class arbitration.<sup>60</sup> It based the award, in part, on twenty-one other clause construction awards that reached the same conclusion in similar circumstances, though none dealt with international maritime contracts.<sup>61</sup> Stolt-Nielsen petitioned the district court to vacate the panel's award, which it did on grounds of manifest disregard for the law.<sup>62</sup> The court reasoned that the panel failed to do a choice-of-law analysis, which would have revealed that the dispute was governed by federal maritime law controlled by custom and usage, and agreed with Stolt-Nielsen's assertion that maritime arbitration clauses never allow

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<sup>54</sup> *Id.* See also American Arbitration Ass'n, Supplementary Rules for Class Arbitrations (2003), available at <http://adr.org/sp.asp?id=21936> (last visited Mar. 16, 2011) [hereinafter Supplementary Rules].

<sup>55</sup> Supplementary Rules, *supra* note 54. These Supplementary Rules were promulgated in response to the Supreme Court's ruling in *Bazze*, 539 U.S. at 444.

<sup>56</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1765.

<sup>57</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 548 F.3d 85, 89 (2d Cir. 2008) *rev'd Stolt-Nielsen*, 130 S. Ct. 1758.

<sup>58</sup> *Id.*

<sup>59</sup> *Id.*

<sup>60</sup> *Id.* Consistent with the process established by the Supplemental Rules, the panel merely decided that the contracts allowed for class arbitration. It did not certify a class or otherwise proceed with class arbitration. *See id.*

<sup>61</sup> *Id.* at 89-90.

<sup>62</sup> *Id.* at 90.

class arbitration.<sup>63</sup>

The Second Circuit reversed, holding that the high bar for manifest disregard for the law was not met.<sup>64</sup> Manifest disregard of the law requires that the arbitrators: (1) knew of the valid legal principle; (2) appreciated that this principle controlled the outcome of the disputed issue; and (3) nonetheless willfully flouted the governing law by refusing to apply it.<sup>65</sup> The subjective third prong only applies to sources cited and brought to the arbitrator's attention by the parties.<sup>66</sup>

## 2. The Supreme Court's decision in *Stolt-Nielsen*

The Supreme Court reversed, holding 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.”<sup>67</sup> AnimalFeeds had argued that the panel should allow class arbitration because: (1) the clause does not preclude it, and it is allowed under *Bazze*; (2) public policy favors such an outcome; and (3) the clause would otherwise be unconscionable were it to preclude class proceedings.<sup>68</sup> The Court decided that the arbitrators' award was based entirely on public policy considerations.<sup>69</sup>

The Court held that the arbitration panel exceeded its powers by basing its award on public policy,<sup>70</sup> noting that “[i]t is only when [an] arbitrator strays from interpretation and application of the agreement and effectively dispense[s] his own brand of industrial justice that his decision may be unenforceable.”<sup>71</sup> The Court further noted that the parties had stipulated to the arbitration panel that the arbitration clauses were “silent” as to class arbitration, and that “silence” meant that there was no agreement as to that issue by the parties.<sup>72</sup> The panel, however, looked to other arbitration decisions — without

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<sup>63</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 435 F. Supp. 2d 382, 385-87 (S.D.N.Y. 2006).

<sup>64</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1766.

<sup>65</sup> *Stolt-Nielsen S.A.*, 435 F. Supp. 2d at 384.

<sup>66</sup> *See Stolt-Nielsen S.A.*, 548 F.3d at 93.

<sup>67</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1775.

<sup>68</sup> *Id.* at 1768.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.* at 1770.

<sup>71</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1767 (quoting *Major League Baseball Players Ass'n.*, 532 U.S. at 509) (internal quotation marks omitted).

<sup>72</sup> *Id.* at 1766.

analyzing whether those decisions were based on the FAA, New York law, or maritime law — and then purported to fashion a rule that it thought was the best outcome given the particular situation.<sup>73</sup> In doing so, the Court held, the panel exceeded its authority under the arbitration agreement.<sup>74</sup> Therefore, the Court found that section 10(b) of the FAA required it to either direct a rehearing by the arbitrators or decide the question that was posed to the arbitration panel.<sup>75</sup> The Court reasoned that, because only one outcome was possible, no rehearing was necessary.<sup>76</sup>

More significantly, the Court said that the arbitration panel — and the parties themselves — incorrectly interpreted *Bazzle* as controlling precedent.<sup>77</sup> The parties had proceeded as if *Bazzle* required an arbitrator to decide whether a contract permitted class arbitration.<sup>78</sup> However, the Supreme Court disabused them of that notion and pointed out that the Court did not reach a consensus in *Bazzle*.<sup>79</sup> A plurality of the court decided only that an arbitrator, not a court, decides whether an arbitration agreement is silent as to class arbitration.<sup>80</sup> The Court stated that *Bazzle* did not create a rule for deciding whether an arbitration contract permits class arbitration.<sup>81</sup>

3. Following *Stolt-Nielsen*; use of class arbitration to resolve multiple disputes is not a given — class arbitration must be agreed to by all of the parties

The Supreme Court's reading of *Bazzle* is narrow but sound. Some courts read *Bazzle* to espouse the rule that whether an arbitration agreement — silent as to the issue of class arbitration — allows for class arbitration is a matter of contractual interpretation for the arbitrator and not a court.<sup>82</sup> The Supreme Court has said, however, that parties who have interpreted *Bazzle* in such a manner were apparently “baffled” by

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<sup>73</sup> *Id.* at 1768-69.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.* at 1770.

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* at 1772 (noting that *Bazzle* did not reach a majority decision on any of the three questions before the court).

<sup>79</sup> *Id.*

<sup>80</sup> *Id.* at 1771.

<sup>81</sup> *Id.*

<sup>82</sup> See e.g., *Garcia*, 115 Cal. App. 4th at 298 (citing *Bazzle*, 539 U.S. at 451); See also 28 CAUSES OF ACTION 2d 203 (2010).

the decision.<sup>83</sup>

The Supreme Court's treatment of its decision in *Bazzle* was the main focus of *Stolt-Nielsen*. Before *Stolt-Nielsen* it seemed that the Court would have to handle *Bazzle* carefully if it decided to reverse the Second Circuit. But the Court opted for force over finesse in its treatment of *Bazzle*. The Court has now said that *Bazzle* means that the issue of whether an arbitration agreement is silent as to class arbitration is a matter of contractual interpretation for the arbitrator, and that is the extent of the ruling. The Court in *Stolt-Nielsen* addressed the next question: Can an arbitrator decide that an arbitration agreement that is silent as to class arbitration nonetheless allows for it? The short answer is that an arbitrator cannot order a party to proceed with class arbitration unless there is some evidence in the contract that all of the parties have agreed to class arbitration.

### *III. The Fall-out from Stolt-Nielsen – Consumer Class Action Waivers, Unconscionability, and the FAA*

#### A. State courts' unconscionability determination and the impact on waivers of class arbitration

Numerous courts have heard arguments that class arbitration waivers are unconscionable in a consumer setting, at least in circumstances where potential plaintiffs would be unable to vindicate their rights — or would not be sufficiently incentivized to do so — were it not for the class mechanism.<sup>84</sup> Often these cases arise in circumstances where the underlying contracts are uniform agreements styled as contracts of adhesion. There are approximately two hundred appellate court decisions that have dealt with this issue.<sup>85</sup> The cases most in contention involve no-value (or cost-preclusive) consumer claims. These are instances in which a complainant's potential recovery is less than his costs of bringing a claim. Some states, led by California, have invalidated class arbitration waivers in these circumstances as unconscionable because the class arbitration waivers are characterized as exculpatory clauses.<sup>86</sup>

States' unconscionability laws are not uniform. Most states recognize a distinction between procedural and substantive

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<sup>83</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1772.

<sup>84</sup> See generally, 13 A.L.R. 6th 145 (listing cases).

<sup>85</sup> *Id.*

<sup>86</sup> See e.g., *Laster*, 584 F.3d at 853-57.

unconscionability that appears to have its derivation in one law review article.<sup>87</sup> Procedural unconscionability means that the bargaining was one-sided and thus unfair to a party, whereas substantive unconscionability means that the terms of the contract, in whole or in part, are one-sided and unfair.<sup>88</sup> While almost all states have adopted this distinction, courts are split as to whether a plaintiff has to show both procedural and substantive unconscionability in order to invalidate an arbitration agreement.<sup>89</sup> Most courts require both;<sup>90</sup> however, some courts have held that either one alone can be enough or that substantive unconscionability is enough standing alone.<sup>91</sup>

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<sup>87</sup> See generally, Arthur Allen Leff, *Unconscionability and the Code - The Emperor's New Clause*, 115 U. PA. L. REV. 485 (1967).

<sup>88</sup> See e.g., *Belton v. Comcast Cable Holdings, LLC*, 151 Cal. App. 4th 1224, 1245 (Cal. 2007).

<sup>89</sup> 8 WILLISTON ON CONTRACTS § 18:10 (4th ed.).

<sup>90</sup> 21 WILLISTON ON CONTRACTS § 57:15; *BlueCross BlueShield of Ala. v. Rigas*, 923 So. 2d 1077, 1087 (Ala. 2005); *Armendariz v. Foundation Health Psychcare Servs., Inc.*, 6 P.3d 669 (Cal. 2000) (sliding scale); *Voice Stream Wireless Corp. v. U.S. Comms. Inc.*, 912 So. 2d 34 (Fla. Dist. Ct. App. 2005) (sliding scale); *Nec Tech. Inc. v. Nelson*, 478 S.E.2d 769, 773 n.6 (Ga. 1996); *Lovey v. Regence BlueShield of Idaho*, 72 P.3d 877, 882 (Idaho 2003); *In re Marriage of Shanks*, 758 N.W.2d 506, 515 (Iowa 2008); *Freedman v. Comcast Corp.*, 998 A.2d 68, 85 (Md. App. 2010); *Liparoto Const., Inc. v. General Shale Brick, Inc.*, 772 N.W.2d 801, 805 (Mich. App. 2009); *Woods v. QC Fin. Servs., Inc.*, 280 S.W.3d 90, 94 (Mo. App. 2008) (sliding scale); *Myers v. Nebraska Inv. Council*, 724 N.W.2d 776 (Neb. 2006); *D.R. Horton v. Green*, 96 P.3d 1159, 1162 (Nev. 2004) (sliding scale); *Sitogum Holdings, Inc. v. Ropes*, 800 A.2d 915, 921 (N.J. Super. Ct. Ch. Div. 2002); *Tillman v. Comm. Credit Loans, Inc.*, 655 S.E.2d 362, 370 (N.C. 2008); *Praus v. Praus*, 786 N.W.2d 697, 700 (N.D. 2010); *Hayes v. Oakridge Home*, 908 N.E.2d 408, 414 (Ohio 2009); *Wittmer v. Exxon Corp.*, 434 A.2d 1222, 1228 (Pa. 1981); *In re Turner Bros. Trucking Co., Inc.*, 8 S.W.3d 370, 376 (Tex. App. 1999); *Cottonwood Fin., Ltd. v. Estes*, 784 N.W.2d 735, 726 (Wis. App. 2010); *Williams v. Walkier-Thomas Furniture Co.*, 350 F.2d 445, 446-48 (D.C. Cir. 1965).

<sup>91</sup> *Helstrom v. North Slope Borough*, 797 P.2d 1192, 1200 (Alaska 1990) (using a sliding scale and holding substantive is enough); *Maxwell v. Fidelity Fin. Servs., Inc.*, 907 P.2d 51, 59 (Ariz. 1995) (holding substantive is enough); *Hottle v. BDO Seidman LLP*, 846 A.2d 862, 879 (Conn. 2004) (using a sliding scale and holding substantive is enough); *Frank's Maint. & Eng'g, Inc. v. C.A. Roberts Co.*, 408 N.E.2d 403, 409-410 (Ill. App. Ct. 1980) (holding either one is enough); *Remco Enterprises, Inc. v. Houston*, 677 P.2d 567, 572 (Kan. Ct. App. 1984) (holding either one is enough); *Buhrer v. BDO Seidman, LLP*, No. 022190C, 2003 WL 22049503, at \*2 (Super. Ct. Mass. 2003) (using a sliding scale and substantive enough); *Gillman v. Chase Manhattan Bank, N.A.*, 534 N.E.2d 824, 829 (N.Y. Ct. App. 1988) (holding substantive is enough); *Vasquez-Lopez v. Beneficial Oregon, Inc.*, 152 P.3d 940, 948 (Or. Ct. App.

For example, the Ninth Circuit has held that a class action waiver in an arbitration agreement embedded in a consumer contract of adhesion, which involves predictably low dollar amounts of damages, is unconscionable because the consumer needs the class procedure to vindicate his or her rights.<sup>92</sup> The Illinois Supreme Court has held that provisions in arbitration agreements that purport to waive a party's right to bring a class proceeding in arbitration are substantively unconscionable in small value consumer contract claims.<sup>93</sup>

In *Kinkel*, the plaintiff tried to bring a class action against Cingular, her cellular phone service provider.<sup>94</sup> She alleged that Cingular charged an illegal fee for early termination.<sup>95</sup> Cingular moved to compel arbitration under the parties' arbitration agreement, which stated that the arbitrator could not hear class disputes.<sup>96</sup> The appellate court held that the class action waiver was unconscionable but severable from the rest of the arbitration clause, which *was* enforceable.<sup>97</sup> The Illinois Supreme Court affirmed.<sup>98</sup> In rejecting Cingular's conflict preemption argument — namely that Section 2 of the FAA preempted any state statute that would not allow for class action waiver — the Illinois Supreme Court said that when state courts are applying state law to a question of enforceability of a particular contract, they are not required by the FAA “to necessarily reach an outcome that encourages individual arbitration. Further, class arbitration cannot be in conflict with the FAA when the Supreme Court has

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2007) (holding substantive is enough); *Vintage Health Resources, Inc. v. Guiangan*, 309 S.W.3d 448, 461 (Tenn. Ct. App. 2009) (holding either one is enough); *Resource Mgmt. Co. v. Weston Ranch & Livestock Co.*, 706 P.2d 1028, 1043 (Utah 1985) (holding either one is enough); *Tjart v. Smith Barney, Inc.*, 28 P.3d 823, 830 (Wash. Ct. App. 2001) (holding either one is enough); *Arnold v. United Companies Lending Corp.*, 511 S.E.2d 854, 861 (W. Va. 1998) (holding substantive is enough).

<sup>92</sup> *Shroyer v. New Cingular Wireless Servs., Inc.* 498 F.3d 976, 993 (9th Cir. 2007); *but see Guadagno v. E\*Trade Bank*, 592 F. Supp 2d. 1263, 1270 (C.D. Cal 2008) (holding class action waiver in arbitration agreement not unconscionable where the contract was not a contract of adhesion *and* gave the consumer 60 days to opt out).

<sup>93</sup> *Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 278 (Ill. 2006).

<sup>94</sup> *Id.* at 254.

<sup>95</sup> *Id.*

<sup>96</sup> *Id.*

<sup>97</sup> *Kinkel v. Cingular Wireless LLC*, 828 N.E.2d 812, 823 (Ill. App. Ct. 2005).

<sup>98</sup> *Kinkel*, 857 N.E.2d at 250.

recognized the arbitrability of class claims.”<sup>99</sup>

On balance, this entire body of case law may become a legal curiosity in light of the Court’s holding in *Stolt-Nielsen*. Even if litigants “win” a judgment invalidating a class waiver as unconscionable, the class waiver is severable from the rest of the arbitration contract, thereby leaving an arbitration agreement, at best, silent as to class proceedings.<sup>100</sup> *Stolt-Nielsen* did not create an exception that would allow a court to compel arbitration that utilizes the class mechanism without a contractual basis showing that the parties agreed to it, even where that court held an applicable class waiver unconscionable. *Stolt-Nielsen* necessarily means that a defendant cannot be compelled to proceed with class arbitration where the agreement contains a specific waiver of class arbitration.

However, not all courts have found class arbitration agreements unconscionable. In *Jenkins*, the Eleventh Circuit held that agreements between a cash advance business and its borrower customer were valid under the FAA, even though the agreement provided that the customer waived his right to a class action and agreed to arbitrate any dispute arising from the pay-day loans.<sup>101</sup> Also, the Fourth Circuit will enforce contracts, including waiver of a jury and class claims, even when it would lead to a consumer’s inability to proceed with a case because her individual claim is too small.<sup>102</sup> The Third and Seventh Circuits also follow this approach.<sup>103</sup>

#### B. *Laster v. AT&T Mobility LLC*<sup>104</sup>

In *Laster*, the Concepcions were customers of AT&T Mobility LLC (“ATTM”)<sup>105</sup> who purchased cellular phones and cellular phone service as a bundled transaction pursuant to a

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<sup>99</sup> *Id.* at 262 (citing *Bazze*, 539 U.S. at 444).

<sup>100</sup> This assumes that a “blow-out clause” is not in place.

<sup>101</sup> *Jenkins v. First Am. Cash Advance of Ga., LLC*, 400 F.3d 868, 875 (11th Cir. 2005) (reversing the lower court decision and remanding for an arbitrator to decide whether the underlying lending contracts were void ab initio). *See id.* at 883.

<sup>102</sup> *Snowden v. CheckPoint Check Cashing*, 290 F.3d 631, 638 (4th Cir. 2002).

<sup>103</sup> *See Johnson v. Western Suburban Bank*, 225 F.3d at 366, 369 (3d Cir. 2000); *Livingston v. Assoc. Fin., Inc.*, 339 F.3d 553, 559 (7th Cir. 2003).

<sup>104</sup> *Laster*, 584 F.3d at 849.

<sup>105</sup> Actually, the Concepcions were customers of Cingular, but AT&T acquired Cingular Wireless in 2007, renaming it AT&T Mobility.

written contract.<sup>106</sup> ATTM said that the phones were free to people who signed up for service.<sup>107</sup> In accordance with California law, ATTM charged the Concepcions sales tax on the retail value of the two phones, totaling \$30.22.<sup>108</sup> The contract provided that all claims be submitted to arbitration, and it barred class claims in arbitration.<sup>109</sup> In addition, the contract allowed either party to sue in small claims court.<sup>110</sup>

On March 27, 2006, the Concepcions sued ATTM, alleging fraud.<sup>111</sup> The District Court for the Southern District of California consolidated their case with a putative class action covering the same issues, the *Laster* case.<sup>112</sup> In December 2006, ATTM added a “premium payment” clause to its arbitration agreement.<sup>113</sup> This clause provided that, in the event that an arbitrator issues an award in the customer’s favor that is greater than ATTM’s last written settlement offer prior to arbitrator selection, ATTM would pay any customer an amount equal to the value of the maximum claim that may be brought in small claims court in the county of the customer’s billing address.<sup>114</sup> In March 2008, ATTM moved to compel arbitration.<sup>115</sup> The district court denied the motion, holding that the class waiver was unconscionable under California law, which was not preempted by the FAA.<sup>116</sup> The Ninth Circuit upheld that decision.<sup>117</sup>

Under California’s unconscionability law, a provision is unenforceable only if it is both procedurally and substantively unconscionable.<sup>118</sup> California law provides that procedural unconscionability generally arises in uniform contracts, which are

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<sup>106</sup> *Laster*, 584 F.3d at 852.

<sup>107</sup> *Id.*

<sup>108</sup> Brief for Petitioner-Appellant at 9, *AT&T Mobility LLC v. Concepcion*, cert. granted, 130 S. Ct. 3322 (2010) (No. 09-893), 2010 WL 3017755, at \*9 [hereinafter Brief for Petitioner-Appellant] (“California requires that sales tax be paid on the full retail value of a phone when it is sold as part of a bundled transaction.”) (citing CAL. CODE REGS. tit. 18, §§ 1585(a)(4), (b)(3)).

<sup>109</sup> *Id.* at 852-53.

<sup>110</sup> *Laster v. T-Mobile USA, Inc.*, No. 05cv1167 DMS, 2008 WL 5216255, at \*2 (S.D. Cal. 2008).

<sup>111</sup> *Id.* at 853.

<sup>112</sup> *Id.*

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> *Id.*

<sup>116</sup> *Id.*

<sup>117</sup> *Id.* at 852.

<sup>118</sup> *Id.* at 853.

characterized as adhesion contracts, whereas substantive unconscionability arises when there are harsh, one-sided terms.<sup>119</sup> California uses a “sliding-scale” approach towards unenforceability, which allows for less procedural unconscionability in a contract where there is more substantive unconscionability, and vice versa.<sup>120</sup>

In *Discover Bank*,<sup>121</sup> the California Supreme Court developed what has been interpreted as a “three-part test” to determine whether a class action waiver in a consumer contract is unconscionable: (1) whether the agreement is a contract of adhesion; (2) whether the disputes between the contracting parties likely involve small amounts of damages; and (3) whether it is alleged that the party with superior bargaining power has carried out a scheme deliberately to cheat large numbers of consumers out of individually small sums of money.<sup>122</sup> The *Discover Bank* rule is grounded in a California exculpatory clause statute, which states that “contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud . . . are against the policy of the law.”<sup>123</sup> A party does not need to prove all three elements to prevail.<sup>124</sup> However, the Ninth Circuit held that all three were present in this case.<sup>125</sup>

The Ninth Circuit also rejected ATTM’s argument that the premium payment sanitized the class waiver provision.<sup>126</sup> ATTM asserted that its contract and agreement to arbitrate are not aimed at disputes with predictably small amounts of damages, as required by *Discover Bank*, because ATTM has itself provided for larger recoveries with its premium payment clause.<sup>127</sup>

Here, ATTM contended that a \$7,500 premium payment (where plaintiffs only claimed \$30.22 in actual damages) sufficiently incentivized would-be plaintiffs to bring claims and sufficiently deterred ATTM from engaging in wrongful

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<sup>119</sup> *Id.*

<sup>120</sup> *Id.*

<sup>121</sup> *Discover Bank v. Superior Court*, 113 P.3d 1100 (Cal. 2008).

<sup>122</sup> *Laster*, 584 F.3d at 854 (citing *Shroyer*, 498 F.3d at 983).

<sup>123</sup> CAL. CIV. CODE § 1668 (West 2010).

<sup>124</sup> *Laster*, 584 F.3d at 854 (noting that there are circumstances where a provision is unconscionable even without meeting all three requirements).

<sup>125</sup> *Id.*

<sup>126</sup> *Id.* at 855.

<sup>127</sup> *Id.*

conduct.<sup>128</sup> The court disagreed, stating that “the premium payment provision does not transform a \$30.22 case into a predictable \$7,500 case.”<sup>129</sup> The court predicted ATTM would simply pay the face value of the customer claim, rather than contesting it and risking \$7,500.<sup>130</sup> Thus, the court reasoned that ATTM could cheat numerous customers out of small sums while keeping its liability to a minimum.

The court went on to state that the provision essentially “guarantee[s] that the company will make any aggrieved customer whole who files a claim. Although this is, in and of itself, a good thing, the problem with it under California law—as we read that law—is that not every aggrieved customer will file a claim.”<sup>131</sup> The Ninth Circuit determined that the FAA did not preempt California unconscionability law relating to class arbitration waivers in consumer adhesion contracts.<sup>132</sup>

The Ninth Circuit also held that the FAA does not expressly preempt California unconscionability law related to class waivers in consumer contracts of adhesion.<sup>133</sup> The FAA expressly preempts state laws that allow for a revocation of an arbitration agreement but does not allow for a revocation of a contract generally.<sup>134</sup> ATTM argued that *Discover Bank* created a new rule that does not apply to contracts generally, but instead targets arbitration clauses for invalidation.<sup>135</sup> The court rejected that argument, stating that *Discover Bank* was simply a refinement of California’s sliding-scale approach to unconscionability law, the difference being that *Discover Bank* applied the sliding-scale in the class waiver setting.<sup>136</sup> The *Discover Bank* rule states, “if a contract clause is, in practice, exculpatory, as long as there is any degree of procedural unconscionability, the element of substantive unconscionability is generally adequate, as a matter of law.”<sup>137</sup> In *Shroyer*, the court had previously rejected the argument that *Discover Bank* exposes arbitration agreements to special scrutiny.<sup>138</sup>

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<sup>128</sup> *Id.*

<sup>129</sup> *Id.*

<sup>130</sup> *Id.* at 856.

<sup>131</sup> *Id.* at 856 n.9.

<sup>132</sup> *Id.* at 856-59.

<sup>133</sup> *Id.* at 857.

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> *Id.*

<sup>137</sup> *Id.*

<sup>138</sup> *Id.* (citing *Shroyer*, 498 F.3d at 987).

The court also stated that the FAA did not impliedly preempt California unconscionability law.<sup>139</sup> The purposes of the FAA are two-fold: “to reverse judicial hostility to arbitration agreements by placing them on the same footing as any other contract, and second, to promote the efficient and expeditious resolution of claims.”<sup>140</sup> The court stated that California unconscionability law does not offend either of these purposes.<sup>141</sup>

Lastly, ATTM argued that the Supreme Court’s decision in *Preston*<sup>142</sup> superseded *Shroyer*, but the court rejected this argument as well. The court distinguished *Preston* from the case before it on the grounds that *Preston* involved a challenge to the contract’s validity as a whole, whereas this challenge was specific to the arbitration clause.<sup>143</sup>

### C. The Supreme Court confronts the issues in *Concepcion*

#### 1. ATTM’s Argument<sup>144</sup>

ATTM argued before the Court that the FAA preempts California’s *Discover Bank*<sup>145</sup> rule.<sup>146</sup> The main policy of the FAA is to ensure that agreements to arbitrate are enforced according to their terms. Congress enacted the FAA to overcome the very judicial hostility to arbitration that is inherent in California’s purported rule of unconscionability law that applies to arbitration agreements alone.

ATTM, as Petitioner, argued that the FAA allows for invalidation of arbitration agreements on limited grounds.<sup>147</sup> Section 2 of the FAA provides that an arbitration agreement may be revoked on grounds that exist at law or in equity for the revocation of any contract.<sup>148</sup> Petitioner also argued that, because California’s rule only applies to arbitration agreements, the rule is not one for the revocation of any contract.<sup>149</sup> Further, Petitioner notes that the terms of *this* arbitration agreement are

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<sup>139</sup> *Id.*

<sup>140</sup> *Id.*

<sup>141</sup> *Id.*

<sup>142</sup> *Preston*, 552 U.S. at 346.

<sup>143</sup> *Laster* 584 F.3d at 859.

<sup>144</sup> Brief for Petitioner-Appellant, *supra* note 108.

<sup>145</sup> *Discover Bank*, 113 P.3d at 1103.

<sup>146</sup> Brief for Petitioner-Appellant, *supra* note 108, at 2.

<sup>147</sup> *Id.* at 15-16.

<sup>148</sup> Federal Arbitration Act, 9 U.S.C. § 2 (2009).

<sup>149</sup> Brief for Petitioner-Appellant, *supra* note 108, at 17.

fair.<sup>150</sup> Indeed, with the exception of a class proceeding, the arbitration agreement provides just about every conceivable consumer-friendly dispute amenity.<sup>151</sup>

Petitioner asserted that if the Ninth Circuit's decision in this case were upheld, it would signify the end of arbitration of consumer disputes in California.<sup>152</sup> Class arbitration combines the worst elements of arbitration and litigation to form a process that no business would enter voluntarily — it is a high cost and high stakes process leading to an award with uncertain preclusive effect on class members and subject to extreme limitations on review.<sup>153</sup> If the price of having an arbitration agreement includes the possibility of being dragged into class arbitrations, companies will likely abandon arbitration.<sup>154</sup>

## 2. The Concepcions' argument<sup>155</sup>

The Concepcions' core argument is that the FAA does not preempt the California rule of unconscionability that invalidated the class waiver provision because California's unconscionability law is, under Section 2, a ground for the revocation of any contract and does not discriminate against arbitration agreements.<sup>156</sup> Courts have applied the general contract law of at least twenty states to invalidate class waivers in arbitration contracts.<sup>157</sup> The Concepcions also argue that the California rule applies outside the context of arbitration.<sup>158</sup> In fact, the first California appellate decision dealing with unconscionability of

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<sup>150</sup> *Id.* at 19.

<sup>151</sup> The arbitration agreement provides that ATTM pays all arbitration fees of the customer for non-frivolous claims; the arbitration venue is designed for the customer's convenience; a customer can choose to bring a claim in small claims court; full remedies are available in arbitration; there is no confidentiality requirement; if the arbitrator awards an amount to the customer exceeding ATTM's last written settlement offer, then the customer is guaranteed at least \$7,500 and double attorney's fees; and ATTM will never seek attorney's fees even when entitled to do so. *See id.* at 5-7.

<sup>152</sup> *See id.* at 56.

<sup>153</sup> *See id.* at 53-55.

<sup>154</sup> *See id.* at 55-56.

<sup>155</sup> Brief for Respondents-Appellees, *AT&T Mobility LLC v. Concepcion*, cert. granted, 130 S. Ct. 3322 (2010) (No. 09-893), 2010 WL 4411292 [hereinafter Brief for Respondents-Appellees].

<sup>156</sup> *Id.* at 12.

<sup>157</sup> *Id.* at 18.

<sup>158</sup> *See id.* at 21.

class waivers was *America Online*<sup>159</sup> — a case that did not involve arbitration.<sup>160</sup>

In *America Online*, the court determined that the California consumer protection law<sup>161</sup> allowed for class actions, but that the comparable Virginia law<sup>162</sup> did not.<sup>163</sup> Further, the court held that class actions are of great importance in California law, and that the lack of access to the class mechanism was enough to render unenforceable the forum selection clause in the America Online Terms of Service Agreement.<sup>164</sup>

Respondents also noted that the amount of consumers actually using this allegedly pro-consumer arbitration process is very low, despite the fact that AT&T has the worst customer satisfaction rating in an industry that generates more consumer complaints than any other.

#### *IV. Was the Ninth Circuit Decision in Accord With Supreme Court Precedent Prior to Stolt-Nielsen?*

##### A. Is there a special rule for consumer contracts?

The Court in *Stolt-Nielsen* held that an arbitration clause that is silent as to the issue of class arbitration is precluded in the absence of any contractual evidence of the parties' intent to allow for class arbitration.<sup>165</sup> The Court has stated that any arbitration

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<sup>159</sup> *America Online, Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699 (Cal. Ct. App. 2001). Former subscribers of America Online ("AOL") filed a class action against the company, alleging that AOL improperly debited their credit cards for monthly service fees after the class members had terminated their subscriptions. The Terms of Service Agreement ("TOS") between the subscribers and AOL designated Virginia courts as the exclusive venue and Virginia law as applicable law for any dispute. The class alleged that the TOS was unenforceable as an unconscionable contract of adhesion. The *America Online* court stated that California law "favors forum selection agreements only so long as they are procured freely and voluntarily, with the place chosen having some logical nexus to one of the parties or the dispute, and so long as California consumers will not find their substantial legal rights significantly impaired by their enforcement. Therefore, to be enforceable, the selected jurisdiction must be 'suitable,' 'available,' and able to 'accomplish substantial justice.'" *Id.* at 707.

<sup>160</sup> See Brief for Respondents-Appellees, *supra* note 155, at 22.

<sup>161</sup> CAL. CIVIL CODE §§ 1752, 1781 (West 2010).

<sup>162</sup> VA. CODE ANN., § 59.1-203 (West 2008).

<sup>163</sup> *America Online, Inc.*, 108 Cal. Rptr. 2d at 710-12.

<sup>164</sup> *Id.* at 712.

<sup>165</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1777.

contract that does not speak to class arbitration contains an implied waiver of the ability of a party to avail itself of the class mechanism because the contract does not contain evidence of the parties' intent to allow for it. Moreover, where the agreement contains a specific waiver, there is no plausible argument that the parties agreed to class arbitration.

However, should there be a special rule that governs consumer arbitration? Can consumers say that this rule cannot apply to them because they have a compelling reason, i.e., they are consumers dealing with sophisticated companies and are compelled to accept contracts of adhesion? Moreover, because only small damage claims may accrue to businesses that deal with consumers, the only practical recourse available to consumers is through a class proceeding. Ultimately, the argument is reduced to the proposition that unless companies agree to class arbitration, no arbitration process can be used in a consumer setting.

The Court, however, has spoken on this issue:

§2 gives States a method for protecting consumers against unfair pressure to agree to a contract with an unwanted arbitration provision. States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause “upon such grounds as exist at law or in equity for the revocation of *any* contract.” 9 U.S.C. § 2 (emphasis added). What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal “footing,” directly contrary to the Act’s language and Congress’ intent.<sup>166</sup>

#### B. Does *Preston* forecast a possible outcome?

In *Preston*, the Court held that “when parties agree to arbitrate all questions arising under a contract, state laws lodging primary jurisdiction in another forum, whether judicial or administrative, are superseded by the FAA.”<sup>167</sup> A broader

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<sup>166</sup> *Allied-Bruce Terminix Cos., Inc.*, 513 U.S. at 281.

<sup>167</sup> *Preston*, 552 U.S. at 349-350.

reading of *Preston* is that the FAA preempts a state law that undermines a primary objective of an arbitration agreement such as “achieving streamlined proceedings and expeditious results.”<sup>168</sup>

In *Preston*,<sup>169</sup> an attorney, Preston, contracted to represent Ferrer, an entertainer, in some capacity.<sup>170</sup> The contract to render services contained an arbitration clause, specifying American Arbitration Association (“AAA”) rules.<sup>171</sup> Preston later demanded arbitration over unpaid fees, and Ferrer petitioned the California Labor Commissioner (“CLC”) to declare their contract void on grounds that Preston had been acting as a talent agent without a license.<sup>172</sup> The CLC’s officer denied the motion on grounds that the CLC did not have the authority to grant the relief sought.<sup>173</sup> Ferrer filed in state court, seeking a declaration that the dispute as to the validity of the contract was not subject to arbitration.<sup>174</sup> Ferrer moved for an injunction to stop arbitration proceedings.<sup>175</sup> Preston moved to compel arbitration.<sup>176</sup>

The superior court denied Preston’s motion and enjoined Preston from proceeding with arbitration unless and until the Labor Commissioner determined she did not have jurisdiction.<sup>177</sup> While Preston’s appeal was pending, the Supreme Court’s decision in *Buckeye* came down, holding that “challenges to the validity of a contract providing for arbitration ordinarily ‘should . . . be considered by an arbitrator, not a court.’”<sup>178</sup>

The California appeals court affirmed, holding that the California Talent Agencies Act<sup>179</sup> (“TAA”) vested exclusive jurisdiction in the Labor Commissioner, and that *Buckeye* was inapplicable because it did not involve an administrative agency with exclusive jurisdiction over the dispute.<sup>180</sup> The California Supreme Court denied review.<sup>181</sup> The United States Supreme

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<sup>168</sup> *Id.* at 357-58 (quoting *Mitsubishi Motors Corp.*, 473 U.S. at 614, 633).

<sup>169</sup> *Id.* at 350.

<sup>170</sup> *Id.*

<sup>171</sup> *Id.*

<sup>172</sup> *Id.*

<sup>173</sup> *Id.*

<sup>174</sup> *Id.*

<sup>175</sup> *Id.* at 351.

<sup>176</sup> *Id.*

<sup>177</sup> *Id.*

<sup>178</sup> *Id.* (quoting *Buckeye*, 546 U.S. at 446).

<sup>179</sup> CAL. LAB. CODE §§ 1700-1700.47 (West 2003 & Supp. 2008).

<sup>180</sup> *Preston*, 552 U.S. at 351.

<sup>181</sup> *Id.*

Court, however, granted certiorari “to determine whether the FAA overrides a state law vesting initial adjudicatory authority in an administrative agency.”<sup>182</sup>

Ferrer claimed Preston acted as his talent agent without a license, thereby making the contract void and entitling Preston to no compensation.<sup>183</sup> Conversely, Preston argued that he acted as a personal manager, not a talent agent, and that the contract was valid, fees were due, and the TAA did not apply.<sup>184</sup> Preston contended that Ferrer had to argue his TAA defense in arbitration.<sup>185</sup> Ferrer insisted that, under California law, the proceeding was within the jurisdiction of the Labor Commissioner.<sup>186</sup> The Court stated, however, that “[t]he dispositive issue . . . contrary to Ferrer’s suggestion, is not whether the FAA preempts the TAA wholesale. The FAA plainly has no such destructive aim or effect. Instead, the question is simply who decides whether Preston acted as a personal manager or as talent agent.”<sup>187</sup>

The Court noted that, as it held in *Southland*, the national policy favoring arbitration of claims where parties have agreed to arbitrate applies in both, state and federal courts, and blocks state legislatures from undermining arbitration agreements.<sup>188</sup> The FAA displaces state law to the contrary.<sup>189</sup> The question arises: Who decides whether grounds exist at law or in equity for the revocation of any contract? An arbitrator will address this issue when the challenge is to the contract as a whole, while a court will address the issue when the challenge is to the arbitration clause alone.<sup>190</sup> The rule applies in state court too,<sup>191</sup> despite its federal court origins.<sup>192</sup> The Court adhered to *Buckeye* and determined that the decision is one for an arbitrator to decide because the contract was within Section 2 and because Ferrer challenged the validity of the whole contract.<sup>193</sup>

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<sup>182</sup> *Id.* at 351-52.

<sup>183</sup> *Id.* at 352.

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> *Id.*

<sup>187</sup> *Id.* (citation omitted).

<sup>188</sup> *Id.* at 353.

<sup>189</sup> *Id.*

<sup>190</sup> *Id.*

<sup>191</sup> *Preston*, 552 U.S. at 353. (citing *Buckeye*, 546 U.S. at 447-48).

<sup>192</sup> *See* *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 403-04 (1967).

<sup>193</sup> *Id.* at 354.

The Court further noted that that the TAA's procedural prescriptions conflicted with the FAA's dispute resolution in two ways: "First, the TAA . . . grants the Labor Commissioner exclusive jurisdiction to decide an issue that the parties agreed to arbitrate; second, the TAA . . . imposes prerequisites to enforcement of an arbitration agreement that are not applicable to contracts generally."<sup>194</sup>

The Court rejected Ferrer's contention that arbitration would be merely postponed under TAA guidelines, thus making the TAA compatible with the FAA.<sup>195</sup> The Court reasoned that if arbitration occurred at all, it "would likely be long delayed, in contravention of Congress' intent 'to move the parties to an arbitrable dispute out of court and into arbitration as quickly and easily as possible.'"<sup>196</sup> The Court noted that "[a] prime objective of an agreement to arbitrate is to achieve 'streamlined proceedings and expeditious results.'"<sup>197</sup>

Ferrer contended that allowing parties to proceed directly to arbitration would undermine the Labor Commissioner's ability to stay informed of potentially illegal activity and would deprive artists who are protected by the TAA of the Labor Commissioner's expertise.<sup>198</sup> The Court, however, noted that the involvement of an agency does not limit parties' ability to contract for arbitration, and administrative agencies can still prosecute companies in their own name.<sup>199</sup>

The Court in *Preston* concluded that the underlying issue was merely a question concerning the proper forum in which the parties' dispute would be heard.<sup>200</sup> *Preston* did not give up any substantive statutory rights by submitting his dispute to arbitration in accordance with the arbitration agreement that he signed.<sup>201</sup> The Court disapproved of Ferrer's distinction between judicial and administrative proceedings that was adopted by the appeals court.<sup>202</sup> The Court stated that "[w]hen parties agree to arbitrate all questions arising under a contract, the FAA

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<sup>194</sup> *Id.* at 356 (citation omitted).

<sup>195</sup> *Id.* at 358.

<sup>196</sup> *Id.* (quoting *Moses H. Cone Memorial Hosp.*, 460 U.S. at 22).

<sup>197</sup> *Id.* at 357 (citing *Mitsubishi Motors Corp.*, 473 U.S. at 633; *Allied-Bruce Terminix Cos., Inc.*, 513 U.S. at 278; *Southland Corp.*, 465 U.S. at 7).

<sup>198</sup> *Id.* at 358.

<sup>199</sup> *Id.*

<sup>200</sup> *Id.* at 359.

<sup>201</sup> *Id.*

<sup>202</sup> *Id.*

supersedes state laws lodging primary jurisdiction in another forum, whether judicial or administrative.”<sup>203</sup>

*Preston* could be read to denote that the FAA preempts any state law that would frustrate a major purpose of arbitration contracts — speedy dispute resolution. This is the essential argument Petitioner makes in *Concepcion*. More significantly, in *Preston*, the Court does not defer to important California public policy considerations when those public policy considerations come into conflict with the FAA.

*V. Does the Court’s Action in American Express Merchants’ Litigation Suggest an Outcome?*

*American Express Merchants’ Litigation* is a commercial class action antitrust case brought by credit card merchants.<sup>204</sup> The agreement between American Express and the plaintiff merchants contained an arbitration provision and a class action waiver.<sup>205</sup> In *American Express*, the plaintiffs showed that the median damages available under the Clayton Act for individual class members was a modest \$1,751.<sup>206</sup> Plaintiffs also presented evidence that antitrust cases require extensive expert analysis costing anywhere from three hundred thousand dollars to in excess of one million dollars.<sup>207</sup> Plaintiffs further showed that expert fees were not recoverable under the Clayton Act, and that the arbitration agreement in question did not provide for the recovery of such fees.<sup>208</sup> The Second Circuit concluded that, given the low value of individual class members’ potential recovery and the unrecoverable expert fees, individual claims were, as a practical matter, precluded.<sup>209</sup> Based on these facts, the Second Circuit ruled that the class action waiver was unenforceable because it effectively served “to grant Amex *de facto* immunity from antitrust liability.”<sup>210</sup> The court stated:

[W]e stress that we do not hold here that class action

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<sup>203</sup> *Id.*

<sup>204</sup> *In Re American Express Merchants’ Litigation*, 554 F.3d 300 (2d Cir. 2009), *vacated and remanded sub nom.*, 130 S. Ct. 2401 (2010).

<sup>205</sup> *Id.* at 305.

<sup>206</sup> *Id.* at 317.

<sup>207</sup> *Id.* at 316.

<sup>208</sup> *See id.* at 317-18.

<sup>209</sup> *See id.* at 320. <sup>209</sup> *See also, generally, Handbook on Arbitration Practice*, American Arbitration Association 2010, at 155.

<sup>210</sup> *Id.* at 320.

waivers in arbitration agreements are *per se* unenforceable. We also do not hold that they are *per se* unenforceable in the context of antitrust actions. Rather, we hold that *each* case which presents a question of enforceability of a class action waiver in an arbitration agreement must be considered on its own merits, governed with a healthy regard for the fact that the FAA ‘is a congressional declaration of a liberal federal policy favoring arbitration agreement.’<sup>211</sup>

In May 2009 American Express filed a certiorari petition in the *American Express Merchants’ Litigation*. On May 3, 2010 the Court issued a summary order in *American Express Co. v. Italian Colors Restaurant*,<sup>212</sup> granting certiorari, summarily vacating the Second Circuit judgment, and remanding it “for further consideration in light of” *Stolt-Nielsen*.<sup>213</sup> It is unclear why the Court vacated the judgment. Perhaps the Court believed the waiver was, in fact, enforceable or perhaps there was some other unexplained reason related to the Court’s decision in *Stolt-Nielsen*.

#### VI. Conclusion

It is always dangerous to predict how the Court will decide any particular matter. However, in *Concepcion*, there is ample Supreme Court jurisprudence supporting the validation of the ATTM arbitration agreement, including the class action waiver. Moreover, it can be argued that consumers would not benefit from a decision that precludes them from agreeing to arbitration and contracting away the right to institute class proceedings. Class actions — be they in court or in front of an arbitrator — do not routinely vindicate the rights of members of the class in an effective manner. Certainly, arbitration panels are free to certify classes that would raise the cost of doing business for those companies that deal with large numbers of consumers, who would subsequently pass that cost on to all consumers.

American business, while far from pristine in its approach to doing business with consumers, has improved its performance significantly. In *Concepcion*, the ATTM agreement is very fair to

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<sup>211</sup> *Id.* at 321.

<sup>212</sup> 130 S. Ct. 2401 (2010) (summary disposition).

<sup>213</sup> *See id.*

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the individual consumer, as indicated by the Ninth Circuit.<sup>214</sup> Moreover, it has been noted that terms in consumer contracts have recently shifted from those that favor the business—such as those that prohibit punitive damages and attorneys’ fees, require arbitration to proceed in a remote location, require the consumer to pay half or all of the arbitration fees, or give the company the sole authority to select the arbitrator—to those terms that fall under the guiding principle of “fairness to the consumer.”<sup>215</sup>

While it is accurate to acknowledge that consumer class actions complement government efforts against bad business practices, it may not make sense to make such a policy evergreen when fairness for the individual consumer is achieved. Ultimately, giving arbitration the opportunity to show that it has significant potential advantages in resolving consumer disputes may make for sound long-term policy.

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<sup>214</sup> *Laster* 584 F.3d at 856 n.9.

<sup>215</sup> Ramona L. Lampley, *Is Arbitration Under Attack?: Exploring the Recent Judicial Skepticism of the Class Arbitration Waiver and Innovative Solutions to the Unsettled Legal Landscape*, 18 CORNELL J.L. & PUB. POL’Y 477, 503-04 (2009).