No. 09-893

In the Supreme Court of the United States

AT&T MOBILITY LLC,

Petitioner,

v.

VINCENT AND LIZA CONCEPCION,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF THE *AMICUS CURIAE*[1]

The Chamber of Commerce of the United States of America is the world's largest federation of businesses and associations. The Chamber represents three hundred thousand direct members and indirectly represents an underlying membership of more than three million U.S. businesses and professional organizations of every size and in every economic sector and geographic region of the country. An important function of the Chamber is to represent the interests of its members in matters before the courts, Congress, and the Executive Branch. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of vital concern to the nation's business community.

Many of the Chamber's members and affiliates regularly employ agreements to arbitrate in their business contracts with their customers and employees. By agreeing to arbitrate with their counterparties, they avoid costly and time-consuming litigation when disputes arise. In its place, they adopt a dispute resolution mechanism that is speedy, fair, inexpensive, and effective. Based on the legislative policy reflected in the Federal Arbitration Act (FAA) and this Court's consistent endorsement of arbitration over the past several decades, Chamber members

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[1] No counsel for a party wrote this brief in whole or in part, and no counsel for a party or party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than *amicus curiae*, its members, or its counsel made a monetary contribution to this brief's preparation or submission. Both petitioner and respondents have filed blanket consents to *amicus* briefs; the consents are reflected on the Court's docket.

have structured millions of contractual relationships around arbitration agreements.

A class-arbitration waiver is a key component of many Chamber members' arbitration agreements. Decisions like the opinion below, which invalidated a class-arbitration waiver, frustrate the parties' intent, undermine their existing agreements, and erode the benefits offered by arbitration as an alternative to litigation. Because so many of the advantages of arbitration would be lost if the Ninth Circuit's decision were affirmed, the Chamber has a strong interest in this case.

INTRODUCTION AND SUMMARY OF ARGUMENT

Congress enacted the FAA to stop courts from discriminating against arbitration agreements. Congress did so because it recognized that arbitration is a desirable alternative to more costly and time-consuming litigation. Here, petitioner AT&T Mobility LLC (ATTM) sought to avail itself of those benefits. The court below held that it could not do so, however, at least not unless ATTM also agreed to allow for class arbitration. The court said that class arbitration was necessary as a matter of California judicial policy, notwithstanding the FAA.

ATTM explains why the decision below disregards the FAA in practice, even if it pretends to adhere to it in form. The Chamber generally agrees with, and will not repeat, ATTM's arguments. This brief identifies further errors in the Ninth Circuit's reasoning.

I. The court below struck ATTM's class-arbitration waiver as unconscionable because the court thought

that class arbitration must be available to deter unlawful conduct. That reasoning is erroneous.

First, multiple factors—among them, the availability of other private remedies and the existence of robust public law enforcement authority—dramatically reduce the need for devices like class arbitration that allegedly provide further deterrence.

Second, insofar as a lingering need for deterrence remains, class arbitration does not provide it. Both logic and a wealth of empirical evidence make clear that the threat of class actions, whether through litigation or arbitration, does not discourage unlawful behavior.

Third, a predictable effect of forcing class arbitration on businesses (and consumers) that do not want it is to cause businesses to forgo arbitration entirely. At least for the many cases in which the requirements for class certification are not met, consumers will then have no place to turn but to prohibitively expensive litigation—or to abandon their claims in frustration.

II. The FAA preempts the attempted application of unconscionability doctrine in this case for at least four reasons. First, the decision below reflects the very hostility to arbitration that the FAA was enacted to counteract. Second, the specialized formulation of the unconscionability doctrine for cases involving class-action waivers in general, and this case in particular, is not a recognizable or defensible application of the general California law of unconscionability. Third, even if it were, the Ninth Circuit and California courts apply that formulation to dispute resolution contracts only, and not to all contracts, as the

courts must for the state law to come within the savings clause of Section 2 of the FAA.

Fourth, and overarchingly, by holding that there can be no arbitration that does not also allow for class arbitration, the decision below attacks the very purpose of the FAA: to provide parties a lower-cost alternative to litigation. Class arbitration is enormously more expensive and complex than traditional, bilateral arbitration. At a minimum, the FAA preempts state judicial rules that superimpose onto arbitration agreements a procedure (class arbitration) that is so "fundamental[ly]" and "crucial[ly]" different from bilateral arbitration that some businesses have already chosen to forgo arbitration entirely rather than submit to it. *Stolt-Nielsen S.A.* v. *Animalfeeds Int'l Corp.*, 130 S. Ct. 1758, 1776 (2010).

ARGUMENT

I. Class Arbitration Does Not Deter Misconduct, But Forces Consumers Into Costly Litigation

The court below held that the class-arbitration waiver to which ATTM and respondents agreed was unconscionable because the court thought the provision was "in effect an exculpatory clause." Pet. App. 11a. The court reasoned that class arbitration must be available to deter businesses from "exact[ing] small sums from millions of consumers." *Id.* at 7a (internal quotation marks omitted).

That reasoning is erroneous. Logic and empirical evidence make clear that class actions do not deter unlawful behavior. Rather, the most likely effect of forcing class arbitration on companies is to cause them to abandon arbitration altogether, as Comcast

Corp., the nation's largest cable services provider, has already done. To the extent such abandonment occurs, consumers and employees will lose the many benefits of arbitration as they are herded into onerous litigation—or, more likely, at least for the many consumers and employees whose claims do not meet the stringent prerequisites for class certification, simply abandon their claims in frustration. The thinness of the Ninth Circuit's reasoning on this score, and of the California decisions on which the Ninth Circuit relied, suggests the true motivation for discriminating against class-arbitration waivers: the same hostility to arbitration agreements that Congress tried to eradicate more than 80 years ago and that this Court has sought to abolish ever since.

We elaborate these points below. We begin by observing that in this case the need for deterrence is minimal, and thus so is the benefit to be had from any additional deterrent device.

A. There Are More Important Deterrents To Unlawful Conduct Than Class Actions

The primary function of private civil litigation is compensation of injured plaintiffs. The primary function of class actions is the same: properly certified and circumscribed class actions enable plaintiffs to litigate "a suit involving common questions when there are too many plaintiffs for proper joinder." *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 809 (1985).

Deterrence is a secondary function of private civil litigation, but the American legal system has other mechanisms for achieving deterrence as their *primary* purpose. Severe corporate misconduct has been subjected to criminal sanctions. Criminal law aside,

the American legal system has a host of mechanisms for *public* pursuit and punishment of corporate misconduct. One of the laws at issue in this case, for example, empowers the state Attorney General and local prosecutors to enforce the law through civil penalties and injunctive relief. See CAL. BUS. & PROF. CODE §§ 17204, 17206. In addition, federal regulators such as the Federal Trade Commission and Federal Communications Commission have multiple tools to protect consumers from unscrupulous practices by businesses in general and telecommunications companies in particular. See, *e.g.*, Federal Trade Commission Act § 5, 15 U.S.C. § 45(a) (allowing FTC to take action against "unfair or deceptive acts or practices" in interstate commerce); 47 U.S.C. § 201(b) (allowing FCC to define and prohibit "unjust or unreasonable" practices by carriers).

State and federal law enforcement authority are powerful deterrents of unlawful conduct. See, *e.g.*, *Iberia Credit Bureau, Inc.* v. *Cingular Wireless LLC*, 379 F.3d 159, 175 (5th Cir. 2004) (state law enforcement mechanisms "further tend[] to show" that class-arbitration waivers do "not leave the plaintiffs without remedies or so oppress them as to rise to the level of unconscionability"); cf. *Gilmer* v. *Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28-29 (1991) (rejecting argument that arbitration in lieu of agency proceedings would undermine the role of the EEOC in enforcing the Age Discrimination in Employment Act of 1967); *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279 (2002) (similar). Because these other public law-enforcement mechanisms exist, private parties are free to resolve their disputes through alternative arrangements, unless "Congress itself has evinced an

intention to preclude" them from doing so. *Gilmer*, 500 U.S. at 26 (internal quotation marks omitted).

B. Class Arbitration Does Not Deter Misconduct

The court below thought that class arbitration will deter unlawful behavior by increasing the liability a defendant faces for committing such misconduct. See Pet. App. 7a. That analysis ignores the practical financial incentives that govern plaintiffs, defendants, and their lawyers.

Litigation is enormously expensive to businesses because of the cost of discovery and related distractions and lost business opportunities. That is true of individual lawsuits alone. But, if the action is brought on behalf of not one plaintiff but hundreds or thousands or more, the stakes skyrocket. Whether the forum is arbitral or judicial, once a class is certified an action that individually might be worth only a few hundred dollars or less can instantly metastasize into a potentially catastrophic judgment of hundreds of millions or even billions of dollars of damages. Defendants will almost inevitably settle in those circumstances. See, *e.g.*, Michael E. Solimine & Christine Oliver Hines, *Deciding to Decide: Class Action Certification and Interlocutory Review by the United States Courts of Appeals Under Rule 23(f)*, 41 WM. & MARY L. REV. 1531, 1546 n.74 (2000) ("[T]hat defendants would rather settle large class actions than face the risk, even if it be small, of crushing liability from an adverse judgment on the merits is widely recognized."); see also *id.* at 1546 (observing that class certification "has a huge impact on the subsequent course of the litigation").

That observation might be consistent with the Ninth Circuit's idea that class actions deter misconduct *if* there were a high correlation between the merits of a plaintiff's claim and a defendant's decision to settle. But there is not, for the same reasons described above. Defendants have a financial incentive to settle class actions even when the plaintiff's claim has little or no merit. Basic mathematics and risk aversion make it so: Attorneys' fees aside, a risk-averse defendant that thinks it has a 90 percent chance of defeating a $100 million class action is still better off settling for $9.9 million. The result is an *in terrorem* effect that compels defendants to settle claims that have no merit. See, *e.g.*, *Shady Grove Orthopedic Assocs., P.A.* v. *Allstate Ins. Co.*, 130 S. Ct. 1431, 1465 n.3 (2010) (Ginsburg, J., dissenting) ("A court's decision to certify a class * * * places pressure on the defendant to settle even unmeritorious claims.").[2] The pressure to settle is only amplified when the class action is an arbitration, and the company's fate is committed to an arbitrator whose decisions are subject to review that is "among the nar-

[2] Echoing Judge Friendly, distinguished jurists have lamented these "blackmail settlements." See, *e.g.*, *In re Rhone-Poulenc Rorer Inc.*, 51 F.3d 1293, 1298 (7th Cir. 1995) (Posner, J.) (citing HENRY J. FRIENDLY, FEDERAL JURISDICTION: A GENERAL VIEW 120 (1973)); *In re Lorazepam & Clorazepate Antitrust Litig.*, 289 F.3d 98, 102 (D.C. Cir. 2002) ("[T]he grant of class status can put substantial pressure on the defendant to settle independent of the merits of the plaintiffs' claims."); see also Linda Silberman, *The Vicissitudes of the American Class Action – With a Comparative Eye*, 7 TUL. J. INT'L & COMP. L. 201, 205 (1999) ("[T]he specter of huge damage awards against defendants in a class action suit and the expense of litigating these large suits in a system without cost-shifting frequently led defendants to settle even marginal cases, with the settlement often including substantial attorneys' fees for the class lawyers.").

rowest known to law." *Dominion Video Satellite, Inc.* v. *EchoStar Satellite L.L.C.*, 430 F.3d 1269, 1275 (10th Cir. 2005) (internal quotation marks omitted).

Plaintiffs and their lawyers obviously know this, and they adapt their behavior accordingly. So long as defendants are likely to settle litigation or arbitration whenever a class is certified, plaintiffs' lawyers have an incentive to seek such certification, even if their clients deserve no compensation. See, *e.g.*, Robert G. Bone & David S. Evans, *Class Certification and the Substantive Merits*, 51 DUKE L.J. 1251, 1291–1292 (2002) (observing "what most class action lawyers know to be true: almost all class actions settle, and the class obtains substantial settlement leverage from a favorable certification decision").

Plaintiffs' lawyers have wasted no time in taking advantage of California's refusal to enforce class-arbitration waivers. Already, they have persuaded the Ninth Circuit not to enforce Texas law, which upholds class-action waivers, see Pet. App. 68a, even though Texas law was explicitly provided for in a choice-of-law clause to which all the parties agreed. See *Omstead* v. *Dell, Inc.*, 594 F.3d 1081, 1083, 1086 (9th Cir. 2010) (choice-of-law provision is unenforceable in part because "application of [Texas] law would be contrary to a fundamental policy of California because the sales agreement's class action waiver was unconscionable under California law"). *Omstead* at least involved a class of California plaintiffs objecting to the application of another State's law. See *id.* at 1083 n1. But forum-shopping counsel have been audacious enough to bring class actions in California on behalf of *non-California residents* whose *home States would have compelled arbitration*—and, what is more, the lawyers have done so with success. See,

e.g., *Masters* v. *DirecTV, Inc.*, Nos. 08-55825, 08-55830, 2009 WL 4885132, at *1 (9th Cir. Nov. 19, 2009) (unpublished).

Taken together, these incentives nullify whatever deterrent effect a class device might have. If, from a defendant's perspective, it will face class arbitration and be forced to settle *regardless* of whether it acts unlawfully, then the defendant has no financial incentive to alter its behavior one way or the other. See, *e.g.*, A. MITCHELL POLINSKY & STEVEN SHAVELL, *The Theory Of Public Enforcement of Law*, *in* 1 HANDBOOK OF LAW AND ECONOMICS 404, 427 (2007). In fact, as discussed later, see *infra* I.C, a defendant has an affirmative ***dis***incentive to invest in arbitration at all, in light of the great costs and few benefits to it of class arbitration.

The empirical literature bears these observations out. One respected study of securities class actions from the Stanford Law Review concluded that the chief determinants of whether plaintiffs would bring suit, and the size of the resulting settlements, were the decline in a defendant's stock price and the amount of the defendant's insurance coverage. Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 516–519 (1991). By contrast, the merits of the plaintiff's underlying suit had little effect on the defendant's decision to settle. *Ibid.* Other studies have found similar results. See, *e.g.*, Patrick M. Garry et al., *The Irrationality of Shareholder Class Action Lawsuits: A Proposal for Reform*, 49 S.D. L. REV. 275, 287 n.98 (2005); James Bohn & Stephen Choi, *Fraud in the New-Issues Market: Empirical Evidence on Securities Class Actions*, 144 U. PA. L. REV. 903, 979–980 (1996); Joseph A. Grundfest, *Why*

Disimply?, 108 HARV. L. REV. 727, 742–743 (1995). This case involves a consumer class action and not a securities class action, and the stakes are perhaps lower, but the underlying logic is the same because in each case the risk of a judgment large in comparison to the profitability of the challenged activity creates a powerful incentive to settle even unmeritorious suits. Indeed, because defense costs tend to be a smaller fraction of the potential damages at stake in a case seeking enormous class damages than in a case seeking lesser class damages, defendants may have even more of an incentive to settle the lesser cases.

The decision below addresses none of these points. It does not explain why these predictable incentives will not cause plaintiffs to bring class actions—and defendants to settle them—even when the actions have no merit. Nor does it rebut empirical findings like those above. The decision does not, for that matter, consult *any* empirical evidence, even though the question whether class arbitration deters misconduct is amenable to empirical study. Instead, the court merely speculated that, if the amount of liability is large enough, defendants will engage in a smaller amount of unlawful behavior. The conclusion simply does not follow from the premise.

C. The Decision Below Will Cause Many Businesses To Abandon Arbitration Altogether, Forcing Consumers To Litigate Or Give Up Their Claims

Few companies will bind themselves to agreements that allow for class arbitration when the companies can simply abandon arbitration altogether instead. Whereas individual arbitration simplifies, speeds, and reduces expense, class arbitration com-

plicates, slows, and increases expense. Class arbitration does so to such a degree, moreover, that its costs dwarf the benefits of individual arbitration. Businesses will likely forgo arbitration entirely before they will choose to suffer class arbitration. Consumers will then have no option but to litigate their claims or to give up.

1. The virtues of individual (*i.e.*, bilateral) arbitration have been lauded frequently by scholars, practitioners, Congress, and courts, particularly this Court. Above all, arbitration gives consumers "a less expensive alternative to litigation." *Allied-Bruce Terminix Cos.* v. *Dobson*, 513 U.S. 265, 280–281 (1995); *14 Penn Plaza LLC* v. *Pyett*, 129 S. Ct. 1456, 1464 (2009) (same); *Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 633 (1985) (same). Its streamlined procedures minimize the "delays, expense, uncertainties, loss of control, * * * and animosities that frequently accompany litigation." Y2K Act, Pub. L. No. 106-37, §§ 2(a)(3)(B)(iv), 2(b)(3), 113 Stat. 185, 186–187 (1999) (encouraging businesses and users of technology to use "alternative dispute mechanisms" to avoid "costly and time-consuming litigation"); see also *Stolt-Nielsen*, 130 S. Ct. at 1775 ("In bilateral arbitration, parties forgo the procedural rigor and appellate review of the courts in order to realize the benefits of private dispute resolution: lower costs, greater efficiency and speed, and the ability to choose expert adjudicators to resolve specialized disputes.").

In addition, consumers tend to "fare better in arbitration, both in terms of the likelihood of success on the merits and the size of the award, than in litigation." Joshua S. Lipshutz, Note, *The Court's Implicit Roadmap: Charting the Prudent Course at the Junc-*

ture of Mandatory Arbitration Agreements and Class Action Lawsuits, 57 STAN. L. REV. 1677, 1712 (2005). It is not surprising, then, that consumers—as opposed to the plaintiffs' bar and certain courts—have largely been satisfied with arbitration as an alternative to litigation. See Harris Interactive, *Arbitration: Simpler, Cheaper, and Faster Than Litigation* 24–28 (2005), *available at* http://www.adrforum.com /rcontrol/documents/ResearchStudiesAndStatistics/ 2005HarrisPoll.pdf.

Not so with class arbitration. It shares with individual arbitration a name only. The differences are "fundamental" and "crucial." *Stolt-Nielsen*, 130 S. Ct. at 1776.

An arbitrator "no longer resolves a single dispute between the parties to a single agreement, but instead resolves many disputes between hundreds or perhaps even thousands of parties." *Stolt-Nielsen*, 130 S. Ct. at 1776. With more people come more rules. The American Arbitration Association's (AAA) rules governing class arbitrations mimic the Federal Rules of Civil Procedure for class litigation. See AAA, Supplementary Rules for Class Arbitrations, *available at* http://www.adr.org/sp.asp?id=21936. For example, class arbitration demands the same onerous class certification determinations that class litigation requires. See *id.* at Rules 4–5. Class arbitrations can thus be just as time-consuming, procedurally complex, and expensive as traditional class litigation—perhaps even more so, because once a class determination is made the arbitrator "shall" stay all proceedings "for a period of at least 30 days to permit any party to move a court * * * to confirm or to vacate" the decision. *Id.* at Rule 5(d). And, under the AAA rules, "the presumption of privacy and confidentiality

that applies in many bilateral arbitrations shall not apply in class arbitrations." *Stolt-Nielsen*, 130 S. Ct. at 1776 (internal quotation marks omitted); see AAA Supplementary Rules at Rule 9(a). Just last Term, those differences led this Court to conclude that "class-action arbitration changes the nature of arbitration to such a degree" that one cannot presume that parties have consented to it without affirmative evidence. *Stolt-Nielsen*, 130 S. Ct. at 1775.

Cost and complexity aside, what makes class arbitration truly intolerable to many businesses is the nature of the adverse judgments it can produce. Like class litigation, class arbitration can cripple a business with a gargantuan judgment. But unlike class litigation, where appellate review of a court's certification and merits decisions is robust, the standard for vacating an arbitrator's decision is "among the narrowest known to law." *Dominion Video Satellite, Inc.*, 430 F.3d at 1275 (internal quotation marks omitted); see also *Stolt-Nielsen*, 130 S. Ct. at 1776 ("[T]he commercial stakes of class-action arbitration are comparable to those of class-action litigation, even though the scope of judicial review is much more limited." (citation omitted)); *id.* at 1767 (an arbitrator's decision will not be overturned unless the arbitrator "effectively 'dispense[s] his own brand of industrial justice'").

Even if a business defeats a class arbitration, there is no guarantee that the judgment will have the same preclusive effect that it would have in class litigation. Among other reasons, nonparticipating consumers can argue colorably that they cannot be bound by a decision of an arbitrator whom they had no say in choosing. See generally Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class*

Action, Will the Class Action Survive?, 42 WM. & MARY L. REV. 1, 113 (2000); see also Edward K.M. Bilich, *Consumer Arbitration: A Class Action Panacea?*, 7 CLASS ACTION LITIG. REP. (BNA) 768, 771 (2006) (class arbitration proceedings may not bind all class members because of the "deferential standard of review" applied to arbitrators' decisions). On nearly every dimension, then, class arbitration has the costs but not the benefits of individual arbitration.

Given the choice, businesses will likely forgo arbitration entirely before they will suffer class arbitration. Comcast Corp., the country's largest cable company, has already done so. It generally refuses to allow any of its California customers to arbitrate, *even if* the customers would have done so individually and not as a class. See Comcast Agreement for Residential Services § 13.k, *available at* http://www.comcast.net/terms/subscriber/ ("**SPECIAL NOTE REGARDING ARBITRATION FOR CALIFORNIA CUSTOMERS:** IF YOU ARE A COMCAST CUSTOMER IN CALIFORNIA, COMCAST WILL NOT SEEK TO ENFORCE THE ARBITRATION PROVISION ABOVE UNLESS WE HAVE NOTIFIED YOU OTHERWISE.") (emphasis in original).[3] Other large and important companies that deal with consumers are poised to do the same. Both Verizon[4]

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[3] See also *Kristian* v. *Comcast Corp.*, 469 F. Supp. 2d 1, 1 (D. Mass. 2006) (Comcast declines to arbitrate after the court of appeals struck its class-action waiver but allowed Comcast to withdraw from arbitration).

[4] Verizon Wireless Service Agreement, *available at* http://www.verizonwireless.com/text-01/CUSTOMER_AGREEMENT/footer--customerAgreement.jsp.shtml ("**[i]f for some reason the prohibition on class arbitrations * * * cannot be enforced, then the agreement to arbitrate will not apply.**") (emphasis in original).

and Sprint,[5] for example, include nonseverability clauses in their arbitration agreements that declare the entire agreement inapplicable if the class-waiver provision is deemed unenforceable. It is a short step from such provisions to Comcast's blanket ban on arbitration for all California customers.

The companies listed above are just a handful in the telecommunications business. We should expect the same flight from arbitration in the many other industries that rely on bilateral arbitration to minimize their dispute resolution costs, including credit, brokerage, insurance, financial services, legal, accounting, health care services, and still others. Like Sprint's and Verizon's, for example, American Express's Cardmember Agreement states that "THERE SHALL BE NO RIGHT OR AUTHORITY FOR ANY CLAIMS TO BE ARBITRATED ON A CLASS ACTION BASIS," and that, "should any portion of this Restrictions on Arbitration subsection be deemed invalid or unenforceable, then the entire Arbitration provision * * * shall not apply."[6]

2. Without the ability to resolve disputes efficiently through bilateral arbitration, consumers will

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[5] Sprint Terms & Conditions, *available at* http://shop.sprint.com/en/legal/legal_terms_privacy_popup.shtml ("**If for any reason any court or arbitrator holds that this restriction [against class arbitration] is unconscionable or unenforceable, then our agreement to arbitrate doesn't apply and the dispute must be brought in court**.") (emphasis in original).

[6] American Express Cardmember Agreement, Delta SkyMiles Credit Card, *available at* https://secure.cmax.americanexpress.com/Internet/UDAP/CardMemberAgreementsOnline/US_en/CMADetailsPage/PersonalCards/DeltaSkyMiles/DeltaSkyMiles.pdf.

lose at least as much as businesses will, probably more. Consumers have no other realistic place to turn. Surely class *litigation* is not the answer. To begin with, the door is tough to open. Even though courts continue to certify many class actions that should not be certified—see, *e.g.*, *Dukes* v. *Wal-Mart Stores, Inc.*, 603 F.3d 571, 628 (9th Cir. 2010) (en banc) (Ikuta, J., dissenting)—the fact remains that only 20% of putative classes are certified. Thomas E. Willging & Shannon R. Wheatman, *Attorney Choice of Forum in Class Action Litigation: What Difference Does It Make?*, 81 NOTRE DAME L. REV. 591, 635–636 (2006); Judicial Council of California, *Class Certification in California: Second Interim Report from the Study of California Class Action Litigation* 5 (2010), *available at* http://www.courtinfo.ca.gov/reference/documents/classaction-certification.pdf. Certification is not allowed unless "the trial court is satisfied[] after a rigorous analysis" that common questions of law and fact predominate over questions affecting only individual members. *Gen. Tel. Co.* v. *Falcon*, 457 U.S. 147, 161 (1982). Most consumer claims that could have been arbitrated will not survive the trial court's "close look." *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591, 615 (1997) (internal quotation marks omitted).

Even if they do, the consumer—as opposed to her attorney—is unlikely to see any money. Class-action litigation can drag on for years in pursuit of "relatively paltry potential [individual] recoveries." *Amchem*, 521 U.S. at 617 (internal quotation marks omitted). This may be why Congress found that "[c]lass members often receive little or no benefit from class actions, and are sometimes harmed." Class Action Fairness Act of 2005, Pub. L. No. 109-2,

§ 2(a)(3), 119 Stat. 4. Lawyer fees, on the other hand, usually consume a large chunk of a class's recovery. As the district court observed, "class members rarely receive more than pennies on the dollar for their claims, and * * * few class members (approximately 1–3%) bother to file a claim when the amount they would receive is small." Pet. App. 41a.

Or the recovery might not entail any money for consumers at all. Coupon-based settlements, in which consumers receive vouchers redeemable for goods or services in lieu of cash, have grown common in consumer class actions. See Christopher R. Leslie, *A Market-Based Approach to Coupon Settlements in Antitrust and Consumer Class Action Litigation*, 49 UCLA L. REV. 991, 993–994 (2002). But restrictions on consumers' ability to redeem the coupons can reduce the value of these settlements dramatically. See *id.* at 996. Congress tried to close this loophole in the Class Action Fairness Act, but failed. See, *e.g.*, Edward A. Purcell, Jr., *The Class Action Fairness Act in Perspective: The Old and the New in Federal Jurisdictional Reform*, 156 U. PA. L. REV. 1823, 1873–1874 (2008); Robert H. Klonoff & Mark Herrmann, *The Class Action Fairness Act: An Ill-Conceived Approach to Class Settlements*, 80 TUL. L. REV. 1695, 1698–1705 (2006).

The only people who are almost sure to profit from class actions are the attorneys who bring them. See, *e.g.*, 151 CONG. REC. H726 (daily ed. Feb. 17, 2005) (statement of Rep. Sensenbrenner) ("The class action judicial system has become a joke, and no one is laughing except the trial lawyers * * * all the way to the bank." (internal quotation marks omitted)); Samuel Issacharoff & Robert H. Klonoff, *The Public Value of Settlement*, 78 FORDHAM L. REV. 1177, 1189

(2009) ("In some settlements, such as 'coupon' settlements, * * * class counsel receive large fees while class members receive little or nothing of actual value."). Class counsel and defendants each have an incentive to settle on terms that may be unfavorable to the plaintiff consumers but reap large fees to counsel. See Jill E. Fisch, *Class Action Reform,* Qui Tam*, and the Role of the Plaintiff*, 60 L. & CONTEMP. PROBS. 167, 168 (1997) ("Particularly problematic is the possibility that class action litigation will produce handsome compensation for class counsel but little discernible benefit for class members."); see also, *e.g.*, *Mirfasihi* v. *Fleet Mortgage Corp.*, 356 F.3d 781, 783, 785 (7th Cir. 2004) (class of 1.4 million customers settled for less than $2.5 million).

With class litigation often a dead end, and businesses likely unwilling to arbitrate under California's terms, consumers will have nowhere to turn but to individual litigation. But in small-stakes cases, other than those amenable to litigation in small claims court, such litigation is also a dead end. As one court colorfully put it, "only a lunatic or a fanatic sues for $30." *Carnegie* v. *Household Int'l, Inc.*, 376 F.3d 656, 661 (7th Cir. 2004).

Because of the decision below, meritorious claims that could have been arbitrated—and, under ATTM's agreement, would likely have been compensated in full or more, see Pet. App. 39a—will go unprosecuted. In exchange, consumers will receive only a device that does not deter unlawful conduct and that, in any event, businesses will almost surely reject, as they are entitled to do.

II. California's Manipulation Of Unconscionability Doctrine To Invalidate ATTM's Class-Arbitration Waiver Is Preempted By The FAA

1. Ironically, and perversely, for the reasons given above the Ninth Circuit's insistence on superimposing California's public policy will do no more than send consumers right back where they were almost a century ago, before Congress enacted the FAA to avoid this very scenario. That may ultimately be the underlying motivation for the California and Ninth Circuit decisions that have caused the issue in the present case to come before this Court.

It is no secret that, despite the FAA and this Court's repeated admonitions, some lower courts still harbor prejudice against arbitration. See, *e.g.*, Susan Randall, *Judicial Attitudes Toward Arbitration and the Resurgence of Unconscionability*, 52 BUFF. L. REV. 185, 186 (2004) ("[J]udges find unconscionable specific features of arbitration agreements, such as forum selection clauses and confidentiality requirements, which are routinely enforced as unobjectionable in nonarbitration agreements."); Stephen J. Ware, *Arbitration and Unconscionability After* Doctor's Associates, Inc. v. Casarotto, 31 WAKE FOREST L. REV. 1001, 1034 (1996) ("Judicial decisions apply unconscionability, and other common law doctrines, more aggressively to arbitration agreements than to other contracts."). Moreover, evidence suggests that the prejudice may be geographically concentrated. See Michael G. McGuinness & Adam J. Karr, *California's "Unique" Approach to Arbitration: Why This Road Less Traveled Will Make All the Difference on the Issue of Preemption Under the Federal Arbitration Act*, 2005 J. DISP. RESOL. 61, 62 ("California has created a

new brand of unconscionability. It is far more demanding—and it is unique to arbitration.").[7]

Whatever the reason for the prejudice, the FAA explicitly proscribes it. 9 U.S.C. § 2 (an arbitration provision "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract"). It is no absolution under the FAA for a court to obscure its prejudice beneath the veneer that class arbitration deters misconduct, especially when the foreseeable price of that feeble deterrent is to cause businesses to give up arbitration entirely. See *Circuit City Stores, Inc.* v. *Adams*, 532 U.S. 105, 122 (2001) (courts may not "chip away at [the FAA] by indirection"). California's jerry-built unconscionability doctrine for class-arbitration waivers runs afoul of Congress's "liberal federal policy favoring arbitration agreements," *Waffle House, Inc.*, 534 U.S. at 289 (internal quotation marks omitted), and this Court's admonition that States may *not* "decide that a contract is fair enough to enforce all its basic terms * * * but not fair enough to enforce its arbitration clause," *Allied-Bruce*, 513 U.S. at 281. The decision below does exactly that and is therefore preempted by the FAA.

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[7] In contrast to their practice twenty years ago, courts—especially California courts—are now nearly twice as likely to find arbitration agreements unconscionable as they are any other contract. See Randall, *supra*, 52 BUFF. L. REV. at 187; see also Stephen A. Broome, *An Unconscionable Application of the Unconscionability Doctrine: How the California Courts are Circumventing the Federal Arbitration Act*, 3 HASTINGS BUS. L.J. 39, 39 (2006) ("While in most jurisdictions the judiciary has long abandoned its historical hostility to arbitration as an alternative to litigation, * * * in California the courts continue to view arbitration agreements critically.").

2. Even aside from the motivation of the courts that have adopted and applied the rule of *Discover Bank* v. *Super. Ct.*, 113 P.3d 1100, 1103 (Cal. 2005), the rule is preempted by the FAA because it is not a rule applicable to all contracts generally. Although cast as "simply a refinement of the unconscionability analysis applicable to contracts generally in California," Pet. App. 12a–13a (quoting *Shroyer* v. *New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 987 (9th Cir. 2007)), the *Discover Bank* rule distorts the traditional analysis profoundly.

In place of the usual substantive unconscionability test, the California courts have substituted a test crafted specifically to deal with class-action waivers in arbitration agreements, and the Ninth Circuit has followed it. See Pet. App. 4a–11a. The cases in this line are irreconcilable with Section 2 of the FAA and this Court's cases interpreting it, which permit the invalidation of agreements to arbitrate only "upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added).

Unconscionability is, "by its very nature, vaguely defined," McGuinness & Karr, *supra*, 2005 J. DISP. RESOL. at 74 (citing JOSEPH M. PERILLO, CORBIN ON CONTRACTS: AVOIDANCE AND REFORMATION § 29.1 (rev. ed. 2002)), but there are limits to the doctrine's reach. Ordinarily, to find a contract unconscionable, California courts require some combination of "procedural" and "substantive" unconscionability. *Discover Bank*, 113 P.3d at 1108; see also Randall, *supra*, 52 BUFF. L. REV. at 191 (observing that, according to the Uniform Commercial Code, "[c]ourts generally recognize two types of unconscionability * * * and may re-

quire the presence of both in order to find a particular agreement unconscionable").

Substantive unconscionability (the kind at issue here) "focuses on the actual terms of the agreement and evaluates whether they create 'overly harsh' or 'one-sided' results as to 'shock the conscience.'" *Aron* v. *U-Haul Co.*, 49 Cal. Rptr. 3d 555, 564 (Cal. Ct. App. 2006); accord *Discover Bank*, 113 P.3d at 1108 (observing that the substantive unconscionability test focuses on "overly harsh" or "one-sided" results). In California, as elsewhere, an unconscionable bargain is one such as "no man in his senses, and not under delusion, would make on the one hand, and as no honest and fair man would accept on the other." *Odell* v. *Moss*, 62 P. 555, 557 (Cal. 1900) (quoting 1 Story, *Eq. Jur.* §§ 244, *et seq.*); accord *Cal. Grocers Ass'n* v. *Bank of Am.*, 27 Cal. Rptr. 2d 396, 402 (Cal. Ct. App. 1994).

Despite these established principles, California courts and the Ninth Circuit have invoked substantive unconscionability to invalidate arbitration agreements on the basis of the class-action waivers contained in those agreements, even when it is clear that the waivers inflict no harm on the parties appearing before the court. To reach that result, the courts have applied California's *Discover Bank* rule, which was articulated for the first time by the California Supreme Court in a 2005 case addressing "the unconscionability of class action waivers in arbitration agreements." Pet. App. 5a.

Under the *Discover Bank* rule, the unconscionability of class-arbitration waivers turns not on their harshness or one-sidedness, but on three different factors, including whether it is "alleged that the party

with superior bargaining power has carried out a scheme deliberately to cheat large numbers of consumers out of individually small sums of money." Pet. App. 7a.[8] When such allegations have been made, California courts say, invalidation of class-arbitration waivers is necessary to deter companies from adopting policies that inflict small injuries on many people; when each injury is too small for an individual to bother pursuing, the "unscrupulous wrongdoer" will pocket "the benefits of its wrongful conduct." *Discover Bank*, 113 P.3d at 1106, 1108; see also Pet. App. 46a.

That rationale is wrong for all the reasons stated earlier in this brief. In any event, regardless of the proffered rationale, it is clear that the California courts are not invalidating class-arbitration waivers because they are "harsh" or "oppressive" to the contracting parties. As this case demonstrates, courts following the *Discover Bank* rule will invalidate the waivers even when the terms are admittedly those a reasonable person would want. See Pet. App. 4a–5a, 42a (invalidating ATTM's arbitration agreement because of its class-arbitration waiver even though the district court found that consumers "may well prefer" arbitration to a class action). At least with regard to class-action waivers, then, it seems "California has created a new brand of unconscionability," one that is "far more demanding" than the norm and "unique to

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[8] Courts applying the *Discover Bank* rule also consider whether the agreement is a contract of adhesion and whether disputes between the contracting parties are "likely to involve small amounts of damages." Pet. App. 7a. The Ninth Circuit has suggested that class-action waivers may be unconscionable even if they do not satisfy all three parts of the *Discover Bank* test. See *ibid.*

arbitration." McGuinness & Karr, *supra*, 2005 J. DISP. RESOL. at 62; see also Broome, *supra*, 3 HASTINGS BUS. L.J. at 39–40 ("Although ostensibly applying the 'generally applicable' contract defense of unconscionability, in cases involving the validity of arbitration agreements the California courts routinely apply an entirely different test, requiring less of parties seeking to avoid arbitration.").

3. Under the FAA, arbitration agreements must be enforced and interpreted under the same principles of contract law applicable to contracts generally, placing arbitration agreements "upon the same footing as other contracts." *Volt Info. Scis., Inc.* v. *Bd. of Trs. of Leland Stanford Jr. Univ.*, 489 U.S. 468, 474 (1989) (internal quotation marks omitted). For a state contract principle to override an arbitration agreement, it is insufficient that it avoids overt discrimination against arbitration; it must apply universally to "any" and every contract. This means courts may invalidate class-action waivers in arbitration agreements as unconscionable only if they have subjected the waivers to the same unconscionability analysis they would have applied to the terms of any other contract. See *Perry* v. *Thomas*, 482 U.S. 483, 492 n.9 (1987).

The unconscionability standard that the Ninth Circuit and California courts employ against class-action waivers is not a ground for the invalidation of "any" contract, as Section 2 of the FAA requires, but rather a rule applicable only to the subset of contracts that concern resolution of disputes. When parties agree to arbitrate, they agree to resolve any future differences out of court. And when California changes the rules of unconscionability governing agreements to resolve disputes out of court—here by

looking beyond the parties before the court to find unconscionability—it changes the rules of unconscionability that govern arbitration agreements.

That is precisely what the FAA prohibits. There is nothing objectionable about saying that a provision of an arbitration agreement may be invalidated because it is unconscionable under state law. See, *e.g.*, *Doctor's Assocs., Inc.* v. *Casarotto*, 517 U.S. 681, 686 (1996). The *ad hoc* manipulation of unconscionability doctrine, however, is inconsistent with this Court's admonition that state-law contract defenses may be used to void arbitration provisions only if they "arose to govern issues concerning the validity, revocability, and enforceability of contracts *generally*." *Perry*, 482 U.S. at 492 n.9 (emphasis added).

4. We add one further point. An overarching problem with the decision below is that the particular rule the court imposed—that there can be no arbitration unless there is also class arbitration—attacks the very core of what arbitration is. The only reason businesses choose to arbitrate is to "trade[] the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition of arbitration." *Mitsubishi Motors Corp.*, 473 U.S. at 628. Hence "parties may specify *with whom* they choose to arbitrate their disputes." *Stolt-Nielsen*, 130 S. Ct. at 1774 (emphasis in original). To force on businesses and consumers "crucial[ly]" different procedures that inflict the costs and complexity of litigation is to shove them into exactly the forum that the FAA lets them avoid. *Id.* at 1776.

So it is no defense for the court below to say that its prohibition against class waivers is lawful merely because the prohibition might in theory apply to liti-

gation, too. The very comparison is inappropriate. Our point is precisely that class arbitration makes arbitration too *similar* to litigation. Claiming that the rule applies equally to litigation is therefore no response. If the FAA stands for anything, it must be that a court cannot impose a rule that so "fundamental[ly]" and "crucial[ly]" changes the nature of arbitration that several major businesses have already determined that they will give up arbitration entirely before they will accept the rule. *Stolt-Nielsen*, 130 S. Ct. at 1776; see also *id.* at 1769 n.7 (rejecting the same argument the California courts and the Ninth Circuit invoked in invalidating the parties' class action waiver—namely, that class arbitration is necessary as a matter of public policy given the small value of plaintiffs' individual claims).[9]

[9] Another way to view the issue is from the perspective of the Congress that enacted the FAA in 1925. At that time, the only arbitration agreements that existed were bilateral ones. See *Discover Bank*, 113 P.3d at 1110 ("[N]ot only is classwide arbitration a relatively recent development, but class action litigation for damages was for the most part unknown in federal jurisdictions at the time the FAA was enacted in 1925.") The decision below explicitly outlaws such agreements by striking them unless they further permit class arbitration. In other words, the decision below invalidates exactly the type of agreement—bilateral arbitration—that the enacting Congress necessarily had in mind, and sought to protect, when it enacted the FAA. See generally David S. Clancy & Matthew M.K. Stein, *An Uninvited Guest: Class Arbitration and the Federal Arbitration Act's Legislative History*, 63 BUS. LAW. 55 (2007).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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AUGUST 2010