ASSOCIATION OF BUSINESS TRIAL LAWYERS SAN DIEGO

abtl REPORT

Volume XVIII No. 2 *Summer 2011*

Plaintiff and Defense Perspective on:

Class Action Waivers After The U.S. Supreme Court Decision In *AT&T v. Concepcion*

By Shannon Petersen, Esq. and Alan Mansfield, Esq.

On April 27, 2011, the U.S. Supreme Court held in *AT&T v. Concepcion* that the Federal Arbitration Act "preempts California's rule classifying most collective arbitration waivers in consumer contracts as unconscionable."[1] The Court referred to this rule as the "*Discover Bank* rule," after *Discover Bank v. Superior Court*.[2] In *Concepcion*, the Ninth Circuit Court of Appeals affirmed a trial court's finding, based on *Discover Bank*, that a class action waiver in a form arbitration agreement was unconscionable because 1) the contract was a contract of adhesion, 2) the damages at issue were small (averaging $30 per class member), and 3) the plaintiff alleged a scheme to cheat consumers out of small sums of money.

The U.S. Supreme Court reversed. Writing for a 5-4 majority (Justice Thomas wrote a concurrence), Justice Scalia concluded state laws that undermine the enforceability of class action waivers in consumer arbitration agreements improperly obstruct the FAA. The following is a defense and plaintiff perspective on the impact of *Concepcion*.

Discover Bank Is Dead: A View From The Defense

Shannon Peterson, Esq.

Concepcion fundamentally alters the law in California and elsewhere. In addition to *Discover Bank*, the Court's decision also necessarily overturns a host of California cases limiting the enforceability of class action waivers and restricting arbitration agreements on public policy grounds. While the Court's decision applies only to arbitration agreements written under the FAA, it is only a matter of time before

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The Sky Is Not Falling: A Plaintiff's Perspective

Alan M. Mansfield, Esq.

Public interest groups, business associations and plaintiffs' attorneys have either rejoiced or lamented, depending on their point of view, how *Concepcion* either protects businesses from predatory lawsuits or makes it impossible for consumers to obtain redress from predatory practices. While *Concepcion* holds it is a violation of the FAA to find an arbitration clause with a class action waiver provision in certain types of

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form contracts across the country are re-written to provide for arbitration under the FAA and thus benefit from this decision.

According to the Court, the "overarching purpose" of the FAA "is to ensure the enforcement of arbitration agreements according to their terms so as to facilitate streamlined proceedings."[3] This purpose trumps any state law designed to protect class action rights. The Court was unpersuaded by the rationale of *Discover Bank* that enforcing class action waivers in cases involving small sums of money will essentially kill such claims. As the dissent argued: "The *realistic* alternative to a class action is not 17 million individual suits, but zero individual suits, as only a lunatic or a fanatic sues for $30."[4] The majority was untroubled: "The dissent claims that class proceedings are necessary to prosecute small-dollar claims that might otherwise slip through the legal system. But States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons."[5]

As Justice Thomas explained in his concurring opinion, "Contract defenses unrelated to the making of an agreement—such as public policy—could not be the basis for declining to enforce an arbitration clause."[6]

Under *Concepcion*, many other seminal California cases refusing to enforce arbitration clauses now share *Discover Bank*'s death, including *Gentry v. Superior Court*;[7] *Cruz v. Pacific Health Systems, Inc.*;[8] *Broughton v. Cigna Healthplans*;[9] and *Fisher v. DCH Temecula Imports LLC*,[10] among others.

In *Gentry*, the California Supreme Court held that in most cases an arbitration clause cannot be used to waive a statutory right. In *Fisher*, the court relied on *Gentry* and held that there is an unwaivable statutory right to a class action under the Consumers Legal Remedies Act (the CLRA). Both decisions are grounded in state public policy favoring class actions rights over a parties' agreement. Both are now out the window in light of *Concepcion*.

Similarly, in *Broughton* and *Cruz*, the

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California Supreme Court held that claims for a public injunction under the CLRA and the Unfair Competition Law (the UCL) are not subject to arbitration. The Court in *Concepcion* rejected this approach as well. "When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA."[11]

Plaintiffs will try to work around *Concepcion*, but they have little room to maneuver. Though the FAA does not preempt "generally applicable contract defenses" such as fraud, duress, or unconscionability, a plaintiff can no longer argue that the class action waiver itself is unconscionable. Plaintiffs will continue to argue procedural unconscionability, but the Supreme Court did not think much of this argument either, holding that "the times in which consumer contracts were anything other than adhesive are long past."[12] Non-negotiable form contracts remain enforceable. For plaintiffs' class action counsel, the sky is indeed falling. ▲

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arbitration clauses *per se* unconscionable, as the dissent observed, the California Supreme Court had already held as much in *Discover Bank*: "[c]lass action and arbitration waivers are not, in the abstract, exculpatory clauses . . . We do not hold that all class action waivers are necessarily unconscionable."[13] Thus, the U.S. Supreme Court may have only overruled that which the California Supreme Court did not say.

The U.S. Supreme Court's ruling is also limited in that it focused primarily on attacking class action arbitrations under the FAA, not class action waivers generally. The Court conceded if such a clause had other unconscionable elements or defenses that did not apply only to arbitration, such a clause could be stricken without offending the FAA under its savings clause, which "permits agreements to arbitrate to be invalidated by generally applicable contract defenses, such as fraud, duress, or unconscionability."[14] *Concepcion* leaves open whether a class action waiver provision in a non-interstate commerce case, or when combined with other unconscionable elements or defenses that are not solely arbitration-related, could still be invalidated.

The Court also recognized that, "Of course States remain free to take steps addressing the concerns that attend contracts of adhesion—for example, requiring class action-waiver provisions in adhesive arbitration agreements to be highlighted."[15] While this may be an avenue of pursuit in some cases, Defendants will counter that this only applies to laws created by legislation, and not judges, and that any such law cannot interfere with arbitration. Defendants will also argue that this footnote must be reconciled with the Court's own precedent in *Doctor's Associates, Inc. v. Casarotto*,[16] holding that the FAA preempted a Montana statute requiring all contracts containing arbitration provisions to provide notice of such on the first page in underlined and capitalized letters.

The U. S. Supreme Court also did not address a number of other key issues. For example, despite the defense's claim to the contrary, *Concepcion* does not alter the rule of *Broughton* or *Cruz* that claims for injunctions under the CLRA

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or UCL cannot be arbitrated because of the need for judicial oversight over a public injunction (in fact, the majority cited the lack of judicial oversight over a class action as one of the reasons for its holding). Nor did the Court address the holdings of *Gentry, Fisher*, and other California cases that an unwaivable statutory right to a class action exists under certain California statutes. Indeed, the U.S. Supreme Court expressly declined to review *Gentry* several years ago. It and its progeny remain good law.[17] Unless the U.S. Supreme Court decides to undertake a wholesale review of California law, significant questions as to the scope of *Concepcion* remain.

Nor did the Court address class action waivers outside the context of arbitration agreements. California precedent remains unaltered in such circumstances. The Court also did not address the so-called "poison pill" provision contained in many arbitration agreements—that if a class action waiver is found to be unenforceable for any reason, the entire arbitration clause is unenforceable. While arguably such provisions are not enforceable, it remains to be seen how courts will address these issues.

Finally, there is the possibility *Concepcion* will be short-lived. In an ironic twist (since they likely have much more bargaining power than consumers ever will), since 2002 car dealers have been exempt from arbitration clauses altogether for claims by and against car manufacturers under the "Motor Vehicle Franchise Contract Arbitration Fairness Act."[18] The Act was necessary, according to the legislative history, because of "the disparity in bargaining power between motor vehicle dealers and manufacturers," and because motor vehicle franchise agreements "are inherently coercive and one-sided contracts of adhesion." An argument is being advanced that, if this was the justification for imposing a legislative exemption under the FAA for car dealers, the same protections should apply to all consumers. In fact, on May 17, 2011, a trio of Democratic Senators introduced a bill in Congress called the "Federal Arbitration Fairness Act" that would eliminate forced arbitration clauses in consumer and employment contracts. There are other arbitration exemptions as well, such as in the insurance and residential mortgage loan context.

Has the sky fallen, just as pundits claimed with passage of the PSLRA, CAFA and Proposition 64? Likely no—just tell plaintiffs the height of the bar and they'll adjust to hurdle it. But we agree it will take years for plaintiffs, defendants, and the courts to sort out the limits of *Concepcion* and its application to established California authority. ▲

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1. *563* U.S. ___, 131 S.Ct 1740, 1746 (Apr. 27, 2011)
2. 36 Cal.4th 148 (2005)
3. *Id.* at 1748.
4. *Id.* at 1761.
5. *Id.* at 1753.
6. *Id.* at 1755.
7. 42 Cal. 4th 443 (2007) (*cert. den.* 128 S. Ct. 1743, Mar. 31, 2008)
8. 30 Cal. 4th 303, 316 (2003)
9. 21 Cal. 4th 1066, 1082 (1999)
10. 187 Cal. App. 4th 601 (2010)
11. *Concepcion*, 131 S.Ct. at 1747
12. *Id.* at 1750.
13. 36 Cal.4th at 161-62
14. *Concepcion* at 1746.
15. *Id.* at 1750, n.6
16. 517 U.S. 681 (1996)
17. *See also Gutierrez v. AutoWest, Inc.*, 114 Cal.App.4th 77, 95 (2003) ("plaintiffs are entitled to contest the arbitration clause on the basis that it is a private agreement in contravention of public rights—a separate, generally available contract defense not preempted by the FAA"); *America Online, Inc. v. Superior Ct.*, 90 Cal.App.4th 1, 17-18 (2001); *Cf. Piccardi v. Eighth Jud. Dist.*, 127 Nev. Adv. Rpt. 9 (Nev. Supr. Ct., dated March 31, 2011) (holding provision that waived consumer protections under Nevada statutory law unenforceable, even under FAA, citing *Fisher)*
18. 15 U.S.C. § 1221 *et seq.*