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LEGAL ALERT

Legal Alert: Supreme Court Finds FAA Preempts State Law Prohibiting Class Action Waivers in Arbitration Agreements

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This article is a continuation of Ford & Harrison LLP's focus on the use of arbitration agreements to protect employers from collective/class-action exposure under the Fair Labor Standards Act.

On April 27, 2011, the United States Supreme Court issued *AT&T Mobility LLC v. Concepcion* addressing the enforceability of an arbitration agreement in a consumer contract that prohibited classwide arbitration. In a 5-4 decision, the Court held that the agreement was enforceable, reversing the Ninth Circuit's determination that the agreement prohibiting class claims was unconscionable under California law. The *Concepcion* decision is a strong indication that an arbitration agreement prohibiting classwide arbitration in the employment context would be enforceable. (For a link to the *Concepcion* slip opinion, click here).

Background

Vincent and Liza Concepcion entered into an agreement for the sale and servicing of cellular telephones with AT&T. The agreement provided for arbitration of all disputes between the parties. The agreement specified that all claims be brought in the parties' "individual capacity, and not as a plaintiff or class member in any purported class or representative proceeding." Subsequently, the Concepcions filed suit against AT&T in federal court over a dispute regarding their cell phone contract.

AT&T moved to compel arbitration pursuant to the terms of the contract it held with the Concepcions. The arbitration agreement included favorable terms for customers – claims could be brought in the county in which the plaintiff resided or in magistrate court, and provided that AT&T would pay at a minimum a recovery of $7,500, plus twice the amount of the plaintiff's attorneys' fees, if a plaintiff obtained an award greater than AT&T's final settlement offer. The District Court denied AT&T's motion based on a California Supreme Court case, *Discover Bank v. Superior Court*, 113 P.3d 1100 (2005), which held that arbitration provisions in most consumer contracts are unconscionable. The Ninth Circuit affirmed, holding that the *Discover Bank* rule was not preempted by the Federal Arbitration Act (FAA) because that rule was applicable to contracts generally in California.

Section 2 of the FAA makes arbitration agreements "valid, irrevocable, and

enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. §2. Under California law, courts may refuse to enforce contracts based on the doctrine of unconscionability. In *Discover Bank*, the California Supreme Court essentially held that class-action waivers in arbitration agreements in the consumer context were unconscionable, and thus unenforceable. In *Concepcion*, the United States Supreme Court framed the issue before it as: "whether §2 [of the FAA] preempts California's rule classifying most collective-arbitration waivers in consumer contracts as unconscionable."

The United States Supreme Court held that requiring classwide arbitration would interfere with the fundamental attributes of arbitration, and noted that the "principle purpose of the FAA is to ensure that private arbitration agreements are enforced according to their terms." To that end, parties may agree to limit the issues subject to arbitration, arbitrate according to specific rules, and limit *with whom* a party will arbitrate its disputes. By applying the *Discover Bank* rule, the California courts interfere with the principle purpose of arbitration. The Court went on discuss how class arbitration differs from bilateral arbitration by 1) undermining the efficiency of arbitration by making arbitration slower and more expensive; 2) requiring procedural formality; and 3) increasing the risks to the defendant, because mistakes are more frequent in arbitration, and the effect of any mistake would be magnified with class arbitration.

Application to Employers

Employers have no greater weapons to prevent collective or class-action lawsuits by employees than the Supreme Court's decisions in *Concepcion* and *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758 (2010). In *Stolt-Nielsen*, the Supreme Court held that "a party may not be compelled under the [FAA] to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so." (For a link to Ford & Harrison's Legal Alert regarding the *Stolt-Nielsen* decision, click here or go to http://www.fordharrison.com/shownews.aspx?show=6159). In *Concepcion*, the Court took an additional step in enforcing arbitration agreements that contain class-action waivers.

Class- and collective-action claims are becoming increasingly frequent and expensive for employers, with claims arising under the Fair Labor Standards Act (FLSA) and state wage-hour claims leading the way. Although *Concepcion* involved a consumer contract, the Court's analysis likely would apply to arbitration agreements in the employment context. If anything, consumer contracts, like those in *Concepcion*, are more "unconscionable" than those found in the employment context because employment claims are often brought individually and are generally for more money than consumer contracts. Usage of class-action waivers will undoubtedly face additional obstacles – i.e. the National Labor Relations Board has filed charges alleging that class-action waivers violate employees' right to engage in concerted activities – however, this opinion is another strong signal from the United States Supreme Court that it will favor the FAA and arbitration agreements entered into between parties. Arbitration agreements could be used to significantly reduce liability from class-action claims.

Employers' Bottom Line

Employers stand to benefit tremendously from the Supreme Court's

Concepcion decision, if they wish to implement arbitration agreements to avoid class actions. Employers would have a variety of options to implement arbitration agreements with class-action waivers. These arbitration agreements can be tailored to fit an employer's specific needs. For example, the agreement could apply only to wage-hour claims, leaving claims arising under Title VII to federal courts. Employers should consider whether using arbitration agreements would suit their employment needs.

If you have any questions regarding the Court's decision or the issues addressed in this Alert, please contact the authors, John Allgood, jallgood@fordharrison.com, Jeff Mokotoff, jmokotoff@fordharrison.com, or Henry Warnock, hwarnock@fordharrison.com, attorneys in our Atlanta office, or the Ford & Harrison attorney with whom you usually work.