A Timely Analysis of Legal Developments

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The U.S. Supreme Court in *AT&T Mobility L.L.C. v. Concepcion* has held that an arbitration agreement covered by the Federal Arbitration Act does not violate public policy because it disallows classwide proceedings. The Court's decision explicitly overrules the California Supreme Court decision in *Discover Bank v. Superior Court* where the California court found that a consumer arbitration agreement that prohibited class arbitrations was unconscionable and therefore unenforceable.

Supreme Court Finds California Class Action Arbitration Waiver Enforceable

By Henry Lederman

Can a state declare that an arbitration agreement covered by the Federal Arbitration Act ("FAA") violates public policy because it disallows classwide proceedings? In *AT&T Mobility LLC v. Concepcion*, No. 09-893 (Apr. 27, 2011), the United States Supreme Court answered "No." Such laws, the Court held, whether made by a state legislature or court, stand as an obstacle to the enforcement of arbitration agreements in accordance with their terms, which is the primary requirement of the FAA. As such, those laws are preempted.

The Supreme Court's Decision

The Court's decision in *Concepcion* overrules the California Supreme Court's decision in *Discover Bank v. Superior Court*.[1] In that case, the California court found a consumer arbitration agreement that forbade class arbitrations was unconscionable because individual bilateral arbitration was not an adequate substitute for the deterrent effects of class actions where, as in that case, the amount of damages was predictably small. In effect, the California Supreme Court held, by requiring individuals to arbitrate their small individual claims only, and not classwide, in an agreement that was nonnegotiable, the company was imposing an illegal exculpatory contract on the weaker party.

The Court rejected this rationale as a basis for refusing to enforce an agreement in accordance with its terms. The 5-4 majority, in an opinion authored by Justice Scalia, dismantled the various rationales supporting the *Discover Bank* rule. The Court concluded that it was improper for the California court to impose class arbitration where the agreement did not permit it. These state law rules stood as an obstacle to the accomplishment of the FAA's objectives, primarily to enforce agreements as written, and simply cannot stand, as the main goal of arbitration is to "facilitate streamlined proceedings," and class arbitrations, the Court observed, were anything but. The Court concluded "[r] equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA."

Concomitantly, the Court also recognized another key feature of arbitration, which is "that parties may agree to limit the issues subject to arbitration . . . and to limit *with whom* a party will arbitrate its disputes. . . ." Thus, it is the "informality of arbitral

proceedings [that] is itself desirable, reducing the cost and increasing the speed of dispute resolution." Class arbitration foisted upon unwilling parties was inconsistent with that goal.

In this regard, the Court found that the *Discover Bank* rule interfered with arbitration because it allowed a consumer *after the fact of contract formation* to demand a class arbitration even though the contract forbade it. It further rejected the dichotomy between adhesive and non-adhesive contracts that formed an underpinning of the California Supreme Court's rule because "the times in which consumer contracts were anything other than adhesive are long passed." As the Court observed, even without classwide arbitration, consumers were "free to bring and resolve their disputes on a bilateral basis," but with the availability of classwide arbitration as mandated by the *Discover Bank* rule, the Court found there was "little incentive for lawyers to arbitrate on behalf of individuals when they may do so for a class and reap far higher fees in the process." In sum, "[t]he conclusion follows that class arbitration, to the extent it is manufactured by *Discover Bank* rather than consensual, is inconsistent with the FAA."

What Does This Mean for Employment Arbitration Agreements?

Employers therefore will ask what does this case mean for us? *Concepcion*, after all, was a consumer case, not an employment case. In short, however, it appears that *Concepcion* could be a game-changer in the area of employment class actions.

In *Gentry v. Superior Court*,[2] the California Supreme Court applied and expanded upon the now preempted *Discover Bank* rule in determining that individual wage and hour claims and associated penalties were likely too small to justify enforcement of an express class action waiver. In addition to the *Discover Bank* "size of claim" factor, however, *Gentry* required consideration of other factors external to the parties' agreement before enforcing a contractual class waiver. The *Gentry* court, thus, additionally required consideration of absent class members' awareness of their rights, whether these individuals might fear retaliation if they sued on their own, and an unspecified range of other factors that courts may review when faced with a clause in an employment arbitration agreement that forbade class arbitrations.

It is difficult to see how the *Gentry* rules, yet additional obstacles themselves to the enforcement of the parties' agreement, survive *Concepcion*. If the single *Discover Bank* factor that an individual's claim may be "too small" to fulfill the policy of deterring law violation thus making class actions a necessary component of the dispute resolution scheme is preempted by the FAA, it would appear that adding more hurdles – "obstacles" the United States Supreme Court would say - that employers would have to surmount before they could get their agreements enforced only exacerbates the problems with the California scheme identified in *Concepcion*.

Employers considering their options for resolving disputes may now well add another reason to consider arbitration.

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[1] 36 Cal. 4th 148 (2005).

[2] 42 Cal. 4th 443 (2007).