OUTSIDE PERSPECTIVES

The Death of Consumer Class Actions?

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ON APRIL 27, 2011, THE UNITED STATES Supreme Court issued its ruling in *AT&T Mobility LLC v. Concepcion*, holding that arbitration clauses in consumer contracts that prohibit class-wide litigation or arbitration are enforceable under the Federal Arbitration Act and that state laws prohibiting these clauses are preempted by federal law. Some commentators have declared that this ruling will result in the death of consumer class actions. While that is unlikely, there is no doubt that this ruling will dramatically change the landscape of consumer litigation and will, for the time being, permit many businesses to limit, if not avoid, exposure to class action lawsuits.

The *Concepcion* case involved a contract under which AT&T Mobility provided Vincent and Liza Concepcion with both cellular service and a free cell phone. This contract required that all disputes be resolved through arbitration brought in the parties' "individual capacity, and not as a plaintiff or class member in any purported class or representative proceeding." The contract also provided that AT&T Mobility would pay for all arbitration costs for non-frivolous claims; that the arbitration must take place in the county in which the customer is billed; that for claims of $10,000 or less the customer could choose how the arbitration would be conducted (in person, by telephone, or based solely upon the documents); that either party could bring individual lawsuits in small claims court in lieu of arbitration; and that the arbitrator may award any form of individual relief, including injunctions and punitive damages. The contract also prohibited AT&T Mobility from seeking reimbursement of its attorney's fees and, in the event that a customer receives an arbitration award greater than AT&T Mobility's last written settlement offer, AT&T Mobility was required to pay a $7,500 minimum recovery and twice the amount of the claimant's attorney fees.

The Concepcions received their free cell phone but were charged $30.22 in sales tax based on the phone's retail value. Several years later, they brought a class action lawsuit against AT&T Mobility in the United States District Court for the Southern District of California, alleging that AT&T Mobility engaged in false advertising and fraud by charging sales tax on cell phones that it advertised as being free. AT&T Mobility moved to compel arbitration under the terms of its contract. The Concepcions opposed that motion, arguing that under California law the arbitration agreement was unconscionable and unenforceable because it disallowed class action procedures in the arbitration. Although the district court found that AT&T Mobility's arbitration agreement was "quick, easy to use," that it would likely to result in full, or even excess, payments to customers and that class members would actually be worse off through the class action, it nonetheless held that the arbitration clause was unconscionable and therefore refused to compel arbitration. The district court's ruling was affirmed by the United States Court of Appeals for the Ninth Circuit.

The Supreme Court Strikes Down Attempts to Ban Class Action Waivers

The United States Supreme Court reversed the district court's and the Ninth Circuit's rulings, holding that the Federal Arbitration Act ("FAA") preempted the California rule prohibiting class action waivers in arbitration agreements. The FAA was enacted in response to widespread judicial hostility to arbitration agreements and therefore provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." While this statute reflects a liberal federal policy favoring arbitration, it nonetheless permits courts to find arbitration agreements invalid on grounds applicable to any contract, such as fraud, duress, or unconscionability. The Supreme Court stated that the FAA prohibits courts from invalidating arbitration agreements based on

state-law contract defenses that apply only to arbitrations or that derive their meaning from the fact that an agreement to arbitrate is at issue. The Concepcions argued that the California rule prohibiting class action waivers as unconscionable was permitted under the FAA because unconscionability is a ground that "exists at law or in equity for the revocation of any contract." The Supreme Court rejected this argument, finding that the application of the unconscionability rule in this particular context would require parties to engage in class-wide arbitration even when the applicable arbitration agreement did not permit it or provide for it. The Supreme Court noted that the "principal purpose" of the FAA was to ensure that arbitration agreements are enforced according to their terms. As such, parties are able to limit the issues subject to arbitration, to specify the rules applicable to the arbitration, and to limit with whom a party will arbitrate its disputes. Class-action arbitration, to the extent that it is *imposed* on the parties by the California rule rather than by *agreement* of the parties, is inconsistent with purpose of the FAA. Therefore, the Supreme Court held that arbitration clauses that prohibit class action lawsuits and arbitrations are valid and enforceable, and that state laws to the contrary are preempted by the FAA.

Businesses Should Consider Adding Class Action Waivers to Their Arbitration Agreements

While it is doubtful that this ruling is the death knell of consumer class action lawsuits, it is certain that the ruling will permit businesses to add arbitration clauses to their consumer contracts that prohibit most class action lawsuits. Prior to this ruling, courts in a number of states, including California, struck down arbitration agreements that included class action waivers as being unconscionable because a class action lawsuit may be the only practical way to remedy a wrong that "cheats large numbers of consumers out of individually small sums of money." As a result of the Supreme Court's ruling, every state must now enforce arbitration agreements that include class action waivers. This ruling is not the last word on this issue, however, and there are at least two ways in which these arbitration agreements might be struck down in the future. First, courts still have the authority under the FAA to invalidate arbitration agreements on the ground of unconscionability if the agreements are drafted in a manner that impose undue burdens on consumers that prevent them from pursuing their claims or if the agreements improperly limit the relief a consumer can obtain through arbitration. For example, an arbitration agreement that requires the arbitration to take place in a state other than that where the customer lives or which places an artificially low dollar limit on a customer's recovery will likely be held to be unenforceable. The Supreme Court's ruling is also subject to the mandates of federal law. The Supreme Court only held that *state laws* prohibiting class action waivers were preempted by the FAA. Federal laws and regulations that limit or prohibit class action waivers are unaffected by this ruling. For example, the Dodd-Frank Wall Street Reform and Consumer Protection Act gives both the Securities Exchange Commission and the newly-created Bureau of Consumer Financial Protection the power to regulate arbitration agreements in securities and consumer finance contracts. Either agency may in the future issue regulations that limit or prohibit the use of arbitration agreements or class action waivers. There are also bills pending in Congress that, if enacted, would prohibit the use of arbitration agreements in employment, consumer, and franchise contracts. While it is unclear what these agencies or Congress will do, the Supreme Court's ruling permits companies to take action now to reduce the likelihood of being defendants in class action lawsuits.

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