Arbitration After *AT&T Mobility v. Conception:* Judicial, Regulatory And Strategic Legal Responses To High Court's 2011 Ruling

This discussion is moderated by ***Glenn G. Lammi****, Chief Counsel, Legal Studies Division, Washington Legal Foundation. Featured speakers are* ***Andrew Pincus*** *and* ***Evan Tager****, both Partners with Mayer Brown and attorneys for the petitioner.*

Lammi: *AT&T Mobility LLC v. Concepcion (Concepcion)* is a U.S. Supreme Court decision that many in the plaintiffs' bar criticize as the most harmful case in the history of consumer protection, as it could end all class action suits. The Court ruled by a five-to-four vote that the Federal Arbitration Act (FAA) supersedes California's state law, which, considers arbitration clauses that limit dispute resolution to an individual, instead of a class of plaintiffs, unconscionable. Under the Court's ruling, clauses that prohibit class action arbitration are generally enforceable. After the decision, plaintiff supporters of class actions have asked courts around the country to find a way around *Concepcion*, with little success.

Tager: Starting with an overview of the Federal Arbitration Act (FAA) and how we got to *Concepcion*, I will discuss some of the ways in which the plaintiffs' bar has attempted to distinguish the case and how the courts have responded. The Federal Arbitration Act was passed in 1925 in order to reverse the longstanding judicial hostility to arbitration. The key provision in the Act is the Section 2 savings clause, which requires that arbitration agreements be enforced save upon such grounds that existed in law or in equity for the revocation of any contract. In the early days, the FAA was used mostly to enforce contracts between businesses. Beginning in the 1990s, however, businesses began to include arbitration clauses in their agreements with customers. The plaintiffs' bar responded by seeking to invoke unconscionability provisions of state law under the savings clause in Section 2 to attack various features of the arbitration provisions. Among the features they attacked, and had some success in invalidating, were provisions that allowed businesses to bring their disputes against customers in court while requiring the customers to proceed in arbitration, deemed to be non-mutual and unconscionable under some state laws. There were cases involving fee splitting, requiring that the customer pay or the employee pay half of the cost of the arbitration, making arbitration of an individual claim prohibitively expensive. A number of the early arbitration clauses contained limitations on remedies, and almost all the early arbitration clauses contained confidentiality requirements, considered to be one of the benefits of arbitration although courts often struck those down. Some arbitration clauses required that the arbitration be brought where the company was located, which for consumers across the country made it unrealistic to arbitrate a small claim, and, finally, an occasional arbitration clause, most notably the Hooters employment arbitration clause, actually gave the company the right to choose the arbitrator – a clause that was struck down. Sensible companies realized that these first-generation arbitration clauses should not be used as a way to give themselves an unfair advantage and began to reform their clauses. These second-generation clauses were much cleaner, and their central feature was the requirement that claims be brought on an individual basis, which was central to the willingness of most companies to create an arbitration program.

The plaintiffs' bar then turned its fire on the class waivers. Most courts upheld these clauses, but a few courts, most notably the California Supreme Court, struck them down as unconscionable, at least in cases where the claims are predictably small.

Pincus: Before *Concepcion* reached the Supreme Court, there had been a lot of litigation in the lower courts about arbitration in general and the preemptive effect of the Federal Arbitration Act on state law grounds for invalidating arbitration clauses as well as on the particular question of class waivers. To us, *Concepcion* seemed like an excellent case for the Court to address for several reasons. It was a typical class action arguing that AT&T had violated California consumer protection law. AT&T, the cell phone provider, stated the phone was free if you signed up for a service plan for a specific number of months. California law requires that the sales tax be charged on that transaction as if the phone were being purchased at its regular retail price, so when the Concepcions got to the checkout counter, they were presented with a bill for the sales tax, which they paid, knowing they had entered the transaction. This case was filed later based on AT&T's claim that the phones were free, but the sales tax was owed. AT&T moved to compel arbitration. The lower courts after reviewing AT&T's arbitration clause indicated that the respondents had a better chance of recovering full compensation in arbitration than in a class action but felt bound by California law, *even though this case was in federal court*. Because of California law, the lower courts had to hold the clause unconscionable because it doesn't permit class proceedings either in arbitration or in litigation. So we brought the case to the Supreme Court, explaining that for nationwide companies, it is difficult to have one consistent dispute resolution program if California renders an arbitration clause invalid.

The provisions of the AT&T clause, which are particularly useful in understanding both AT&T's goal and arbitration in general, represent many hours spent with AT&T on its evolution in helping AT&T obtain its objective – to make customers happy by providing a dispute resolution system that works for the company as well as the customer. The clause is specifically designed to address the claim advanced by the plaintiffs' bar that if you require individualized arbitration, there's no incentive for injured parties to bring small claims owing to the cost of litigation. AT&T wished to provide an incentive so that customers could seek redress to bring any corporate missteps to its attention, and if not fixed, give them an incentive to go to arbitration. So there are a number of provisions of the arbitration clause, such as a provision that AT&T pays all the costs of arbitration, that encourage resolution through arbitration. If AT&T wants to settle before the claim moves to arbitration, the arbitration clause gives AT&T that opportunity. If the customer's award in arbitration is even a dollar more than what AT&T offered in settlement, AT&T has to pay a minimum amount and double attorneys fees.

For the customer, there are no limitations on the kinds of individual relief available – an option to go to small claims court, arbitration close to the customer's home at the customer's option, proceedings governed by the American Arbitration Association and its consumer dispute rules, and, finally, no confidentiality requirement for the results of arbitration. It's hard to imagine a fairer process, and the lower courts seemed to say this was a process where people weren't going to do better than arbitration.

So what did the U.S. Supreme Court do? By a five-to-four vote, they reversed the Ninth Circuit and held that California's state law rule that invalidated arbitration clauses containing class waivers was preempted by the Federal Arbitration Act because requiring those class procedures interfered with a fundamental attribute of arbitration – individualized adjudication.

The argument of the respondents was that they need class proceedings because these small dollar claims wouldn't be asserted and would slip through the legal system. The majority of the Court responded that states may not require a procedure that is inconsistent with the FAA, and that Congress had spoken with the statute. Looking at AT&T's clause, the Court found that respondents' argument didn't work because there was no evidence that even the smallest claim would go unresolved because of the special provisions of the AT&T system. The majority cited the district court's finding that the Concepcions were better off and more likely to be compensated under the AT&T arbitration than as participants in the class action.

Tager: The plaintiffs' bar has fastened onto the language that the Court used to explain why the policy argument it was rejecting had no force under the facts of this case. Their first principal argument is that this ruling only applies to arbitration clauses that contain these special incentives of AT&T's clause. In the Third Circuit *Litman* decision, which interestingly involved Verizon's arbitration clause, the court's holding was much broader, stating that the *Concepcion* decision is clear and precludes states from overturning an arbitration clause on the ground that it bars class actions.

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Corporate Counsel Organization Highlights

Letter From The President Of The New Jersey Corporate Counsel Association

To The Readers Of *The Metropolitan Corporate Counsel:*

This month, I celebrate the one-year anniversary of my NJCCA presidency. With the assistance of our excellent Executive Committee, Board of Directors, Committee Leaders, and Executive Director, this year was hugely successful. I want to take a moment to discuss some of those successes.

Our premier annual events have been superb. In August 2011, we gathered for our annual Build-a-Backpack event in which members and volunteers fill backpacks with school supplies to be delivered to elementary school children in districts having demonstrable financial need. We filled a record number of backpacks and brought smiles to the faces of the many children who received them. In September, we held our annual All-Day CLE Conference, which featured more than 25 separate substantive legal programs and was attended by close to 350 people, breaking all past participation records. The programs were followed by a well-attended cocktail and networking reception. In November we held our Annual Dinner, which featured the governor's chief-of-staff as the keynote speaker. As has become our custom, we began the event with two hours of substantive CLE programming. In December, we held our annual Holiday Outreach event, in which members and volunteers gathered for a festive evening of wrapping books for distribution to children living in shelters. Finally, in May 2012, we gathered for our annual Spring Cocktail Reception. We once again exceeded attendance records and presented two hours of substantive CLE programming as well. All in all, our premier annual events were hugely successful this past year, and we look forward to repeating those successes in the year ahead.

In addition to the above, we held close to thirty stand-alone CLE and/or professional networking events over the past twelve months. We look forward to having a good showing of NJCCA members at the ACC's annual convention in Orlando in September. This past April, several of us attended the ACC's annual Leadership Development Institute in Washington, DC, in which I was a featured panelist. We returned with ideas that will enable us to provide even greater service to NJCCA's members. NJCCA also continues to have a presence on the Board of Directors of the national ACC, enhancing our visibility. The NJCCA's Women's Networking Committee has been recognized for its many activities.

NJCCA is the only ACC affiliate chapter that publishes a monthly online newsletter. Each edition features a substantive legal article of interest and, among other things, a job line and a unique cartoon, Overruled!

Our membership has continued to grow, a testament to the dedication of our volunteers and sponsors who have devoted their time to delivering high-quality CLE and networking opportunities to NJCCA's members. NJCCA is the only professional association exclusively dedicated to serving the interests of the New Jersey in-house legal community. We look forward to building upon our successes in the coming year, and hope to see you at our events. Please feel free to contact our executive director, Gail Girard, with any questions at njcca@comcast.net, and check out our upcoming events at acc.com/chapters/njcca.

Sincerely,
Joseph M. Aronds

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The next argument is that the only state whose law was preempted is California, and the reasoning behind this argument is the Supreme Court treated California as having an across-the-board prohibition against arbitration clauses that require individualized dispute resolution and preclude class actions, because in *Concepcion,* California is arguing that when the claims are small, there can't be arbitration clauses requiring individualized dispute resolution. So the plaintiffs' bar has articulated a two-part argument: *Concepcion* is limited to that kind of state law unique to California while the other state laws require a case-by-case determination of whether it is possible for the individual plaintiff to resolve his or her dispute in a one-on-one bilateral arbitration. In both the *Cruz* case, which involved Florida law, and the *Coneff* case, which involved Washington law, the plaintiffs' bar pushed the argument that *Concepcion* is limited to California law, and in both cases the federal appellate court rejected the argument.

Another argument that has gotten greater traction is whether certain state law claims under California law that effectively require non-individualized treatment are non-arbitrable and therefore outside the scope of the *Concepcion* decision. There are the so-called public injunction claims under the Unfair Competition Law and the Consumer Legal Remedies Act authorizing consumers to seek injunctions against business practices of companies that they have relationships with on behalf of all the public. The California courts have held that those kinds of claims can't be handled by an arbitrator, must be brought in court, and that the FAA is not preemptive. Since *Concepcion,* the federal district courts, and more recently the Ninth Circuit, have held *Concepcion* makes clear that states can't put any particular claim off-limits to arbitration. This is an exceptionally important issue to the business community because it would allow the plaintiffs to bring almost any claim against a national company in California and seek to obtain a public injunction against whatever practice they claim is unfair. Secondly, California has what's known as a Private Attorneys General Act, which allows employees to seek penalties against employers on behalf of all similarly situated employees. That effectively is a class action for penalties, and a divided panel of the California court of appeals in the *Brown* case held that that can't be submitted to arbitration and the FAA is not preemptive.

Pincus: An argument that has carried more weight in the court of appeals is the set of questions relating to the legal rules when the plaintiffs' underlying claim arises under federal law and not under state law. Formerly, the Supreme Court was hostile to the idea of the arbitrability of federal law claims on the basis that federal law claims were not arbitrable. Starting in the late 1960s and early '70s, it reversed course, determining that most federal claims are, in fact, subject to arbitration. The analysis that the Court has applied in those cases is that the FAA obviously doesn't have preemptive effect with respect to another federal law the way it does with respect to state law rules. There's a general policy in favor of arbitration in the FAA, which should be respected unless there's something in the federal statute that indicates some contrary intent of Congress.That's a pretty straightforward analysis and not surprisingly has led to a series of decisions, most recently the *CompuCredit* decision this term, with the Court saying federal claims are arbitrable.

What has happened after *Concepcion?* First, the Second Circuit, in the case involving the arbitration clause in American Express's agreements with its merchants, recently reaffirmed its earlier decision, essentially applying this on a case-by-case vindication test, saying individual arbitration would be prohibitively expensive and therefore the antitrust right couldn't be vindicated in arbitration. That argument having been successful, it is spreading to lots of other contexts and federal claims, most notably Fair Labor Standards Act claims, with divided results in the courts so far and with lots of cases pending on appeal.

So plaintiffs may say *Concepcion*, limited to preemption, applies only to state law. It's true *Concepcion* is a preemption case and did address federal law, but it's important not to argue that *Concepcion* of its own force is dispositive. What *Concepcion* said is that class proceedings interfere with fundamental attributes of arbitration and create a scheme that's inconsistent with the FAA. So if that is true for state claims, it is just as true for federal claims, and that Congress directed a policy in favor of arbitration as provided by the FAA.

The problem for the plaintiffs is they can't find anything because there's certainly nothing in the federal antitrust laws, the securities laws and other statutes enacted before there was a class action mechanism that says class remedies are essential, nor is it present in Rule 23 creating class actions because as the Rules Enabling Act teaches us, Rule 23 doesn't create any substantive rights. So the argument is that once a federal claim is arbitrable, as the Court has said all these claims are, then that's really the end of the argument, which the Supreme Court has said in *Concepcion* means individualized arbitration. This argument is going to be played out in a lot of courts and will be one of the principal arenas of conflict.

Tager: Notwithstanding *Concepcion*, in generally applicable contract law unconscionability principles can still be applied to arbitration clauses, and therefore the problems with clause provisions that are fundamentally unfair, i.e., where the company picks the arbitrator, are still going to be problems. A footnote in *Concepcion* reaffirms the idea that arbitration clauses are contracts of adhesion, and generally applicable laws that don't frustrate the FAA purposes can be applied.

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Let's turn now from the courts to other arenas where there is some hostility to arbitration and where the plaintiffs' bar has turned its attention, recognizing that a lot of its arguments are not doing well in the judicial forum and also to use these policy areas to try and put pressure on the courts to rule their way on these issues.

Viewing the regulatory arenas, it's important to recognize there's a big battle for hearts and minds going on. In Congress there's been an interest for about six years in the Arbitration Fairness Act, which has the effect of banning all predispute arbitration in the employment and consumer context. This would dramatically change the FAA and decades of case law. That bill has been introduced and hearings have been held in the Senate, but it doesn't seem to be going anywhere.

The same can't be said about federal regulatory agencies. The NLRB issued a decision in January just before the terms of several NLRB appointees expired that a mandatory arbitration clause in an employment contract that had a class waiver was an unfair labor practice because it violated employees' rights under the National Labor Relations Act to engage in concertive action. That case is on review in the Fifth Circuit and briefing is underway. This is obviously a very important case because if this ruling were to be upheld, it would apply not only to unionized workplaces but to every workplace.

The SEC is the next stop on our regulatory tour. Carlyle Group looked at *Concepcion* in planning to include in its organizational documents for its IPO a provision requiring individualized arbitration of investor claims. Much pressure was placed upon Carlyle by the plaintiffs' bar and its allies, and Carlyle decided to drop that provision from its IPO documents. One of the places where arbitration has been used the longest is in the broker-dealer context. Charles Schwab looking at *Concepcion* said, "Let's include a class waiver in our arbitration agreement," but FINRA, which is the private regulatory arm of the SEC, essentially started an enforcement action on the basis that this violated its rules. My guess is the biggest area of activity in the next year or so is going to be the Consumer Financial Protection Bureau, which has statutory authority to regulate arbitration or ban it in transactions under its regulatory jurisdictions – which are extremely broad in terms of consumer financial services. The first statutory step is a requirement that it conduct a study of the use of arbitration in the consumer context. The bureau just issued a request for comments for guidance on how that should be conducted and what it should encompass. So stay tuned as there are huge potential implications if the bureau were to go ahead with some regulation or banning of arbitration.