Supreme Court Holds California's Prohibition On Class Action Waivers In Arbitration Agreements Is Pre-Empted By Federal Law

On April 27, 2011, the U.S. Supreme Court held in *AT&T Mobility, LLC. v. Concepcion* that federal law preempts a California rule that banned class action waivers in arbitration agreements. The Supreme Court overturned a previous ruling of the Ninth Circuit that had found AT&T's arbitration agreements with its cell phone customers to be unenforceable because the agreements waived customers' rights to bring claims in arbitration on behalf of a class. The Ninth Circuit's decision rested on *Discover Bank v. Superior Court*, 36 Cal.4th 148, 113 P.3d 1100 (2005), in which the California Supreme Court held that class action waivers in consumer arbitration agreements are unconscionable if the agreement is in an adhesion contract, disputes between the parties are likely to involve small amounts of damages, and the party with inferior bargaining power alleges a deliberate scheme to defraud.

In *AT&T Mobility v. Concepcion*, the Supreme Court determined that the *Discover Bank* rule is preempted by the Federal Arbitration Act ("FAA") because it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Justice Scalia, wrote the majority opinion, joined by Chief Justice Roberts and Justices Alito, Kennedy, and Thomas (who filed a concurring opinion).

The Ninth Circuit had found AT&T's class-action waiver "unconscionable" even though the AT&T arbitration agreement was consumer friendly, cost-free (unless the arbitrator determined a claim to be frivolous), and essentially guaranteed that AT&T would make whole any aggrieved customer who filed a claim. To the Ninth Circuit, the irredeemable vice of the arbitration agreement was that it insulated AT&T from class actions of any kind. The Ninth Circuit viewed such contract waivers as "exculpatory," and void as a matter of California public policy because they would allow a defendant potentially to avoid liability to a large number of customers who were either unaware of their potential claims or who declined to pursue them. The pains taken by AT&T to craft a fair and user-friendly agreement undoubtedly influenced the majority of the Supreme Court in deciding to reverse the Ninth Circuit's decision.

The *AT&T Mobility* appeal received wide attention because the question of class-action waivers has arisen frequently in the context of employment arbitration agreements as well as in commercial contracts. This anticipated decision comes only a year after the Supreme Court's ruling in *Stolt-Neilsen S.A. v. Animalfeeds International, Corp.*, 130 S. Ct. 1758 (2010), which held that if parties to an arbitration agreement did not intend to allow class claims, arbitrators have no power to impose class-wide arbitrations under agreements that are merely "silent" on the issue.

Enlarging on the fundamental differences between bilateral and class-wide arbitration, which formed the basis for the decision in *Stolt-Nielsen*, the majority in *AT&T Mobility* emphasized that "the switch from bilateral to class arbitration sacrifices the principal advantages of arbitration – and makes the process slower, more costly and more likely to generate a procedural morass than final judgment." Class arbitration also greatly increases risks to defendants, the Supreme Court noted, because arbitral errors may go uncorrected in light of the highly limited scope of judicial review of arbitral awards.

In light of *AT&T Mobility v. Concepcion*, it behooves employers with pre-dispute arbitration agreements in employment contracts to consider inserting class-action waivers if their agreements do not already contain them. Employers without arbitration programs are likely to consider adopting them as a means to manage the risk of wage & hour and employment discrimination class actions.

It is expected that class arbitration waivers will continue to face assault from legislative initiatives and from a new source: the National Labor Relations Board ("NLRB"). Following the directive of former NLRB General Counsel Meisburg in a Memorandum issued on June 16, 2010, the NLRB has issued complaints against companies that maintain class actions waivers in pre-dispute arbitration agreements on the theory that such agreements interfere with employees' statutory right to engage in concerted activity. It is expected that other federal enforcement agencies, such as the EEOC, also may take active steps to promote collective litigation strategies against employers they deem to be violating federal law.

Invitations for a webinar on the design, enforcement, and implementation of pre-dispute arbitration agreements to avoid class-action arbitrations in light of *AT&T Mobility* will be forthcoming shortly from Seyfarth Shaw LLP.

For more information, please contact the Seyfarth Shaw attorney with whom you work, or any Labor & Employment attorney on our website.

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