Arbitration Provisions Containing Class Action Waivers: Avoiding Financial Risk and Cost

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Following the United States Supreme Court's ruling in *AT&T Mobility LLC v. Concepcion*, financial institutions should look closely at including an arbitration provision containing a class action waiver in service agreements with their customers.

In *AT&T Mobility LLC v. Concepcion*, the Concepcions entered into an agreement for the sale and servicing of cellular phones with AT&T. The agreement provided for arbitration of all disputes between the parties, but required that a customer maintain his or her claim in an "individual capacity and not as a plaintiff or class member in any purported class or representative proceeding." The AT&T agreement is what is commonly referred to as a contract of adhesion because AT&T offered the contract on a take or leave it basis – the customer had no ability to negotiate its terms with AT&T.

Although AT&T dictated the agreement's terms, the agreement contained customer-friendly language. For example, customers could initiate dispute proceedings by completing a one-page "Notice of Dispute" form available on AT&T's website. Once dispute proceedings were initiated, AT&T could offer to settle the claim. *Id*. If AT&T and its customer were unable to settle or resolve the customer's claim within 30 days, the customer could invoke arbitration by filing a separate "Demand for Arbitration," by completing a simple form that was also available on AT&T's website. *Id*. Should the parties proceed to arbitration, AT&T's agreement provided for the following:

- AT&T paid all arbitration costs for nonfrivolous claims;
- The arbitration must take place in the county in which the customer was billed;
- For claims of $10,000 or less, the customer could choose whether the arbitration proceeded in person, by telephone, or based only on submissions;
- Any party could bring a claim in small claims court in lieu of arbitration;
- The arbitrator could award any form of individual relief, including injunctions and presumably punitive damages.
- The agreement denied AT&T the ability to seek reimbursement for its attorney's fees

Finally, if the AT&T customer received an arbitration award greater than AT&T's last written settlement offer, it required AT&T to pay a $7,500 minimum recovery and twice the amount of the customer's attorney's fees. *Id*.

Under the Federal Arbitration Act (the "FAA"), arbitration provisions are "valid, irrevocable, and

enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Courts throughout the country have relied on this language to invalidate consumer contracts containing arbitration/class action waiver clauses, finding that such provisions are unconscionable (unfair and unreasonable) as a matter law. In fact, unconscionability has served as the primary reason that courts have refused to enforce arbitration/class action waiver clauses.

The Concepcions purchased their AT&T phones and service plans in California. In *Discover Bank v. Superior Court*, the California Supreme Court held that consumer contracts containing arbitration/class action waiver clauses were unfair and unreasonable if a plaintiff alleged that a company had carried out a scheme to deliberately cheat a large number of consumers out of small sums of money. Based on *Discover Bank*, the Concepcions argued successfully at both the trial court and before the U.S. Court of Appeals that AT&T's agreement was unfair and unreasonable because it prohibited an AT&T customer from participating in a class action arising from AT&T's alleged misconduct.

The Supreme Court disagreed with the trial court and the U.S. Court of Appeals, holding that the California rule that prevented enforcing this provision of the agreement was preempted by the FAA. The Supreme Court stated that the principal purpose of the FAA is to "ensure that private arbitration agreements are enforced according to their terms." The Court held that the *Discover Bank* Rule interfered with arbitration by allowing a party to a consumer contract to *demand* classwide arbitration*after* entering into the agreement.

Based on the Supreme Court's ruling in *Concepcion*, courts should enforce arbitration agreements containing a class action waiver. Consequently, financial institutions should consider including arbitration provisions in their customer agreements that require customers to bring any disputes in their individual capacity, rather than as a plaintiff or class member in a class or representative proceeding. Such a provision will allow financial institutions to avoid the financial risks and costs associated with defending class actions.

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