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Concepcion After One Year: The Changed World of Arbitration and Class Actions

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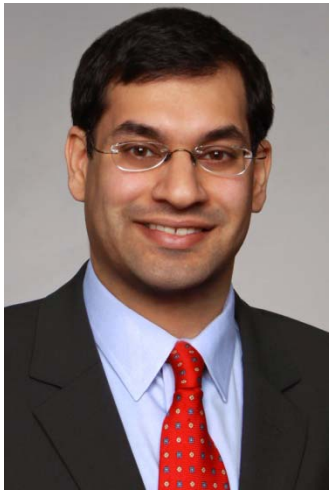
Speakers



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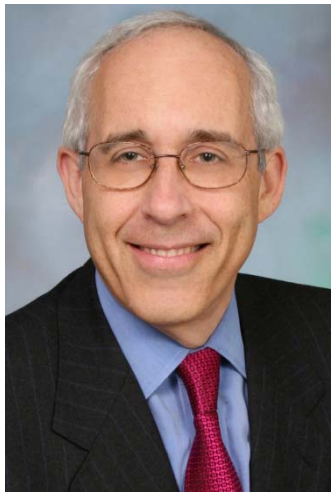

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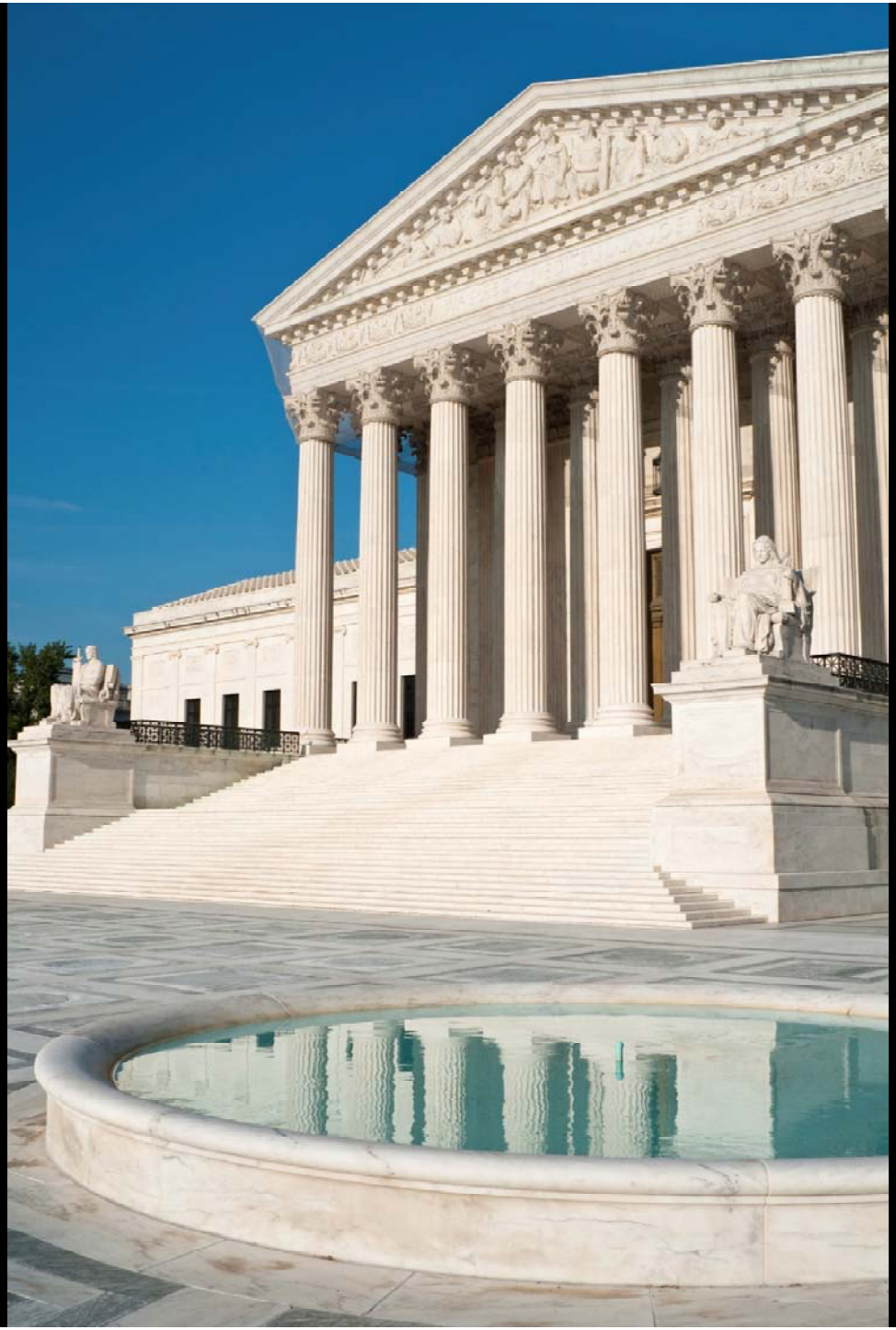
The Road to *Concepcion*

- Businesses began including arbitration provisions in their customer and employee agreements in the 1990s.
- Plaintiffs responded by invoking state unconscionability law, attacking:
  - Non-mutuality (only plaintiff had to arbitrate; company could sue).
  - Payment of arbitration fees by customer/employee .
  - Limitations on remedies (e.g., punitive damages and/or attorneys' fees).
  - Shortened statutes of limitations.
  - Confidentiality requirements.
  - Requirements that arbitration take place near company's headquarters (or in some other inconvenient location).
  - Biased arbitrator-selection process.
- Many of these provisions were struck down; businesses responded to these decisions by revising their arbitration clauses to address the courts' concerns.

The Road to *Concepcion*

- The battle then shifted to the issue of class-wide arbitration.
- Virtually all arbitration clauses included prohibitions on class arbitration and class actions in court; early decisions upheld these provisions.
- The California Supreme Court, however, held that, at least in some circumstances, such provisions are unconscionable. Courts in some other states followed suit.
- Most courts continued to enforce these arbitration provisions provided none of the traditional indicia of unconscionability were present (*e.g.*, limitations on remedies, higher filing costs than for comparable judicial actions).

The Supreme Court's decision in *AT&T Mobility LLC v. Concepcion*



Background of *Concepcion*

- The Concepcions filed a class action alleging that AT&T had violated California consumer-protection law. AT&T moved to compel arbitration.
- The lower courts concluded that the Concepcions could vindicate their claims in arbitration under AT&T's arbitration clause, but held that the clause was unconscionable because class-wide proceedings weren't permitted.
- The Supreme Court granted certiorari to consider whether the California law rule invalidating the arbitration clause was preempted by Section 2 of the Federal Arbitration Act.
  - Section 2 provides that arbitration agreements must be enforced, unless there is a generally applicable rule of state law that would authorize invalidating any contract.

Key Features of AT&T's Arbitration Provision

- Consumer pays **no arbitration costs** as long as the claim is not frivolous.
- AT&T must **pay the consumer a minimum of $5,000** (now, $10,000) plus **double attorneys' fees** if the arbitrator awards the consumer **more than AT&T's final settlement offer**.
- **Arbitrator may award any form of individual relief affecting the individual claimant alone** (including punitive damages, attorneys' fees, and injunctive relief) that would be available to the consumer in court.
- Consumer may file suit in **small claims court** rather than arbitrating.
- Arbitration takes place in the **county in which the consumer resides**, and for claims under $10,000, the consumer may choose whether the arbitration will be in person, by telephone, or on written submission.
- Proceedings (including the process for selecting the arbitrator) are governed by consumer arbitration rules of the independent, non-profit American Arbitration Association.
- Consumers and their attorneys are **not required to keep arbitration confidential**, and may bring issues to the attention of federal or state agencies.

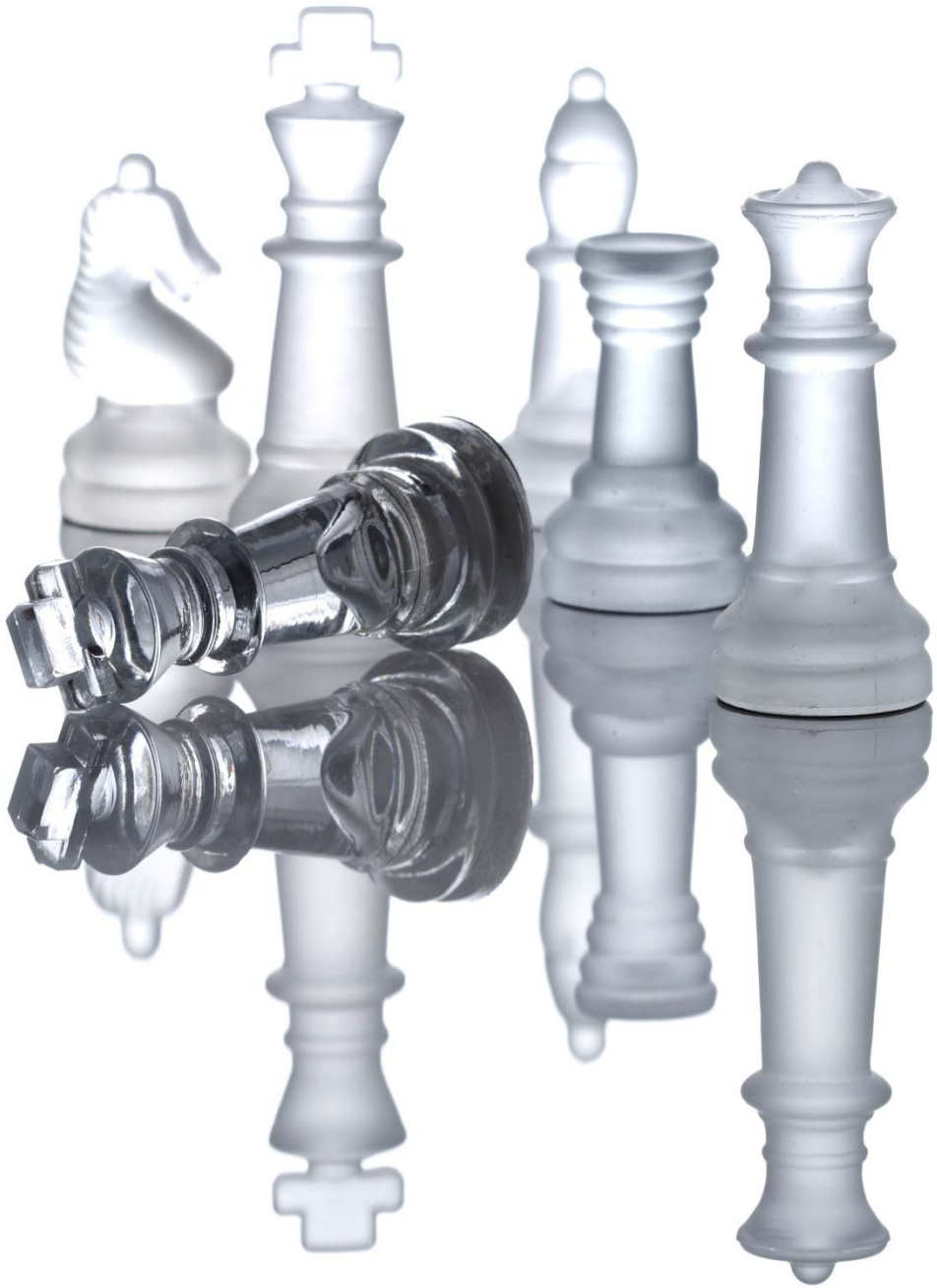
The Supreme Court Decision

By a 5-4 vote, the Supreme Court reversed the Ninth Circuit.

- Held California law preempted : "Requiring the availability of class-wide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA."
- Rejected dissent's argument that "class proceedings are necessary to prosecute small-dollar claims that might otherwise slip through the legal system."
  - "States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons."
  - "Moreover, the ***claim here was most unlikely to go unresolved***" because of the special features of the AT&T arbitration agreement: "Indeed, the District Court concluded that the Concepcions were ***better off*** under their arbitration agreement with AT&T than they would have been as participants in a class action."

Concepcion at One Year:

How the Plaintiffs' Bar, Courts, and Businesses Have Responded to the Decision



The First Wave of Arguments Against Arbitration

- Plaintiffs have argued that arbitration clauses that do not contain all of the pro-consumer provisions of AT&T's clause are outside the scope of *Concepcion's* holding.

- Courts have overwhelmingly rejected that contention.
  - "We understand the holding of *Concepcion* to be both broad and clear: a state law that seeks to impose class arbitration despite a contractual agreement for individualized arbitration is inconsistent with, and therefore preempted by, the FAA, irrespective of whether class arbitration 'is desirable for unrelated reasons.'"

    Litman v. Cellco P'ship, 655 F.3d 225, 231 (3d Cir. 2011)

  - *See also, e.g., Giles v. GE Money Bank*, 2011 WL 4501099 (D. Nev. Sept. 27, 2011); *Tory v. First Premier Bank*, 2011 WL 4478437 (N.D. Ill. Sept. 26, 2011); *Adams v. AT&T Mobility, LLC*, 2011 WL 4720194 (W.D. Wash. Sept. 20, 2011); *Alfeche v. Cash Am. Int'l Inc.*, 2011 WL 3565078 (E.D. Pa. Aug. 12, 2011); *Carrell v. L & S Plumbing P'ship, Ltd.*, 2011 WL 3300067 (S.D. Tex. Aug. 1, 2011).

The First Wave of Arguments Against Arbitration

- Plaintiffs have argued that state courts are not bound by *Concepcion* because Justice Thomas takes the view that the Federal Arbitration Act does not apply in state court.
- But state courts have consistently applied *Concepcion*.
  - *See, e.g.*, *Gustavus, L.L.C. v. Eagle Inv.*, 2012 WL 107988 (Ohio Ct. App. Mar. 30, 2012); *Cottonwood Fin., Ltd. v. Estes*, __ N.W.2d __, 2012 WL 265716 (Wis. Ct. App. Jan. 31, 2012); *NAACP of Camden Cty. East v. Foulk Mgmt. Corp.*, 24 A.3d 777 (N.J. Super. A.D. 2011)
- The Supreme Court's recent, unanimous summary reversal in *Marmet Health Care Center, Inc. v. Brown,* 132 S. Ct. 1201 (2012) should discourage state courts from accepting plaintiffs' invitation to treat *Concepcion* as inapplicable.

The First Wave of Arguments Against Arbitration

- Plaintiffs claim that *Concepcion* permits states to refuse to enforce arbitration agreements when state law authorizes representative relief.
  - Representative action under California's Private Attorney General Act (PAGA)
    - California Court of Appeal has held that PAGA claims cannot be required to be arbitrated on an individual basis, despite *Concepcion*. *See Brown v. Ralph's Grocery Co.*, 197 Cal. App. 4th 489 (2011).
    - A federal district court has explained, however, that mandating the availability of representative PAGA actions in arbitration is just as inconsistent with the FAA as class arbitration. *See Quevedo v. Macy's Inc.*, 798 F. Supp.2d 1122(C.D. Cal. 2011).
  - Public injunctive relief under California's Consumers Legal Remedies Act (CLRA) or Unfair Competition Law (UCL)
    - Although federal district courts had been divided, the Ninth Circuit recently held that the FAA preempts California's rule that claims for public injunctive relief are exempt from arbitration. *See Kilgore v. Key Bank, N.A.*, 673 F.3d 947 (9th Cir. 2012).

The First Wave of Arguments Against Arbitration

- Plaintiffs asserting state-law causes of action have argued that they should be permitted to prove that their claims cannot be vindicated effectively in individualized arbitration.

- These arguments have been rejected.

  – "*Concepcion* is broadly written. … The Court observed that individualized proceedings are an inherent and necessary element of arbitration."

  – "The dissent in *Concepcion* focused on a related but different concern—… not so much that customers have no effective *means* to vindicate their rights, but rather that customers have insufficient *incentive* to do so. … But as the Supreme Court stated in *Concepcion*, such unrelated policy concerns, however worthwhile, cannot undermine the FAA."

Coneff v. AT&T Corp., 673 F.3d 1155, 1159 (9th Cir. 2012)

See also Cruz v. Cingular Wireless LLC, 648 F.3d 1205, 1214 (11th Cir. 2011)

The Next Challenge to Arbitration – Federal-Law Claims

- Plaintiffs have argued that, if they can prove that they are not as readily able to vindicate their own rights under federal statutes without the use of the class action device, then an agreement to arbitrate on an individual basis is unenforceable.
- Prior to *Concepcion*, some plaintiffs successfully invoked this argument in allegedly complex antitrust cases. In these cases, plaintiffs submitted evidence purporting to show that the cost of pursuing an individual claim (including expert witnesses' fees) would far exceed the amount of the claim. *See Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006); *In re Am. Express Merchants' Litig.*, 634 F.3d 187 (2d Cir. 2011).

The Next Challenge to Arbitration – Federal-Law Claims

- The Second Circuit reaffirmed its holding in *In re American Express Merchants' Litigation*, 667 F.3d 204 (2d Cir. 2012).
  - The plaintiffs had provided an uncontested estimate of costs of proving antitrust claim, including expensive expert witness fees in the hundreds of thousands of dollars.
  - Court holds that individual arbitration would be "prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws."
  - Concludes that *Concepcion* is limited to preemption of state law and thus can be distinguished in the context of federal claims.
- Plaintiffs are trying to the same argument in Fair Labor Standards Act cases.
  - Plaintiffs win in *Sutherland v. Ernst & Young LLP* (S.D.N.Y. 2011) (appeal pending) and *Raniere v. Citigroup Inc.* (S.D.N.Y. 2011) (appeal pending), lose in *LaVoice v. UBS Fin. Servs.* (S.D.N.Y. 2012).

The Next Challenge to Arbitration – Federal-Law Claims

- Plaintiffs' "vindication" argument contends that *Concepcion* is a preemption decision that applies only to state law.
- But if class proceedings "interfere[] with fundamental attributes of arbitration and thus create[] a scheme inconsistent with the FAA," as *Concepcion* held, that is as true for federal-law claims as for state-law claims.
- Once a federal claim is held to be arbitrable, that FAA policy applies with the same force to the federal claim.
- No federal statutory or common-law authority for courts to devise standards for determining scope of protection provided to arbitration that differ from those applicable to state claims.

The Next Challenge to Arbitration – Federal-Law Claims

- Ninth Circuit rejects "vindication" with respect to AT&T clause:
  - "Although Plaintiffs argue that the claims at issue in this case cannot be vindicated effectively because they are worth much less than the cost of litigating them, the *Concepcion* majority rejected that premise. Significantly, the arbitration agreement here has a number of fee-shifting and otherwise pro-consumer provisions, identical to those in *Concepcion*." *Coneff*, 673 F.3d at 1159.
  - "[W]e distinguish this case from [*In re American Express*]. There, the Second Circuit specifically found that 'the only economically feasible means for plaintiffs enforcing their statutory rights is via a class action.' … To the extent that the Second Circuit's opinion is not distinguishable, we disagree with it and agree instead with the Eleventh Circuit [in *Cruz*]." *Id.* at 1159 n.3.

Proposed Legislation and Regulations that Would Restrict the Use of Arbitration

The Policy Attack

- *Concepcion* was greeted with sustained attack by the plaintiffs' bar, which is still going strong after one year.
  - Public Citizen issues one-year report: "Justice Denied. One Year Later: The Harms to Consumers from the Supreme Court's *Concepcion* Decision Are Plainly Evident."
  - Columns by consumer advocates/others hostile to arbitration.
- Goal is to provoke federal regulatory action, influence courts.
- In fact, policy principles strongly favor arbitration.
  - Provides more access to justice for more claimants.
  - Opponents would trade away this increased justice to permit class actions that virtually always benefit only lawyers and provide little or nothing in compensation or deterrence.
  - Moreover, class actions unnecessary to obtain relief in arbitration.

Possible Federal and State legislation

- The Arbitration Fairness Act
  - Would invalidate **all** "**predispute arbitration agreements**" in employment and consumer contracts and bar enforcement of agreements to arbitrate any "dispute arising under any statute intended to **protect civil rights**."
  - Would **apply retroactively** to all pre-existing arbitration agreements, so long as the "dispute or claim . . . arises on or after" its effective date—invalidating hundreds of millions of arbitration agreements .
  - Would preempt state policies favoring arbitration.
- Industry-specific federal legislation (*e.g.*, bills affecting nursing homes, military contractors)
- State Initiatives
  - *E.g.*, block interlocutory appeals to enforce arbitration agreements; redefine "contracts of adhesion"

National Labor Relations Board

- *D.R. Horton, Inc.*, 357 NLRB No. 184 (Jan. 6, 2012)
  - Employee filed complaint with NLRB, arguing that arbitration provision is an unfair labor practice under Section 8 of National Labor Relations Act because it bars exercise of Section 7 right to engage in "concerted activity."
  - A two-member panel of the Board concluded that because the NLRA protects "concerted activity," it is an unfair labor practice to require arbitration on an individual basis as a condition of employment.
  - D.R. Horton's petition for review in Fifth Circuit is pending.
- NLRB's recent complaint against 24 Hour Fitness USA, which allows employees to opt out of agreements to arbitrate on an individual basis.
- *Morvant v. P.F. Chang's China Bistro, Inc.*, No. 11-CV-05405 YGR (N.D. Cal. May 7, 2012), disagrees with the NLRB's analysis

Securities and Exchange Commission

- Carlyle Group initially planned to include in its organizational documents a provision requiring individualized arbitration of any investor claims.
  - Provision was dropped in the face of opposition.
- FINRA enforcement action against Charles Schwab for including class waiver in broker-dealer arbitration clause.
  - Extent to which *Concepcion* applies in this context will be determined.

Consumer Financial Protection Bureau

The Consumer Financial Protection Bureau may regulate the use of arbitration by businesses subject to its jurisdiction:

- Section 1028 of the Dodd-Frank Wall Street Reform and Consumer Protection Act calls for the Bureau to **study** the use of pre-dispute arbitration agreements in consumer financial markets.
- The Act then gives the Bureau the power to "**prohibit or impose conditions or limitations** on the use of an agreement between a covered person and a consumer for a consumer financial product or service providing for arbitration of any future dispute between the parties, if the Bureau finds that such a prohibition or imposition of conditions or limitations **is in the public interest and for the protection of consumers.**"
  - Note that any rule must be based on the findings of the arbitration study.
- Bureau recently sought public comment about the "scope, methods, and data sources for conducting" its study of arbitration agreements. Comments due by June 23.

Implementing an Arbitration Program

Press reports indicate more companies are implementing arbitration programs. Key drafting issues include:

- Ensuring creation of a contractual relationship – assent by both sides in a manner that can be proven later, if necessary.
- Consider whether to allocate issues of arbitrability to court or to arbitrator.
- Class action waivers should be express.
- Recognize that arbitration provision will be viewed in the court of public opinion as well as by judges.

Implementing an Arbitration Program

Arbitration clauses can be invalidated on the basis of generally-applicable principles of contractual unconscionability.

- Footnote 6 in *Concepcion*:

  "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. Such steps cannot, however, conflict with the FAA or frustrate its purpose to ensure that private arbitration agreements are enforced according to their terms."

- *Marmet Health Care Center v. Brown*, 132 S. Ct. 1201, 1204 (2012):

  "Arbitration clauses may be "unenforceable under state common law principles that are not specific to arbitration and pre-empted by the FAA."

- Draft agreement to avoid these pitfalls:
  - Selection of arbitral forum
  - No limitation of remedies
  - Place/mode of arbitration

Implementing an Arbitration Program

- Consider inclusion of consumer/employee-friendly provisions
  - Extra emphasis on arbitration clause: make it prominent
  - Payment of arbitration fees by company for smaller claims
  - Option of small claims court
- Assess appropriateness of premium approach
  - Arbitration is not “one size fits all”; different structures appropriate for different types of relationships
  - Premium approach has benefit of providing an additional layer of protection in the federal claim context