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 FOR RESPONDENTS

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QUESTION PRESENTED

Class-action bans are provisions in standard form contracts that purport to bar consumers or employees from pursuing classwide proceedings in any forum. In circumstances where they would function as exculpatory clauses, class-action bans have been held unenforceable under the generally applicable contract law of twenty States—without regard to whether they are found in arbitration agreements.

The Federal Arbitration Act (FAA) provides that arbitration agreements are enforceable, "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The question presented is:

> When a class-action ban that is otherwise unenforceable under generally applicable contract law is embedded in an arbitration agreement, is the contract law preempted by the FAA?

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INTRODUCTION

Claiming that its arbitration agreement is more "consumer friendly" than others despite its class-action ban, AT&T seeks to transform a factbound state-law question of unconscionability into a question of federal preemption. But the question whether a contractual provision offends generally applicable state law is a matter that the Federal Arbitration Act (FAA) leaves to the States, so long as state law does not discriminate against arbitration. The FAA makes arbitration agreements enforceable "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Under that savings clause, "States may regulate contracts, including arbitration clauses, under general contract law principles." *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 281 (1995). The California courts, like many others, have applied general contract law to hold that class-action bans in adhesion contracts that effectively exculpate defendants from liability are unenforceable, without regard to whether the bans are part of arbitration agreements. Because the applicable state law does not treat arbitration agreements "in a manner different from that in which it otherwise construes nonarbitration agreements," *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987), the FAA does not preempt it.

From reading AT&T's brief, one might think California had struck out on its own in its approach to the enforceability of class-action bans. In fact, courts applying the general contract law of at least twenty States have held that provisions purporting to bar consumers or employees from pursuing classwide relief in any forum may be unenforceable. If California's highest court has distorted its own common law, as AT&T contends, then so have the highest courts of Alabama, Illinois, Massachu-

setts, Missouri, New Jersey, New Mexico, North Carolina, South Carolina, West Virginia, and Washington. So too have courts applying the law of Arizona, Delaware, Florida, Georgia, Michigan, Ohio, Oregon, Pennsylvania, and Wisconsin. Even if the fidelity of these courts to state common-law principles were relevant to the issue of FAA preemption, it would be an unprecedented incursion on State sovereignty for this Court to conclude that so many States have been untrue to their own law.

One might also think, from reading AT&T's brief, that the enforceability of class-action bans is a question arising only in the context of arbitration, or that state contract law treats class-action bans in arbitration agreements differently from class-action bans in other agreements. To the contrary, courts have found class-action bans unenforceable in cases having nothing to do with arbitration agreements. The first California appellate decision on point was such a case. Thus, the States have been true to their word: They have found class-action bans unenforceable under general principles of contract law, without regard to whether they are embedded in arbitration agreements. Such decisions are not merely facially nondiscriminatory, but nondiscriminatory in purpose and effect.

"To immunize an arbitration agreement from judicial challenge," despite its unlawfully exculpatory effect, "would be to elevate it over other forms of contract—a situation inconsistent with the 'saving clause.'" *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404, n.12 (1967). Requiring the enforcement of exculpatory clauses *only* when they are embedded in arbitration agreements would not "make arbitration agreements as enforceable as other contracts," but "more so." *Id.*

STATEMENT

1. AT&T's wireless service agreement purports to bar its customers from seeking classwide relief in any forum:

> **YOU AND AT&T AGREE THAT EACH MAY BRING CLAIMS AGAINST THE OTHER ONLY IN YOUR OR ITS INDIVIDUAL CAPACITY, AND NOT AS A PLAINTIFF OR CLASS MEMBER IN ANY PURPORTED CLASS OR REPRESENTATIVE PROCEEDING.**

Pet. App. 61a (emphasis in original). The agreement also forecloses injunctive relief that extends beyond a customer's "individual claim" to halt systemic fraud or deceptive practices. *Id.* Both the class-action ban and the injunctive-relief limitation are embedded within an arbitration provision. The agreement also allows either party to bring an action in small claims court, subject to the class-action ban. *Id.* at 58a.

Under the agreement's "blowup clause," if the class-action ban is "found to be unenforceable, then the entirety of this arbitration provision shall be null and void," and any class action must be litigated in court. *Id.* at 61a.

Despite the class-action ban, AT&T describes its agreement as "consumer friendly" because AT&T promises to pay "premiums" if an arbitrators' award exceeds a settlement offer. As the court of appeals explained, however, the agreement permits AT&T to buy off small claimants for the face amount of their claim, ensuring that the "premiums" it purports to offer will never actually be paid. Pet. App. 10a. Thus, "the maximum gain to a

consumer for the hassle of arbitrating a $30.22 dispute is still just $30.22." *Id.* [1]

The agreement thus allows AT&T to negate the incentives that consumers who suspect systemic fraud or deceptive practices might have to investigate, determine whether they have a legal claim, and prosecute that claim. It also effectively eliminates any incentive a lawyer might have to represent such consumers. In the district court, other than routine billing disputes, AT&T could not identify "any claims … for deceptive advertising" or "other alleged wrongdoing" that had ever been resolved under its "consumer-friendly" agreement. Pet. App. 44a.

AT&T's account of "the allegedly unique and 'pro-consumer' nature of the agreements," is belied by the numbers. *Coneff v. AT&T Corp.*, 620 F. Supp. 2d 1248, 1257 (D. Wash. 2009). As one court found, "the actual percentage of customers utilizing [the] allegedly 'pro-consumer' provisions represents an infinitesimal amount." *Id.* at 1258. The court reported that AT&T was involved in fewer than 200 consumer arbitrations—representing, at that time, roughly 0.0029 percent of AT&T's customers—over a five-year period from 2003 to 2007. *Id.* And according to the American Arbitration Association, AT&T was involved in only about 100 consumer arbitrations of any kind between 2005 and 2010.[2]

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[1] The first page of AT&T's brief cites a case describing its agreement as "consumer friendly," but does not disclose that the plaintiff there—a non-English-speaker with no lawyer—was not seeking to bring a class action. The two-page minute order did not discuss the class-action ban; it merely parroted AT&T's description of its own agreement.

[2] American Arbitration Association, http://www.adr.org/si.asp?id=4702 (accessed Sept. 14, 2010).

Compared to the universe of claims that would be asserted through class actions, the numbers starkly demonstrate the claim-suppressing effect of the ban.

2. These numbers must be evaluated not only against AT&T's customer base of 90 million subscribers (Pet. Br. 4), but also in light of published data about consumer complaints and dissatisfaction with AT&T's business practices.

A recent government study identified "billing, terms of the service contract, carriers' explanation of their service at the point of sale, call quality, and customer service as key aspects of wireless phone service with which consumers have experienced problems in recent years," and estimated that 34 percent of wireless customers received "unexpected charges" and 42 percent wanted to switch carriers but did not because of anticompetitive early-termination fees.[3] According to a Federal Communications Commission (FCC) study released this May, at least "17 percent of Americans—30 million people—have experienced" "bill shock" due to large undisclosed increases in their wireless bills.[4] The FCC receives "tens of thousands of wireless consumer complaints each year," but these complaints only scratch the surface, because "most wireless consumers with problems would not com-

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[3]GAO, *FCC Needs to Improve Oversight of Wireless Phone Service*, GAO-10-34 (Nov. 2009), *available at* http://www.gao.gov/new.items/d1034.pdf (hereinafter "*Wireless Phone Service*").

[4]*FCC Survey Confirms Consumers Experience Mobile Bill Shock and Confusion About Early Termination Fees*, http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC298415A1.pdf; FCC, *Americans' perspectives on early termination fees and bill shock*, http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC298414A1.pdf.

plain to the FCC and many do not know where they could complain."[5]

According to the Better Business Bureau, the wireless industry generates more consumer complaints than any other industry.[6] And by several leading measures, AT&T has the worst customer-satisfaction rating in the industry.[7]

Public enforcement is minimal. "According to the FCC, the agency does not regulate issues such as carriers' contract terms or call quality."[8] It "has few rules that specifically address services consumers receive from wireless phone carriers," conducts little monitoring of consumer complaints, and does not enforce its billing rules for wireless carriers.[9] Meanwhile, States' ability to regulate wireless service has been hampered by lack of clarity about the scope of federal preemption.[10]

3. Vincent and Liza Concepcion brought this lawsuit in 2006, alleging that AT&T had violated state consumer-

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[5] GAO, *Wireless Phone Service*, at 15 (reporting a total of 127,072 consumer complaints between 2004 and 2008).

[6] Mary Pilon, *Cellphone Industry Sparks the Most Complaints*, Wall Street Journal, March 8, 2010, *available at* http://blogs.wsj.com/digits/2010/03/08/cellphone-industry-sparks-the-most-complaints/

[7] *See* American Customer Satisfaction Index, 2010 http://www.theacsi.org/ (AT&T Mobility ranked worst of all six major wireless providers) (last visited Sept. 20, 2010); Consumers Union, *Cell-Phone service ratings*, Consumer Reports (Jan. 2010) (AT&T Mobility ranked last in wireless customer satisfaction in nationwide consumer survey).

[8] GAO, *Wireless Phone Service*, at 22

[9] *Id.* at 15-25.

[10] *Id.* at 33-36.

protection laws by advertising wireless phones as "free" without disclosing a $30.22 fee that appeared on their bill. Pet. App. 19a.[11] The Concepcions first purchased their phone service from AT&T in 2002. When they filed suit, their service agreement included AT&T's then-standard arbitration clause, including the class-action ban. *Id.* 19a-20a. Invoking a "change-in-terms" clause, AT&T has repeatedly modified the agreement, but the class-action ban has remained in place each time.[12]

Nine months after the Concepcions filed suit, AT&T again unilaterally modified the agreement through a notice accompanying their monthly bill. *Id.* 20a. The notice included the supposedly "consumer-friendly" provisions under which AT&T would pay attorneys' fees plus a "premium" (the maximum claim that could be brought in small claims court) if an arbitrator issued an award to a consumer exceeding AT&T's last written settlement offer before selection of the arbitrator. *Id.* 21-22a. The record does not show whether the Concepcions actually received that notice. In March 2008, AT&T moved to compel arbitration, and the Concepcions opposed.

The district court followed the California Supreme Court's decision in *Discover Bank v. Superior Court of Los Angeles*, 113 P.3d 1100 (Cal. 2005), which concluded that some class-action bans are unconscionable under

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[11] AT&T attributes the charge to sales tax, but California law allows merchants to pass the cost of sales tax onto consumers only with their consent, *Livingston Rock & Gravel Co., Inc. v. DeSalvo*, 136 Cal. App. 2d 156, 160-61 (Cal. Ct. App. 1955), and AT&T's advertising did not disclose that consumers would have to pay sales tax on the "free" phones.

[12] *See* David Horton, *The Shadow Terms: Contract Procedure and Unilateral Amendments*, 57 UCLA L. Rev. 605, 654-56, 659-60 (2010) (describing history of AT&T's strategic revisions).

California law. The court adhered to an earlier order in which it had found class-action bans unconscionable in a similar case against other wireless carriers with which the Concepcions' suit was consolidated. *Laster v. T-Mobile USA, Inc.*, 407 F. Supp. 2d 1181, 1192 (S.D. Cal. 2005), *aff'd*, 252 Fed. Appx. 777 (9th Cir. 2007), *cert. denied*, 128 S. Ct. 2500 (2008).

Under California law, courts evaluate contracts for both "procedural" and "substantive" unconscionability. Procedural unconscionability "generally takes the form of a contract of adhesion, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it." *Discover Bank*, 113 P.3d at 1108. Substantively unconscionable agreements "may take various forms, but may generally be described as unfairly one-sided," including those that "operate effectively as exculpatory clauses." *Id.*

The district court found AT&T's class-action ban both procedurally and substantively unconscionable. The court agreed with the plaintiffs that the ban would exculpate AT&T from alleged wrongful conduct because, "especially as to deceptive practices, many plaintiffs may not know their rights are being violated." Pet. App. 43a (alterations and emphasis omitted). Absent a class action and procedures "for notifying potential class members," many consumers would be left with "no recovery." *Id.* The court observed that AT&T "did not respond to this argument," was unable to explain how the class-action ban would not function as an exculpatory clause with respect to "thousands" of parties to the agreement "who have no knowledge of the alleged wrongdoing," and could not point to any deceptive-advertising or similar claims brought under its dispute-resolution process. Pet.

App. 44-45a. The court concluded that AT&T had "essentially granted itself a license to push the boundaries of good business practices to their furthest limits," *id.* at 46a (quoting *Discover Bank*, 113 P.3d at 1108), a concern "not sufficiently addressed" by AT&T's revised agreement. *Id.*

4. The court of appeals affirmed, concluding that "AT&T's class action waiver is in effect an exculpatory clause." Pet. App. 11a. The court also concluded that the premium-payment and fees clauses in AT&T's revised agreement would not change the outcome under *Discover Bank*. That analysis, the court explained, "focuses on whether damages are predictably small and, in the end, the premium payment provision does not transform a $30.22 case into a predictable $7,500 case." *Id.* 9a-10a. The court held that the FAA "does not expressly or impliedly preempt California law governing the unconscionability of class action waivers in consumer contracts of adhesion," *id.* 12a, because *Discover Bank* is "simply a refinement of the unconscionability analysis applicable to contracts generally in California." *Id.* 12a-13a (quoting *Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 987 (9th Cir. 2007)).

SUMMARY OF ARGUMENT

I. The FAA makes arbitration agreements enforceable, "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. When the question is whether the FAA preempts state-law contract principles, "the text of § 2 provides the touchstone." *Perry*, 482 U.S. at 492 n.9.

A. By mandating enforcement of arbitration agreements, subject to state-law grounds that apply to "any contract," Section 2 establishes a rule of nondiscrimi-

nation toward arbitration. That rule "places arbitration agreements on an equal footing with other contracts." *Rent-A-Center West, Inc. v. Jackson*, 130 S. Ct. 2772 (2010). So long as a State's contract law does not treat an arbitration agreement "in a manner different from that in which it otherwise construes nonarbitration agreements," *Perry*, 482 U.S. at 492 n.9, the FAA's nondiscrimination standard is satisfied.

B. State-law rulings finding class-action bans unenforceable satisfy that standard because "the principle that class action waivers are, under certain circumstances, unconscionable as unlawfully exculpatory … does not specifically apply to arbitration agreements, but to contracts generally." *Discover Bank*, 113 P.3d at 1112. That courts find class-action bans unenforceable under the same circumstances in both arbitration and nonarbitration agreements alike demonstrates that the state-law principles applied are concerned with aggregation, not arbitration.

C. Although the state law at issue does not discriminate against arbitration, AT&T characterizes the decision below as applying a "rule" that applies "only to dispute-resolution agreements" (Pet. Br. 29) and therefore does not govern "any contract" within the meaning of Section 2. This argument has multiple flaws.

First, AT&T's logic has no sensible limiting principle because any application of general contract law requires application to specific circumstances. *Second*, AT&T's argument has nothing to do with discrimination against arbitration. The best reading of "any contract" is that it encompasses contract principles that apply regardless of whether the contract contains an arbitration clause. *Third*, AT&T's argument is inconsistent with this Court's cases, which treat arbitration agreements as a

species of forum-selection clause, subject to the same contract defenses. *Fourth*, AT&T's approach would preclude courts from policing the worst abuses and thereby lead to the destruction of public confidence in arbitration as a legitimate and fair means of dispute resolution.

Even AT&T shrinks from the implications of its argument, which would prevent application of state unconscionability doctrine to unfairly one-sided provisions within arbitration agreements that AT&T concedes should be unenforceable. AT&T's unwillingness to embrace the consequences of its own theories underscores why the Court should adhere to its longstanding view that so long as the State's law does not discriminate against arbitration, it is not preempted.

D. Although AT&T invokes the FAA's nondiscrimination principle, it simultaneously seeks to undermine that principle by positing a slippery slope under which rogue States could devise seemingly nondiscriminatory laws, such as a law mandating jury trials in arbitration—despite the parties' clear consent to informal procedures. Such rules would be preempted because the statute cannot be read to destroy itself by allowing States to require procedures that are fundamentally incompatible with arbitration. But AT&T's hypotheticals are a far cry from this case, and AT&T itself does not suggest that decisions finding class-action bans unconscionable under the law of twenty States fall into this hypothetical category.

II. *Discover Bank* is an eminently reasonable application of longstanding state contract-law principles to which this Court should defer. AT&T claims that the California Supreme Court "distorted" and "gerrymandered" its own law. But AT&T does not explain how its criticisms of the application of state law are relevant to the federal question before the Court, which is whether

the law *discriminates* against arbitration. Similarly, the theme that its class-action ban is "consumer friendly" runs throughout AT&T's brief, but the question whether the agreement is unconscionable on the facts is purely a question of state law. This Court should decline AT&T's invitation to federalize this "question of state law, which this Court does not sit to review." *Volt Info. Sci., Inc. v. Bd. of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 474 (1989). In any event, the *Discover Bank* ruling is well grounded in established principles of California law.

III. Finally, AT&T, invoking the FAA's purposes of allowing parties to agree upon procedures and removing impediments to arbitration, contends that the state law at issue stands as an obstacle to the accomplishment of the purposes and objectives of Congress. But Congress does not pursue its purposes at all costs, and application of unconscionability principles to class-action bans in adhesion contracts *furthers*, not undermines, two key FAA policies identified by this Court: first, that arbitration is a matter of consent, the content and limits of which is determined by ordinary contract law, and second, that it does not operate to limit available remedies for wrongdoing. The FAA favors arbitration, not exculpation.

ARGUMENT

I. Because It Does Not Discriminate Against Arbitration, the State Contract Law Applied Below Is Not Preempted by the FAA.

The question before the Court is whether an application of state contract law falls within the FAA's savings clause, which provides that arbitration agreements are enforceable "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. "In instances such as these, the text of § 2 provides the

touchstone" for determining whether state law conflicts with the FAA. *Perry*, 482 U.S. at 492 n.9. The FAA preempts state law only "to the extent that it actually conflicts with federal law." *Volt*, 489 U.S. at 477. "The FAA contains no express pre-emptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration." *Id.* Preemption thus "turn[s] on whether state law conflicts with the text" of Section 2 or, put another way, "whether the ordinary meanings of state and federal law conflict." *Wyeth v. Levine*, 129 S. Ct. 1187, 1207 (2009) (Thomas, J., concurring in the judgment).

The savings clause expressly preserves state-law contract principles that do not discriminate against arbitration. The principles applied below do not discriminate against arbitration. As the California Supreme Court has explained, "the principle that class action waivers are, under certain circumstances, unconscionable as unlawfully exculpatory is a principle of California law that does not specifically apply to arbitration agreements, but to contracts generally." *Discover Bank*, 113 P.3d at 1112. Under the law of at least twenty states, courts have reached similar conclusions with respect to class-action bans that function as exculpatory clauses—in both arbitration and nonarbitration agreements alike. *See* Appendix (listing cases). Because there is no "actual conflict" here, core principles of federalism and statutory interpretation require that the State's law prevail.

Enforcing an exculpatory clause because it is part of an arbitration agreement would not make arbitration agreements "as enforceable as other contracts," but "more so." *Prima Paint*, 388 U.S. at 404 n.12. And concluding that applications of general contract principles are preempted if they can be characterized as "applicable only to dispute resolution agreements," as AT&T

contends (at 29), would make unlawful terms enforceable whenever they are laundered through an arbitration agreement. That approach would encourage the very worst abuses and thereby undermine the viability of, and public confidence in, arbitration as a legitimate method of dispute resolution.

A. The FAA's Text Preserves an Essential Role For State Contract Law That Does Not Discriminate Against Arbitration.

1. Section 2, the FAA's "centerpiece provision," *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985), makes written agreements to arbitrate "valid, irrevocable, and enforceable," subject to the savings clause. 9 U.S.C. § 2. By making arbitration agreements "valid, irrevocable, and enforceable," Section 2 overturns the hostility to arbitration enshrined in the ancient "ouster" doctrine, under which "courts traditionally viewed arbitration clauses as unworthy attempts to 'oust' them of jurisdiction" and "refused to order specific enforcement of agreements to arbitrate." *Vaden v. Discover Bank*, 129 S. Ct. 1262, 1274 (2009).

The first clause, in isolation, might require the enforcement of *all* arbitration agreements—no matter how unfair or exculpatory the terms, and even absent bargained-for exchange or true assent. Although AT&T suggests precisely such a policy (at 23-26, 48-57), a statute like that would quickly bring arbitration into disrepute, transforming it from a method of alternative dispute resolution into a tool for stronger parties to exempt themselves entirely from the law.

To avoid that consequence, Section 2's savings clause conditions the enforceability of arbitration agreements on "grounds" available "at law or in equity" for challeng-

ing "any contract." The clause preserves an essential role for state common law, making arbitration agreements subject to contract-law defenses otherwise available at law or in equity.

Taken together, the two clauses of Section 2 establish an "enforceability mandate," under which "State law is … applicable to determine which contracts are binding under Section 2." *Arthur Andersen LLP v. Carlisle*, 129 S. Ct. 1896, 1902 (2009). The FAA's provisions do not "purport to alter background principles of state contract law" and "[i]ndeed § 2 explicitly retains an external body of law governing revocation (such grounds 'as exist at law or in equity')." *Id.* State-law contract defenses that would be available absent the FAA's enactment remain available, so long as they do not run afoul of the Act's text or structure.

Under Section 2, "States may regulate contracts, including arbitration clauses, under general contract law principles." *Allied-Bruce*, 513 U.S. at 281. "Like other contracts," arbitration agreements "may be invalidated by 'generally applicable contract defenses, such as fraud, duress, or unconscionability.'" *Rent-A-Center,* 130 S. Ct. at 2776 (quoting *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996)). Because "§ 2 gives States a method of protecting consumers" against unwanted or unfair terms, *Allied-Bruce*, 513 U.S. at 281, state law is integral to upholding two foundational principles under the FAA—that arbitration is a matter of consent, not coercion, and that it represents an alternative forum, but does not exempt the drafter from the law.

2. Just as integral to the FAA is its nondiscrimination principle. Section 2 "places arbitration agreements on an equal footing with other contracts." *Rent-A-Center*, 130 S. Ct. at 2776. By preserving only defenses that apply to

"any contract," "Congress precluded States from singling out arbitration provisions for suspect status." *Casarotto*, 517 U.S. at 687. In this way, the text of Section 2 establishes a core antidiscrimination principle, ensuring that arbitration agreements are not deemed unenforceable *because* they are arbitration agreements.

Applying that antidiscrimination principle, this Court has held that the FAA preempts state statutes that "mak[e] written, predispute arbitration agreements invalid" *Allied-Bruce*, 513 U.S. at 269, provide that a "contract may not be subject to arbitration" absent conspicuous notice of the arbitration clause on the first page, *Casarotto*, 517 U.S. at 681, and exempt wage-and-hour claims from "any private agreement to arbitrate," *Perry*, 482 U.S. at 484. Those statutes unquestionably discriminated against arbitration. The Court has held that the FAA preempts statutes requiring that disputes parties have agreed to arbitrate nevertheless be referred to a judicial or administrative forum, *Southland v. Keating*, 465 U.S. 1, 5 (1984); *Preston v. Ferrer*, 552 U.S. 346, 358 (2008), because such statutes likewise conflict with Section 2's enforceability mandate.

In a much-quoted footnote in *Perry*, the Court distilled the relevant antidiscrimination framework:

> [S]tate law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. A state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2. A court may not, then, in assessing the rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in

> which it otherwise construes nonarbitration agreements under state law. Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what we hold today the state legislature cannot.

482 U.S. at 492 n.9 (emphasis in original).

The preemption inquiry, then, turns on whether the state law in question *discriminates* against arbitration. So long as a State does not "singl[e] out arbitration provisions for suspect status," *Casarotto*, 517 U.S. at 687, treat an arbitration agreement "in a manner different from that in which it otherwise construes nonarbitration agreements," or "rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding," *Perry*, 482 U.S. at 492 n.9, the FAA's nondiscrimination standard is satisfied.

B. The States That Have Found Class-Action Bans Unenforceable Have Not Discriminated Against Arbitration.

AT&T acknowledges that the preemption question in this case must be answered by the FAA's "fundamental antidiscrimination principle." Br. 28. But although AT&T's brief repeatedly describes California's approach to class-action bans as only "nominally" or "ostensibly" nondiscriminatory (suggesting that the reality is otherwise), it never explains how the State's law has *actually* discriminated against arbitration. Br. 17, 28, 30.[13]

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[13] Although employing the rhetoric of discrimination, AT&T appears to advocate a shift from the FAA's *disparate treatment* regime (which turns on whether the State treats arbitration "in a

(*Footnote continued*)

Although class-action bans have been held unenforceable under the common law of twenty States, not a single state or federal appellate court has concluded that the FAA preempts such determinations. That is because these determinations, including the California Supreme Court's *Discover Bank* decision, easily satisfy the nondiscrimination test: The state does not treat arbitration agreements "in a manner different from that in which it otherwise construes nonarbitration agreements." *Perry*, 482 U.S. at 492 n.9.

1. In California, and under the common law generally, "unconscionability is a doctrine fundamental to the operation of contract law, irrespective of the particular application." *A&M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114, 123 n.12 (Cal. Ct. App. 1982). Indeed, California law "codifies the unconscionability doctrine in Civil Code section 1670.5, *applicable to all types of contracts*, rather than as part of the Commercial Code." *Id.* (emphasis added); *see Graham v. Scissor-Tail, Inc.*, 623 P.2d 165, 175 (Cal. 1981) (describing unconscionability as a "principle of equity applicable to all contracts generally"). Section 1670.5 (which mirrors U.C.C. § 2-302) authorizes courts to "refuse to enforce" any contract found "to have been unconscionable at the time it was made" or sever or "limit the application of any unconscionable

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manner different from that in which it otherwise construes nonarbitration agreements," *Perry*, 482 U.S. at 492 n.9), to a *disparate impact* regime: "[E]ven if nominally neutral," AT&T argues, *Discover Bank* "predictably and inevitably will have a far greater *impact* on arbitration agreements" than on nonarbitration agreements. Pet. Br. 30 (emphasis added). But none of this Court's decisions suggests that neutral state laws are preempted simply because potential defendants often choose to combine otherwise unenforceable provisions with arbitration agreements.

clause so as to avoid any unconscionable result." Cal. Code. Civ. § 1670.5.

California's unconscionability doctrine incorporates the venerable prohibition on exculpatory clauses, which was recognized in "the common law of England and America before the declaration of independence." *Liverpool & G.W. Steam Co. v. Phenix Ins. Co.*, 129 U.S. 397, 412 (1889); *see Restatement (Second) of Contracts* § 195 ("[A] party's attempt to exempt himself from liability for negligent conduct may fail as unconscionable."). That rule, applicable to "all contracts" and codified in California's law since 1872, renders unenforceable "[a]ll contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud." Cal. Civ. Code § 1668.

Considering the enforceability of a class-action ban in a standard credit-card agreement, *Discover Bank* applied California's generally applicable contract law to conclude that "at least some class action waivers in consumer contracts are unconscionable under California law." 113 P.3d at 1108. The court found "an element of procedural unconscionability" because the credit-card agreement was a contract of adhesion that had been sent to the consumer as a "bill stuffer." *Id.* Turning to substantive unconscionability, the court found that class-action bans "may operate effectively as exculpatory contract clauses" because, when many consumers are exposed to the same fraudulent practice by the same seller, "the class action is often the only effective way to halt and redress such exploitation." *Id.* at 1108-09. Even for consumers who are aware of the fraud, "small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights." *Id.* at 1105 (quoting *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591,

617 (1997)). Class actions are thus "inextricably linked to the vindication of substantive rights," and class-action bans, "at least to the extent they operate to insulate a party from liability that would be imposed under California law, are generally unconscionable." *Id.* at 1109.

Discover Bank did "not hold that all class action waivers are necessarily unconscionable." *Id.* at 1110. "But when the waiver is found in a consumer contract of adhesion in a setting in which the disputes between the contracting parties predictably involve small amounts of damages," and it is alleged "that the party with superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money," the waiver is effectively an "exemption of the party 'from responsibility for its own fraud, or willful injury to the person or property of another,'" *id.* (quoting Cal. Civ. Code § 1668), and "unconscionable under California law." *Id.*

Thus, contrary to AT&T's suggestion, *Discover Bank* did not erect a per se rule; rather, state law calls for a fact-specific inquiry into any contract term that would potentially exculpate one party. Under *Discover Bank*, California courts assess enforceability case by case and decline to enforce a class-action ban only where it would lead to an "unconscionable result." Cal. Code. Civ. § 1670.5. Several recent decisions applying California law have *rejected* unconscionability challenges to class-action bans in circumstances where they would not be exculpatory.[14] Other states follow the same even-handed ap-

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[14] *See, e.g., Arguelles-Romero v. Superior Court (Americredit Fin. Servs., Inc.)*, 109 Cal. Rptr. 3d 289, 305-07 (Cal. Ct. App. 2010); *Gold v. Melt*, 2010 WL 1509795, at *7-78 (Cal. Ct. App. 2010); *Walnut Producers of Calif. v. Diamond Foods, Inc.*, 114 Cal. Rptr. 3d

(*Footnote continued*)

proach. For example, the New Jersey Supreme Court issued two decisions the same day—one enforcing a class-action ban in a case where the plaintiff sought over $100,000 in damages, *Delta Funding Corp. v. Harris*, 912 A.2d 104 (N.J. 2006), and one invalidating a class-action ban where each consumer's maximum recovery was $600, *Muhammad v. County Bank of Rehoboth Beach*, 912 A.2d 88, 99 (N.J. 2006).

2. Class-action bans are not limited to arbitration agreements. The approach courts have taken to class-action bans in nonarbitration agreements, both before and after *Discover Bank*, demonstrates that the California Supreme Court and other courts that have reached the same conclusion are concerned with aggregation, not arbitration. That is, they are concerned with the enforceability of contracts that purport to cut off the right to bring classwide proceedings *without regard to forum*. Although the contract in *Discover Bank* included an arbitration clause, the starting point for the court's unconscionability analysis was a California appellate case decided four years earlier, concerning "the validity of a contractual class action waiver *outside the arbitration context*." *Discover Bank*, 113 P.3d at 158 (emphasis added) (citing *America Online, Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699 (Cal Ct. App. 2001) ("*AOL*").

In *AOL*, former subscribers brought a class action alleging that the online service violated state law by debit-

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449, 460-62 (Cal. Ct. App. 2010); *Citibank (South Dakota), N.A. v. Walker*, 2008 WL 4175125, at *4 (Cal. Ct. App. 2008); *Smith v. Americredit Fin. Servs., Inc.*, 2009 WL 4895280, at *6-*8 (S.D. Cal. 2009); *Dalie v. Pulte Home Corp.*, 636 F. Supp. 2d 1025, 1027 (E.D. Cal. 2009); *McCabe v. Dell, Inc.*, 2007 WL 1434972, at *3–*4 (C.D. Cal. 2007); *Torres v. Chrysler Fin. Co.*, 2007 WL 3165665, at *2-*3 (N.D. Cal. 2007).

ing their credit cards for small monthly fees even after their subscriptions were canceled. The company invoked Virginia forum-selection and choice-of-law clauses in its subscription agreement. Because Virginia does not permit consumer class actions, the court concluded, the provisions were the "functional equivalent of a contractual waiver" of the right to bring a class action. *Id.* at 699. The court held that, as applied to the small claims before it, the denial of classwide remedies would "substantially diminish the rights of California residents." *Id.* at 708. *AOL* emphasized several practical justifications for aggregated proceedings, including the "protection of unwary consumers from being duped by unscrupulous sellers" and the impracticability of individual actions where "the amount of individual recovery would be insufficient to justify bringing a separate action," allowing an "unscrupulous seller [to] retain[] the benefits of its wrongful conduct." *Id.* at 712. The court stressed the "salutary" effects of class actions that would be lost if the bans were permitted in such a case, including deterrence and "curtailing illegitimate competition." *Id.*[15]

AOL is not an isolated decision. The Washington Supreme Court held the same forum-selection clause unenforceable in a nonarbitration agreement because it effectively barred class actions, *Dix v. ICT Group, Inc.*, 161 P.3d 1016 (Wash. 2007), on the same day that it issued a

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[15] *AOL* relied in part on an antiwaiver provision in the Consumer Legal Remedies Act, Cal. Civ. Code § 1751, but independently rested on a broader analysis of the effect on consumers' substantive rights. *AOL*, 108 Cal. Rptr. 2d at 711-14 ("The unavailability of class action relief in this context is sufficient in and by itself to preclude enforcement."). *Discover Bank* expressly disclaimed reliance on the statutory antiwaiver portion of *AOL*'s analysis. *See Discover Bank*, 113 P.3d at 1108.

decision striking down a class-action ban in an arbitration clause, *Scott v. Cingular Wireless*, 161 P.3d 1000 (Wash. 2007). In cases having nothing to do with arbitration, courts in Florida and Massachusetts have also held that same provision unenforceable to the extent that it functions as an exculpatory class-action ban.[16]

Courts in California have likewise applied both *Discover Bank* and Section 1668 (the prohibition on exculpatory clauses) in cases involving express class-action bans in *nonarbitration* agreements. *See*, *e.g.*, *In re Yahoo! Litig.*, 251 F.R.D. 459 (C.D. Cal. 2008); *Elhilu v. Quiznos Franchise Co., LLC*, No. 06-CV-07855, Doc. 69 at 8 (C.D. Cal. April 3, 2008). The language of such express class-action bans is no different from class-action bans found in arbitration agreements. *See In re Yahoo!*, 251 F.R.D. at 463 ("Any claim against Overture arising from this Agreement shall be adjudicated on an individual basis, and shall not be consolidated in any proceeding with any claim or controversy of any other party."); *Martrano v. The Quizno's Franchise Co., LLC,* 2009 WL 1704469 (W.D. Pa. 2009) ("The parties agree that any proceeding will be conducted on an individual, not a class-wide, basis, and that any proceeding … may not be consolidated.").

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[16] *America Online, Inc. v. Pasieka*, 870 So.2d 170, 171-72 (Fla. Ct. App. 2004) (agreement unenforceable because consumer law "does not exist solely for the benefit of the individual parties, and is instead designed to afford a broader protection to the citizens of Florida"); *Williams v. America Online*, 2001 WL 135825, at *3 (Mass. Super. Ct. 2001) (holding clause unenforceable where "plaintiffs seek to represent a class of Massachusetts residents, … Massachusetts consumers who individually have damages of only a few hundred dollars"); *see also Doe 1 v. AOL LLC*, 552 F.3d 1077 (9th Cir. 2009) (following *AOL v. Superior Court*).

The approach taken by California and other states is thus both facially nondiscriminatory toward arbitration and nondiscriminatory in purpose and effect. As the Washington Supreme Court put it, "[t]he arbitration clause is irrelevant to the unconscionability." *Scott*, 161 P.3d at 1008. Exculpatory clauses "do not change their character merely because they are found within a clause labeled 'Arbitration.'" *Id.*

C. AT&T's Construction of the Phrase "Any Contract" Is Incoherent and Would Threaten the Viability of, and Public Confidence In, Arbitration As a Legitimate Means of Dispute Resolution.

Although California unconscionability law does not treat arbitration agreements differently from nonarbitration agreements, AT&T characterizes the decision below as applying a rule "applicable only to dispute-resolution agreements." Pet. Br. 29. Based on that characterization, AT&T argues that this "rule" does not govern "contracts generally" and therefore does not fall within Section 2's savings clause. This kind of logic has no sensible limiting principle. Because any application of general contract law to a particular contract or type of contract could be so characterized, the argument is both incoherent and unworkable.

1. AT&T effectively asserts that general principles of contract law, such as unconscionability, are no longer general principles when applied to an arbitration agreement. Instead, they are transformed into rules specific to "dispute resolution agreements." But the same could be said of any application of unconscionability (or any other contract-law defense) to specific facts or circumstances. AT&T's logic would render the FAA's savings clause a nullity. The argument misconceives the nature of com-

mon-law doctrines, which by necessity are continually applied and refined "as new circumstances and fact patterns present themselves." *Rogers v. Tennessee*, 532 U.S. 451, 461 (2001); *see Bisso v. Inland Waterways Corp.*, 349 U.S. 85, 90 (1955) ("This rule is merely a particular application to the towage business of a general rule long used by courts and legislatures to prevent enforcement of release-from-negligence contracts in many relationships."). Under AT&T's reasoning, the rule this Court applied in *Bisso* (the prohibition against exculpatory clauses) governed only "towage contracts" and was not a rule of general applicability.

Under that logic, the preemption of state law depends not on discrimination against arbitration, but on the level of generality with which one chooses to characterize the state-law "rule." AT&T's argument proves too much: On its view, the FAA would preempt the Uniform Commercial Code, including its codification of unconscionability and other general defenses, because most of its provisions govern only specific categories of contracts, such as sales-of-goods agreements or bills of lading. This would come as news to judges, lawyers, and businesses that have long relied on the U.C.C. as part of the general contract law applicable to arbitration agreements. Many general sections of the Restatement would also be preempted. *See, e.g., Restatement (Second) of Contracts* § 211(3) (concerning "standardized contracts," rather than all contracts); *id.* § 15 (contracts made by mentally disabled persons). It is not difficult to devise more absurd examples: By AT&T's reasoning, if a state supreme court applying unconscionability law were to determine that contracts providing for payment of a penalty of a pound of flesh from a debtor were unconscionable, and lower courts in that state applied the precedent to other pound-of-flesh contracts, the rule

would not be applicable to "any contract" but only to pound-of-flesh agreements, and hence would be preempted if applied to an arbitration clause containing such a penalty.

2. Even apart from its incoherence and malleability, AT&T's construction of "any contract" has nothing to do with discrimination against arbitration. The better, more natural, reading of the phrase is that it encompasses "grounds" that "exist at law or in equity for the revocation" of a contract, *regardless of whether the contract contains an arbitration clause*. That reading is consistent with the nondiscrimination or "equal footing" principle articulated in all of this Court's previous FAA preemption cases, under which arbitration agreements are to be treated like other contracts that are similarly situated but for their lack of an arbitration clause. Thus, if a provision of the U.C.C. is applicable only to contracts for sales of goods, the FAA's "equal footing" principle does not require that sales contracts be exempted from that provision because they contain an arbitration agreement. To conclude otherwise would be to make sales contracts containing arbitration agreements more enforceable than otherwise identical sales contracts.

AT&T pays lip service to the principle that arbitration agreements must be placed on an "equal footing" with other contracts. But ultimately, by seeking to exempt them from defenses applicable to other contracts, AT&T asks this Court to treat them as, in Orwell's phrase, "more equal than others." George Orwell, *Animal Farm* 123 ("All animals are equal. But some animals are more equal than others").

3. AT&T's interpretation of the phrase "any contract" also cannot be reconciled with this Court's cases. This Court has explained many times that an arbitration

clause is merely a "species" or "subset" of forum-selection clause. *See, e.g., Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 533, 534 (1995); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 519 (1974); *see also Allied-Bruce*, 513 U.S. at 289 (Thomas, J., dissenting).

Although the law generally favors enforcement of forum-selection clauses, the Court has held that such agreements "should be held unenforceable if enforcement would contravene a strong public policy of the forum in which suit is brought, whether declared by statute or by judicial decision." *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 15 (1972). And the Court has said that courts should police forum clauses in form contracts for unfairness where the parties lack equal bargaining power. *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 595 (1991) ("Forum-selection clauses contained in form passage contracts are subject to judicial scrutiny for fundamental fairness.").

Under AT&T's reasoning, these principles would fall outside Section 2's savings clause because they apply only to forum-selection agreements or "dispute resolution contracts." But in *Vimar*, this Court endorsed precisely the opposite logic: "[A]s foreign arbitration clauses are but a subset of foreign forum selection clauses in general," a rule governing forum-selection had "been extended to arbitration clauses as well." 515 U.S. at 534. The Court characterized "the logic of that extension" as "quite defensible." *Id.* More important, in *Vimar* and, ten years earlier, in *Mitsbushi*, the Court explained that if a foreign arbitration agreement "operated … as a prospective waiver of a party's right to pursue statutory remedies … we would have little hesitation in condemning the agreement as against public policy." *Vimar*, 515 U.S. at 540 (citing exculpatory-clause cases); *Mitsubishi*,

473 U.S. at 637 n.19 (citing 15 Williston, Contracts §1750A (3d ed. 1972) (section on exculpatory clauses)).

Just as in *Vimar*, that "the forum here is arbitration" does not mean ordinary contract-law principles applicable to forum-selection or other "dispute resolution" agreements are preempted. *See Vimar*, 515 U.S. at 538. Rather, the FAA requires enforcement of an arbitration clause only "where there is no independent basis in law or in equity for revocation." *Id.* at 534. The principle that "[f]orum selection clauses contained in form … contracts are subject to judicial scrutiny for fundamental fairness" and may be "condemn[ed] … as against public policy," applies equally to arbitration clauses. *Id.* at 541 (citing *Carnival Cruise Lines*, 499 U.S. at 595).

4. AT&T's theory would also insulate most or all otherwise unenforceable procedural limitations in arbitration clauses from challenge under state law, no matter how egregiously one-sided or exculpatory. Section 2's savings clause would cease to serve its function of "giv[ing] States a method of protecting consumers" against unwanted or unfair terms. *Allied-Bruce*, 513 U.S. at 281. Drafters of adhesion contracts would be free to include not only class-action bans, but also a range of other one-sided and unfair procedural limitations that would ultimately reduce public confidence in arbitration itself.

For example, courts have applied the unconscionability doctrine to invalidate:

- Procedures that allow the contract's drafter or those with close ties to the drafter to select the arbitrator.[17]
- Procedures that give the drafter sole authority to select the pool of eligible arbitrators.[18]
- One-sided limitations on discovery, such as where the defendant can engage in discovery but the plaintiff cannot.[19]
- Unfair terms relating to the allocation of costs of arbitration.[20]
- Limits on the type or amount of relief the arbitrator may award, such as bans on punitive damages or injunctions.[21]
- Provisions requiring arbitration in an unreasonably distant forum.[22]

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[17] *E.g., State ex rel. Vincent v. Schneider*, 194 S.W.3d 853, 859 (Mo. 2006); *Ditto v. RE/MAX Preferred Props., Inc.*, 861 P.2d 1000, 1004 (Okla. Ct. App. 1993).

[18] *E.g., McMullen v. Meijer, Inc.*, 355 F.3d 485, 493-94 (6th Cir. 2004); *Murray v. United Commercial Food Workers Int'l Union*, 289 F.3d 297, 303 (4th Cir. 2002); *Hooters of Am., Inc. v. Phillips*, 173 F.3d 933, 938-39 (4th Cir. 1999); *Penn v. Ryan's Family Steakhouses, Inc.*, 95 F. Supp. 2d 940, 947-48 (N.D. Ind. 2000).

[19] *E.g.*, *Ferguson v. Countrywide Credit Indus., Inc.*, 298 F.3d 778, 786-87 (9th Cir. 2002).

[20] *E.g., McNulty v. H&R Block, Inc.*, 843 A.2d 1267, 1273–74 (Pa. Super. Ct.), *review denied*, 853 A.2d 362 (Pa. 2004).

[21] *E.g., Simpson v. MSA of Myrtle Beach, Inc.*, 644 S.E.2d 663, 670–71 (S.C. 2007); *State ex rel. Dunlap v. Berger*, 567 S.E.2d 265, 277–80 (W. Va. 2002); *see generally* David S. Schwartz, *Understanding Remedy-Stripping Arbitration Clauses: Validity, Arbitrability, and Preclusion Principles*, 38 U.S.F. L. REV. 49 (2003).

[22] *E.g., Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257, 1287–92

(*Footnote continued*)

AT&T itself has acknowledged in this Court that state-law unconscionability jurisprudence appropriately weeds out many of the worst abuses embedded in arbitration clauses—terms that "plainly favor[] the business that drafted them"—such as "a requirement that the consumer pay significant arbitration fees; preclusion of important remedies, such as punitive damages or the right to recover attorneys' fees under applicable fee-shifting statutes; a confidentiality requirement; a provision that allowed the drafter the option of bringing specified claims in court rather than only in arbitration; or a requirement that arbitration take place in an inconvenient location." Amicus Br. of AT&T Mobility in Support of Neither Party, at 4, 7, *T-Mobile v. Laster*, No. 07-976 (May 27, 2008).

Ultimately, AT&T fails to offer the Court a coherent construction of Section 2 that can save arbitration from being overwhelmed by such abuses and thereby ensure public confidence in arbitration as a means of alternative dispute resolution. Instead, AT&T takes two irreconcilable positions.

On the one hand, AT&T argues that state-law rules that can be characterized as governing only "dispute resolution contracts" (at 29-30) or "procedures" (at 49-52) are categorically preempted. Under that reasoning, each of the applications of unconscionability doctrine to abusive provisions in arbitration agreements discussed above—including those applications that AT&T has specifically endorsed—would be preempted.

(9th Cir. 2006) (en banc); *Keystone, Inc. v. Triad Sys. Corp.*, 971 P.2d 1240, 1243–46 (Mont. 1998).

On the other hand, AT&T (1) concedes that the FAA would not preempt "a general standard" requiring that the procedures imposed by an arbitration agreement "ensure that claims feasibly can be vindicated," and (2) appears to acknowledge that the FAA does not "categorically preclude[]" states from denying enforcement of class-action bans under generally applicable contract law.[23] Both of these concessions contradict AT&T's theory that rules applicable to "dispute resolution agreements" and arbitration "procedure" are categorically preempted.

We do not attempt to resolve this intramural dispute between AT&T and itself. Suffice it to say that both positions cannot be correct. In any event, the state law applied in this case *is* a "general standard" designed to ensure that claims can be vindicated. And application of that general standard is an issue of state, not federal, law. As we explain in Part III below, this Court should decline AT&T's invitation to federalize this "question of state law, which this Court does not sit to review." *Volt*, 489 U.S. at 474.

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[23] To be precise, AT&T says: "This is not to say that the FAA precludes States from imposing a general standard—such as a requirement that the parties' chosen procedures ensure that claims feasibly can be vindicated" (Pet. Br. 49 n.16), and "[i]t is *not* our position that the FAA categorically preempts state unconscionability law or categorically precludes States from refusing to enforce provisions requiring bilateral arbitration when other features of those provisions make it unrealistic to vindicate claims on an individual basis." Pet. Cert. Reply 7-8 (emphasis in original).

D. State Laws Aimed At Destroying Arbitration Are Preempted By the FAA, But No Such Rule Is At Issue Here.

While purporting to rely on the FAA's "fundamental antidiscrimination principle" (at 28), AT&T simultaneously tries to undermine it. Peppered throughout AT&T's brief is a slippery-slope argument: AT&T speculates (at 50) that rogue States, "limited only by their imagination[s]," and based on a preference for litigation over arbitration, could devise seemingly nondiscriminatory rules that would, for example, require arbitrators to permit "trials by jury" or to follow "the rules of civil procedure and evidence." Pet. Br. 41, 47, 50.

These scenarios are a far cry from this case. Rules aimed at destroying arbitration, unlike the rule at issue here, *would* be preempted by the FAA—but not for the reasons that AT&T gives. Such rules would be preempted not because they would employ principles of contract law applicable only to "dispute resolution contracts" (Pet. Br. 29), or because the FAA preempts all regulation of "procedures" (Pet. Br. 49-52), or because a State adopting such rules would "distort" its own law (Pet. Br. 32-44). Rather, rules demanding procedures incompatible with arbitration would be preempted by the FAA because they cannot sensibly be reconciled with Section 2. A federal statute's savings clause "cannot in reason be construed as [allowing] a common law right, the continued existence of which would be absolutely inconsistent with the provisions of the act. In other words, the act cannot be held to destroy itself." *Am. Tel. & Tel. Co. v. Cent. Office Tel., Inc.*, 524 U.S. 214, 227-28 (1998) (quoting *Texas & Pacific R. Co. v. Abilene Cotton Oil Co.*, 204 U.S. 426, 446 (1907)). Such state-law rules "directly conflict" with the federal statute. *Id.; see Wyeth*,

129 S.Ct. at 1209 (Thomas, J., concurring in the judgment); Nelson, *Preemption*, 86 Va. L. Rev. 225, 228-31 (2000) (outlining a "logical contradiction" test for preemption).

Accordingly, in light of the text and structure of Section 2, the "grounds" available under the savings clause should not be construed to include a State's mere preference for procedures that are incompatible with arbitration and "would wholly eviscerate arbitration agreements." *Carter v. SSC Odin Operating Co., LLC*, 927 N.E.2d 1207, 1220 (Ill. 2010) (holding anti-jury-trial-waiver statute preempted on this basis); *cf. Southland*, 465 U.S. at 16 n.11 (FAA preempts laws by which "states could wholly eviscerate" Section 2's equal footing principle).

To take the most obvious example, a State could not enact a statute reviving the ouster doctrine. Such a statute would discriminate against arbitration. *See Southland*, 465 U.S. at 13; Cohen, *Commercial Arbitration and the Law* 153-169 (1918). But even apart from its discriminatory effect, the statute would be preempted because it would swallow the general rule of enforceability by making *all* arbitration agreements unenforceable. *Cf. Vaden*, 129 S. Ct. at 1274-75 ("To the extent that that the ancient 'ouster' doctrine continued to impede arbitration agreements, § 2 … directly attended to the problem."). Similarly, because "[a]rbitration carries no right to trial by jury," *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 203 (1956), a rule forbidding jury-trial waivers would make arbitration agreements unenforceable in violation of Section 2. *See also Sydnor v. Conseco Fin. Servicing Corp.*, 252 F.3d 302, 306 (4th Cir. 2001) ("[T]he loss of the right to a jury trial is a necessary and fairly obvious consequence of an agreement to arbitrate."). The

same analysis could apply to a law mandating that arbitrators follow the court system's rules of evidence, even when parties have chosen more flexible procedures. *See Bernhardt*, 350 US. at 203 n.4 ("Arbitrators are not bound by the rules of evidence.")

By contrast, the FAA does not preclude States from applying general contract defenses, such as unconscionability, to one-sided, exculpatory procedural limitations in adhesion contracts if the effect is not to require procedures incompatible with arbitration. For example, an agreement that allowed an employer full discovery but denied any discovery to an employee seeking to bring a discrimination claim would likely be found unconscionable. And, for the same employee, an arbitration agreement that banned *any* discovery for both parties might well "render[] arbitration of his factbound employment-discrimination claim unconscionable." *Rent-a-Center*, 130 S. Ct. at 2780. AT&T's hypotheticals (laws insisting on juries, "plenary" discovery, civil procedure rules), on the other hand, do not implicate concerns about one-sided terms or systematic exculpation. A State's law might reflect the view that "trial by jury is preferable to any other," Va. Const. art I § 11, but factfinding by an impartial arbitrator as opposed to a lay jury would not amount to exculpation. *See, e.g., Schriro v. Summerlin*, 542 U.S. 348, 356 (2004) ("For every argument why juries are more accurate factfinders, there is another why they are less accurate.").

AT&T never claims that classwide proceedings and arbitration are fundamentally incompatible. This Court's recent decision in *Stolt-Nielsen S.A. v. Animalfeeds Int'l Corp.*, 130 S. Ct. 1758 (2010), was premised on the availability of class arbitration as a potential dispute resolution mechanism that parties may adopt by contract. The

Court stated that a party may be "compelled under the FAA to submit to class arbitration" where "there is a contractual basis for concluding that the party *agreed* to do so." *Id.* at 1775 (emphasis in original). Were these two modes of efficient dispute resolution inherently incompatible, that conclusion would make no sense. *See also Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 454-55 (2003) (Stevens, J., concurring) ("There is nothing in the Federal Arbitration Act that precludes" the conclusion that "class-action arbitrations are permissible."); *id.* at 459 (Rehnquist, C.J., dissenting) ("The FAA does not prohibit parties from choosing to proceed on a classwide basis.").[24]

II. States That Have Found Class-Action Bans Unenforceable Have Not Distorted Their Law.

A. This Court Should Defer to the Exposition of State Law By the States' Highest Courts.

AT&T "devotes the bulk of its argument" to "a question of state law, which this Court does not sit to review." *Volt*, 489 U.S. at 474; *see* Pet. Br. 18-21, 31-47. AT&T claims that the California Supreme Court has been unfaithful to California law, reaching a "novel" decision that "deviates from," "distort[s]," and "gerrymander[s]" the State's own law. Br. 20, 32, 47. Those claims are wrong: California, like the many other States that have reached similar conclusions, has faithfully applied longstanding common-law contract principles to the contemporary phenomenon of the class-action ban. But even if the application of California law (and, by logical extension, the

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[24]Here, class arbitration is not a possibility because AT&T prefers to defend class actions in court, reserving arbitration for individual disputes. Pet. App. 61a ("blowup" clause).

law of twenty other States) represented a departure from state-law precedent, that would have no bearing on the question before the Court, which is whether state and federal law actually conflict. As it did in *Volt*, this Court should decline to review whether the court of appeals misapplied California contract law. 489 U.S. at 474-75; *see* S. Ct. Rule 10.

Entertaining AT&T's plea would entail an unprecedented intrusion into state sovereignty, inevitably federalize state contract law, and prove unworkable in practice. This Court, and the lower federal courts, could become endlessly embroiled in assessing the fidelity of state-court decisions to state law, thereby "breeding litigation from a statute that seeks to avoid it." *Allied-Bruce*, 513 U.S. at 275. AT&T supplies no judicially manageable standards to govern that thorny inquiry.[25]

As a matter of "comity and respect," this Court ordinarily "defer[s] to the decisions of state courts on issues of state law." *Bush v. Gore*, 531 U.S. 98, 112 (2000) (Rehnquist, C.J., concurring); *id.* at 148-51 (Ginsburg, J., dissenting). And "as a rule [the Court] should be and [is] 'reluctant to federalize' matters traditionally covered by state common law," including the law of contracts. *Patterson v. McLean Credit Union*, 491 U.S. 164, 183 (1989); *see* Davant, *Tripping on the Threshold: Federal Courts' Failure to Observe Controlling State Law Under the Federal Arbitration Act*, 51 Duke L.J. 521, 546-50 (2001)

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[25]Already, this case has encouraged a tag-along petition by another wireless carrier, alleging that the New Jersey Supreme Court has "manipulat[ed] and "distort[ed]" New Jersey law. Pet. for Cert. in *Cellco P'ship d/b/a Verizon Wireless v. Litman*, No. 10-398 at 22, 26 (filed Sept. 20, 2010).

(Section 2 "preserves an important sphere of state sovereignty").

To be sure, this Court must occasionally consider the relationship between an allegedly abrupt change in state law and preexisting precedents—for example, under the fair-warning principle of the Due Process Clause, *see Rogers,* 532 U.S. 451, or in entertaining judicial takings or Contracts Clause claims. *See Stop the Beach Renourishment, Inc. v. Florida Dept. of Envt'l Prot.*, 130 S. Ct. 2592 (2009); *Hale v. Iowa State Bd.*, 302 U.S. 95, 101 (1937); *Hart and Wechsler's The Federal Courts and the Federal System* 527-40 (5th ed. 2003). But unlike those constitutional claims, which are concerned with *changes* in state law, FAA preemption does not depend on whether state law has changed.

Even by the standards of the fair-notice and takings cases, AT&T's argument goes beyond the proper scope of this Court's review. The argument boils down to a claim that the unconscionabilty principles applied below do not really "*exist* at law or in equity," 9 U.S.C. § 2, measured against preexisting state law. But when there is "doubt about [the] existence" of a state-law principle, this Court "do[es] not make [its own] assessment but accept[s] the determination of the state court." *Stop the Beach*, 130 S. Ct. at 2607 n.9 (Scalia, J., plurality opinion); *see Rogers*, 532 U.S. at 460-62; *id.* at 468-49 (Scalia, J., dissenting) (a "reasonable reading of state law by the State's highest court is binding upon us" as to whether a rule was "truly established" by state law).

Because no perfect eighteenth- or nineteenth-century equivalent to class-action bans exists, the various decisions addressing their enforceability are in that sense necessarily "novel" in relation to the past. But there is a "crucial difference between simply applying a law to a

new set of circumstances and changing the law that has previously been applied to the very circumstances before the court," *id.* at 471, and AT&T does not even suggest that the latter sort of break in the law has occurred here.

B. California Has Been Faithful to Its Own Common Law of Contracts.

AT&T measures *Discover Bank* against a cramped understanding of the history and scope of unconscionability doctrine and concludes that it comes up short. There is nothing aberrant about *Discover Bank*. The California Supreme Court—like the many other courts that have held class-action bans unenforceable—has faithfully applied the State's own contract law.

1. Unconscionability Is Not Limited to Nineteenth-Century Standards. Unconscionability is not, as AT&T contends, limited to the nineteenth-century inquiry into whether a contract is one that "shocks the conscience" and to which "no person who is not acting under delusion would agree." Pet. Br. 32-33, 4. These descriptions "are accurate in the sense that a contract that meets either of these descriptions is surely unconscionable," but they are "underinclusive" compared to modern unconscionability doctrine. *Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 269 (Ill. 2006). Although unconscionability has "deep roots in both law and equity," 7 *Corbin on Contracts* § 29.2, "it is only with the advent of U.C.C. 2-302," in 1952, "that courts began in earnest to grapple with the ramifications of the unconscionability doctrine and to spell out specific content." Ayres and Speidel, *Studies in Contract Law* 562 (7th ed. 2008).

AT&T's formulation, from Justice Story's *Commentaries on the Laws of Equity*, is derived from dicta in an

1804 opinion by English Chancellor Eldon, concerning an exception to the rule that inadequate consideration was not a ground for refusing specific performance. Teeven, *A History of the Anglo-American Common Law of Contract* 316 (1990). The exception, which became widely invoked by the mid-nineteenth century, "expand[ed] the spectrum of cases short of actual fraud qualifying for relief and aided in opening juridical thought to further extensions." *Id.* In short, the "shocks the conscience" standard represents an early stage in the evolution of unconscionability doctrine—not its final state. *Id.*

2. As a Matter of California Law, AT&T's Agreement Is Not Fair to the Parties. AT&T contends that its agreement "is undeniably fair" to the Concepcions and that the unconscionability and exculpatory-clause doctrines are limited to considering "the fairness of the challenged provision to the parties to the agreement before the court." Pet. Br. 34, 43. From those premises, AT&T reasons that *Discover Bank*'s unconscionability analysis impermissibly "rests entirely" on a concern for third parties. Br. 36. AT&T is wrong at each step.

The class-action ban was not "fair to the Concepcions," as AT&T contends (at 36), nor did the lower courts so conclude. The theme that its class-action ban is "consumer friendly" runs throughout AT&T's brief, but AT&T never explains how that claim about fairness relates to the federal preemption issue before the Court, as opposed to the application of state law to the facts. Because the question whether the agreement is unconscionable or unfair implicates only questions of California law and no genuine issue under the FAA, it presents no issue for this Court to resolve. *See Volt*, 489 U.S. at 474. In any event, the California Supreme Court's decision in *Discover Bank* and the lower court decisions in

this case are eminently reasonable applications of state contract law.

First, as the court of appeals recognized, AT&T's agreement allows it to buy off small claimants like the Concepcions for the face amount of their claim, ensuring that the "premiums" and fees it purports to offer consumers will not actually be paid. Pet. App. 10a. AT&T does not claim that these illusory premiums have *ever* been paid out. Thus, "the maximum gain to a consumer for the hassle of arbitrating a $30.22 dispute is still just $30.22." Pet. App. 10a. And AT&T can effectively negate any real incentive an attorney might have to represent a consumer with such a claim. *Id.* AT&T offers no reason to believe that the Concepcions would have brought their $30.22 deceptive-advertising claim if they had been forced to do so individually, or that they could have found counsel to do so. *See Carnegie v. Household Int'l., Inc.*, 376 F.3d 656, 661 (7th Cir. 2004) (Posner, J.) ("The realistic alternative to a class action is not 17 million individual suits, but zero individual suits, as only a lunatic or a fanatic sues for $30."). For that reason, it will often "be in the interest of a class-action defendant" to "'buy off' the individual private claims of the named plaintiffs"—the rare individuals who detect fraud or discrimination and take the initiative to make a claim. *Deposit Guar. Nat'l Bank v. Roper*, 445 U.S. 326, 339 (1980) (noting that "[r]equiring multiple plaintiffs to bring separate actions, which effectively could be 'picked off' by a defendant's tender," "would obviously frustrate the objectives of class actions."). This is a "classic application of the strategy of divide and conquer." *Abron v. Black & Decker*, 654 F.2d 951, 973 (4th Cir. 1981).

Second, as the numbers show (*see supra* 3-5), the "infinitesimal" number of arbitrations and claims under

AT&T's clause, *Coneff*, 620 F. Supp. 2d at 1258, compared to the universe of claims that could have been brought absent the class-action ban, belies the notion that the effect of the ban is anything but exculpatory as a practical matter.

Third, AT&T's fairness argument is internally inconsistent. On the one hand, AT&T (at 37) criticizes *Discover Bank* for failing to restrict its analysis to whether the agreement was unconscionable "at the time it was made," *i.e.*, from an *ex ante* perspective.[26] On the other hand, AT&T's fairness argument depends on a purely *ex post* perspective. AT&T assesses fairness from the perspective of a perfectly informed, sophisticated consumer who has already detected fraud, knows the law has been violated, and seeks to come forward and obtain compensation. Particularly in the context of small-dollar consumer fraud, that picture describes very few people, and it would not be rational for someone to assume, *ex ante*, that he or she will fall into that category.

Fourth, the agreement was unfair to the Concepcions from an *ex ante* perspective because they were forced to give up any benefits that class actions would have *for them*—either as named plaintiffs in a class action or, more likely, as beneficiaries of the compensatory, deterrent, and cost-spreading effects of class actions brought on their behalf by others.

When the Concepcions entered into the transaction, they had no reason to believe they would be capable of

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[26] Although AT&T seeks to exclude consideration of deterrence or effects on others, that is the whole point of *ex ante* analysis: "It involves looking forward and asking what effects the decision about the case will have in the future—on parties who are entering similar situations." Farnsworth, *The Legal Analyst* 5 (2007).

monitoring and detecting AT&T's fraudulent or deceptive practices, recognizing such practices as unlawful, or hiring a lawyer to find out. "Most individuals are too preoccupied with daily life and too uninformed about the law to pay attention to whether they are being overcharged or otherwise inappropriately treated by those with whom they do business." Hensler et al., *Class Action Dilemmas* 68 (2000). That an individual's "claim may be so small, or the plaintiff so unfamiliar with the law, that he would not file suit individually," are among the chief justifications for the class action. *Phillips Petroleum v. Shutts*, 472 U.S. 797, 873 (1985). The class-action mechanism "overcomes the problem that small individual recoveries may fail to provide an adequate incentive for a litigant to investigate a claim." *Muhammad,* 912 A.2d at 100 ("Without the availability of a class-action mechanism, many consumer-fraud victims may never realize that they may have been wronged."); *see Kinkel*, 857 N.E.2d at 263-76 ("The typical consumer may feel that such a charge is unfair," but, without an attorney, will not "be aware that he or she has a claim that is supported by law"); *Gentry v. Superior Court*, 165 P.3d 557, 567 (Cal. 2008) ("[I]ndividual employees may not sue because they are unaware that their legal rights have been violated.").

California courts have long refused to enforce contracts shortening statutes of limitation so as to make it unreasonably difficult, from an *ex ante* perspective, for a party to "discover their causes of action." *Moreno v. Sanchez*, 131 Cal. Rptr. 2d 684, 698 (Cal. Ct. App. 2003); *see Beeson v. Schloss*, 192 P. 292, 294 (Cal. 1920). More generally, the concern that a party may enter into a contract with an exculpatory term that is unfair in light of the party's *ex ante* lack of knowledge has been recognized in California contract law for more than a century.

See, e.g., In re Garcelon's Estate, 38 P. 414, 419 (Cal. 1894) (refusing to enforce an exculpatory clause in part because "the parties to the contract could not," *ex ante*, "have in view any particular subject-matter, or have any conception of the amount which might be involved in the causes of action upon which the covenant was to operate"); *Steven v. Fidelity & Casualty Co. of New York*, 377 P.2d 284, 298 (Cal. 1962) (condemning exclusionary clause in adhesion contract as unconscionable for placing an "unexpected burden" on consumers).

In the language of economics, detecting and investigating fraud requires individuals to incur information, monitoring, and transaction costs, which may actually exceed the individuals' net loss. *See* Hay, *Procedural Justice: Ex Ante vs. Ex Post*, 44 UCLA L. Rev. 1803, 1815-16 (1997) ("[E]ffective deterrence of undesirable behavior may require costly investments by the beneficiary of such deterrence."). Class actions spread those costs, preventing individuals from having to bear them alone. *See Roper*, 445 U.S. at 338 n.9; Posner, *Economic Analysis of the Law* § 21.11 (6th ed. 2003). Under AT&T's contract, however, a consumer is unknowingly made to incur those costs, which are normally borne by all similarly situated people and those who act as private attorneys general. *Id.* It is not reasonable to impose that burden on consumers.

As one seminal California unconscionability case explained, "a contract is largely an allocation of risks between the parties" and a "contractual term is substantively suspect if it reallocates the risks of the bargain in an objectively unreasonable or unexpected manner." *A&M Produce*, 186 Cal. Rptr. at 125. "[N]ot all unreasonable risk reallocations are unconscionable," and reasonableness must be assessed in relation to the level of

relative bargaining power and unfair surprise. *Id. A&M Produce* held unconscionable a disclaimer of warranties on the grounds that it was "patently unreasonable to assume that a buyer would purchase a standardized mass-produced product from an industry seller without any enforceable performance standards. From a social perspective, risk is most appropriately borne by the party best able to prevent its occurrence." *Id.* (citing Holmes, *The Common Law* 117 (1881)). That same principle applies with full force to the monitoring and information costs of detecting fraud, the transaction costs of prosecuting it once it is detected, and the compensatory and deterrent effect of class actions.

3. Contract Law Has Long Been Concerned With a Contract's Effects Beyond the Two Parties. AT&T wrongly claims that the unconscionability and exculpatory-clause doctrines are blind to a contract's effects on similarly situated parties to the same form contract, or to deterrent effects benefitting society. But "the fundamental function of contract law (and recognized as such at least since Hobbes's day) is to deter people from behaving opportunistically toward their contracting parties." Posner, *Economic Analysis of Law* 94 (6th ed. 2003). And contract law recognizes that, "in many relationships, there is a situation where one person is dealing contemporaneously with several others so that a clause limiting his liability to one of them is considered to have a tendency to lead to conduct injurious to others." 8 *Williston on Contracts* § 19:27; *see also* 15 *Corbin on Contracts* § 85.1 (where "the contract's terms are such that it will have [the effect of] defrauding one or more third persons," it is an "accepted tenet of contract law that such a bargain contradicts public policy and cannot be enforced").

By the nineteenth century, American law "recognized the community-wide effect of seemingly private contracts, as between utility company and customer, insurer and insured, and railroad and farmer." Teeven, *A History of the Anglo-American Common Law of Contract* 296 (1990). This Court's cases at the turn of the twentieth century—in the context of form contracts imposed by railroads, shippers, insurers, and telegraph companies—recognized the danger of exculpatory clauses to the public. These cases rested partly on the status of the companies as "common carriers," whose role "is a public one, charg[ed] with a duty of accommodating the public in the line of his employment." *Liverpool*, 129 U.S. at 471. In one leading case, this Court found it obvious that "the public interest" was "affected by such individual contracts" and emphasized the loss in deterrence if they were enforced. *N. Y. Cent. R.R. v. Lockwood*, 84 U.S. 357, 378-79 (1873) ("The [customer] is only one individual of a million. He cannot afford to higgle or stand out and seek redress in the courts."). In 1892, this Court described the parallel concerns of law and equity with the public effects of contracts: The common law would not enforce contracts that "are detrimental to the interests of the public," while equity would refuse to "aid in the enforcement of unconscionable, oppressive, or iniquitous contracts." *Pope Mfg. v. Gormuly & Jeffery Mfg.*, 144 U.S. 224, 233, 236 (1892).

Like this Court, the California courts have long emphasized the public effects of unconscionable and exculpatory contracts. In *Tunkl v. Regents of the University of California*, the California Supreme Court explained that the "public interest" in a contract with an exculpatory clause is the main factor affecting its enforceability. 383 P.2d 441, 443-46 (Cal. 1963). *Tunkl* compared one early case in which an exculpatory clause had been en-

forced in a contract between a railroad and a commercial tenant, because "the interests of the public in the contract" were "more sentimental than real," *Stephens v. S. Pac. Co.*, 41 P. 783, 786 (Cal. 1895), with a decision declining to enforce an exculpatory clause in a bank's form contract. The latter decision, *Hiroshima v. Bank of Italy*, 248 P. 947, 953 (Cal. 1926), rested on a public deterrence rationale—that exculpatory clauses "induce a want of care"—and the reality that "the banking public," not merely the "particular individual," "is interested in seeing that the bank is held accountable for the ordinary and regular performance of its duties." *Id. Tunkl* established an influential test defining the "category of agreements affecting the public interest"—generally mass contracts between individuals and large businesses performing an essential service for the public. 383 P.3d at 447; *see* 8 *Williston on Contracts* § 19:22. *Tunkl*'s insights, in turn, were incorporated into the modern doctrine of unconscionability, which California codified in 1979.[27]

Other States, too, have recognized the classwide effects of exculpatory clauses in standard-form contracts in areas such as housing and employment. As one court put it, "one must ignore present day realities to say that

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[27] *Cont. Airlines v. Goodyear Tire & Rubber Co.*, 819 F.2d 1519, 1527 (9th Cir. 1987) ("*Tunkl*'s approach essentially is rooted in the unconscionability doctrine."); *Graham*, 623 P.2d at 174 n.20 ("contracts having a demonstrable public service aspect may be deemed unconscionable"); Roos, *The Doctrine of Unconscionability: Alive and Well in California*, 9 Cal. W. L. Rev. 100, 105-06 (1972); Cava and Wiesner, *Rationalizing a Decade of Judicial Responses to Exculpatory Clauses*, 28 Santa Clara L. Rev. 611, 654 (1988); Reith, *Contractual Exculpation From Tort Liability in California—The "True Rule" Steps Forward*, 52 Cal. L. Rev. 350 (1964).

such an exculpatory clause … is purely a 'personal and private affair' and 'not a matter of public interest.'" *McCutcheon v. United Homes Corp.*, 486 P.2d 1093 (Wash. 1971). Considered "realistically," an exculpatory clause in a contract is not "a purely private affair" because its "generalized use … may have an impact upon thousands of potential tenants." *Id.; see also Cappaert v. Junker*, 413 So.2d 378 (Miss. 1982) (same in employment context). In short, nothing in the common law of contracts requires courts to shut their eyes to the classwide or societal impact of private contracts.

4. California Law Properly Considers the Circumstances of the Case. Finally, AT&T claims (at 37-39) that *Discover Bank* constitutes an *ex post* analysis because it instructs courts to consider the claims in the case before declining to enforce an unconscionable class-action ban. But that is a *limitation*, not an expansion, of the test. In contrast to an analysis of facial unconscionability, consideration of the circumstances determines whether enforcement will be unconscionable as applied—that is, whether it will have "any unconscionable result." Cal. Code. Civ. § 1670.5. Where a class-action ban would not operate to exculpate the defendant—because, for example, the claims involve large amounts of damages—the ban will be enforced. *See supra*, at 21 n.14. The alternative approach would have a far broader reach. *Compare Discover Bank*, 113 P.3d at 1110 (considering whether case involves "large numbers of consumers" and "individually small sums of money" before striking ban) *with Vasquez-Lopez v. Beneficial Oregon, Inc.*, 152 P.3d 940, 951 (Or. Ct. App. 2007) (striking ban without regard to circumstances). AT&T does not explain how this *limitation* on the reach of a state-law contract defense could possibly discriminate against arbitration.

III. Absent Discrimination Against Arbitration, AT&T's Broad Arguments for Purposes-and-Objectives Preemption Lack Merit.

Alternatively, AT&T argues that application of generally applicable state contract law in this case "'stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.'" *Volt*, 489 U.S. at 477 (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)). AT&T asks the Court go beyond Section 2's text—which expressly preserves state contract-law defenses that do not discriminate against arbitration—and hold that state law is preempted even if it does not discriminate against arbitration. AT&T claims that two goals of the FAA—"allowing parties to select their own dispute-resolution procedures" and "removing impediments to arbitration"—independently preempt state law. Pet. Br. 49-56.

Despite AT&T's protestations (Pet. Br. 48 n.15), both arguments rest on "generalized notions of congressional purpose," *Wyeth*, 129 S. Ct. at 1205 (2009) (Thomas, J., concurring in the judgment), rather than the FAA's text or structure. Because the statute's text answers the preemption question, the Court should not embark on a freewheeling, extratextual attempt to divine the "purposes" or "objectives" envisioned by Congress in 1925. Such an inquiry risks undervaluing the Constitution's system of dual sovereignty, disregarding structural limitations on federal supremacy, and placing unelected federal judges in the unseemly position of choosing among "generalized notions of congressional purposes that are not contained within the text of a federal law." *Id.* at 1205; *see Arthur Andersen*, 129 S. Ct. at 1902 n.5 (describing the "federal policy favoring arbitration" as a "vague prescription" with uncertain meaning).

AT&T's arguments illustrate the "danger of invoking obstacle pre-emption based on the arbitrary selection of one purpose to the exclusion of others." *Pharm. Research & Mfrs. of Am. v. Walsh*, 538 U.S. 644, 678 (2003) (Thomas, J., concurring in the judgment). To be sure, the purposes AT&T cites formed part of Congress's motivation in enacting the FAA. "But no legislation pursues its purposes at all costs" and "it frustrates rather than effectuates legislative intent simplistically to assume that whatever furthers the statute's … objective[s] must be the law." *Rodriguez v. United States*, 480 U.S. 522, 525-26 (1987) (per curiam). To cast aside the FAA's text and preempt state law based on a vague appeal to congressional purpose would ignore the balance struck by the FAA—between enforcing agreements and ensuring consent, and between allowing parties to select procedures and ensuring that arbitration is not used to exculpate stronger parties.

1. AT&T argues that conditioning enforcement of an arbitration agreement on the availability of particular procedures is "self-evident[ly]" incompatible with the FAA. Pet. Br. 49. As discussed in Part I.C. above, a categorical approach to preemption along the lines suggested by AT&T is not only incompatible with the FAA's text, but would risk undermining arbitration's legitimacy as a fair means of dispute resolution. The Court has never previously suggested that general contract-law defenses may not apply to limitations on procedures. Just last Term in *Rent-a-Center*, 130 S. Ct. at 2780, the Court discussed state-law unconscionability challenges involving two types of procedures—one-sided discovery limitations and a fee-splitting provision—and recognized that those challenges would be properly governed by Nevada law. *Id.*

Preston v. Ferrer, 552 U.S. 346 (2008), lends no support to AT&T's view that the FAA immunizes all otherwise unconscionable procedural limitations from state-law challenges. Neither party in *Preston* invoked Section 2's savings clause. The Court held only that the FAA preempted a statute granting an administrative agency exclusive jurisdiction over an issue that the parties had agreed to arbitrate. Here, by contrast, AT&T seeks an end run around the FAA's nondiscrimination standard for preemption of state-law defenses merely because "procedures" are at issue—an approach that has no basis in the FAA's text or this Court's cases. None of the FAA's purposes requires that result.

Indeed, application of state unconscionability law to strike down adhesion contracts with exculpatory clauses *furthers* two of the FAA's key purposes: that arbitration be consensual, and that it provide adequate remedies for wrongdoing. The purpose AT&T invokes—the "purpose of allowing parties to select their own dispute-resolution procedures" (Pet. Br. 49)—is merely one aspect of "the foundational FAA principle" that "arbitration is a matter of consent, not coercion." *Stolt-Nielsen*, 130 S. Ct. at 1773, 1775. And, as AT&T acknowledges, unconscionability is concerned with "whether enforcing the agreement is consistent with the party-autonomy principle underlying contract law." Pet. Br. 41 n.12. The doctrine is premised on the insight that terms "unreasonably favorable to the stronger party … may show that the weaker party had no meaningful choice, no real alternative, or did not in fact assent or appear to assent to the unfair terms." *Restatement (Second) of Contracts* § 208, Comment d; *see also The Kensington*, 183 U.S. 263, 268 (1902) (exculpatory clauses in form contracts "will be deemed as wanting in the element of voluntary assent"). Thus, "a determination that a contract is 'unconscionable' may in

fact be a determination that one party did not intend to agree to the terms of the contract." *Am. Airlines, Inc. v. Wolens*, 513 U.S. 219, 249 (1995) (O'Connor, J., concurring in judgment and dissenting in part).[28]

Applying unconscionability defenses to unfair "procedures" also furthers another key purpose of the FAA—ensuring that arbitration "only determines the choice of forum," *EEOC v. Waffle House*, 534 U.S. 279, 295 n.10 (2002), but does not "operate … as a prospective waiver of a party's right to pursue statutory remedies." *Vimar*, 515 U.S. at 540; *cf. Green Tree Fin. Corp.-Alabama v. Randolph*, 531 U.S. 79, 90 (2000) (recognizing that "the existence of large arbitration costs" may interfere with vindication of statutory rights). Because arbitration under the FAA represents only a choice of forum, the statute does not preempt the ability of the States to police their marketplaces by providing remedies for, and deterring, wrongdoing. The FAA is neutral with respect to the compensation and deterrence policies of substantive state laws, including laws aimed at consumer fraud. The FAA favors arbitration, not exculpation.

Finally, even if the FAA did generally preempt state-law regulation of "procedures," the question whether state law permits a party to enforce an exculpatory class-

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[28]Unconscionability's "intent is not to erase the doctrine of freedom of contract, but to make realistic the assumption of the law that the agreement has resulted from real bargaining between the parties who had freedom of choice and understanding and ability to negotiate in a meaningful fashion." 8 *Williston on Contracts* § 18.8; *see also* Di Matteo and Rich, *A Consent Theory of Unconscionability: An Empirical Study of Law in Action*, 33 Fla. St. L. Rev. 1067 (2006) (empirical study demonstrating that "the notion of true assent" is "an overriding consideration in unconscionability cases").

action ban cannot be cast aside "as being merely [about] what 'procedural mode' [is] available." *Stolt-Nielsen*, 130 S. Ct. at 1776; *see also id.* at 1783 (Ginsburg, J., dissenting) ("[W]hen adjudication is costly and individual claims are no more than modest in size, class proceedings may be 'the thing'—i.e., without them, potential claimants will have little, if any, incentive to seek vindication of their rights."); *Shady Grove Orthopedic Assocs., P.A. v. Allstate Ins. Co.*, 130 S. Ct. 1431, 1442 (2010) ("[M]ost procedural rules do … affect[] a litigant's substantive rights."). As *Discover Bank* made clear, as a matter of state law, the availability of classwide proceedings is, "particularly in the consumer context, often inextricably linked to the vindication of substantive rights." 113 P.3d at 1109.

The class-action device itself arises out of fundamental principles of equity—specifically, the principle that, "to prevent a failure of justice, a court of equity permits a portion of the parties in interest to represent the entire body." *Smith v. Swormstedt*, 57 U.S. 288, 303 (1853). In many cases, as this Court recognized more than a century ago, precluding classwide proceedings altogether "would amount to a denial of justice." *Id.*

2. AT&T also makes what it describes (at 22) as an even "broad[er]" purposes-and-objectives preemption argument, based on the FAA's "liberal policy favoring arbitration." *Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983). "Whatever the meaning of that vague prescription," *Arthur Andersen*, 129 S. Ct. at 1902 n.5, it cannot be invoked to strike down an application of general state-contract law that Section 2 expressly says can negate the enforceability of an arbitration agreement. That is precisely the point of the

statutory phrase "enforceable, save upon such grounds." 9 U.S.C. § 2.

a. AT&T attacks class arbitration as a "lose-lose proposition" that "no rational business will agree to." Pet. Br. 22. But some businesses *do* prefer classwide arbitration. *See Skirchak v. Dynamics Research Corp.*, 508 F.3d 49, 63 (1st Cir. 2007) ("[W]e asked the parties whether each would prefer to be in arbitration even if the class action waiver was stricken. The company said it would prefer to be in arbitration."); *Fensterstock v. Educ. Fin. Partners*, 611 F.3d 124, 140 (2d Cir. 2010) (same). Businesses may decide to choose class arbitration because it combines the efficiencies of both arbitration and aggregation and is faster and potentially less costly than class-action litigation in court. *See* Amicus Br. of American Arbitration Association in *Stolt-Nielsen v. Animalfeeds*, 130 S. Ct. 1758, at 22-24 (statistics suggesting that "class arbitration proceedings … take less time than the average class action in court"). If the decision below is affirmed, businesses will remain free to make that choice.

In any event, the complaints of AT&T and its amici are really criticisms of arbitration itself: They complain, for example, that arbitration lacks appellate review and that arbitral awards are subject to narrow review by courts. Pet. Br. 54-55. The hostility to class arbitration these arguments reflect is "a remnant of the historic mistrust of the arbitral process" that the FAA was intended to eradicate. Buckner, *Toward a Pure Arbitral Paradigm of Classwide Arbitration: Arbitral Power and Federal Preemption*, 82 Denv. U. L. Rev. 301, 301 (2004); *see also Discover Bank*, 113 P.3d at 1113 (view that "arbitration is an inferior forum and therefore cannot be trusted with classwide claims" reflects "the very mis-

trust of arbitration that has been repudiated" by this Court under the FAA). The claim that large cases are too complex for arbitration is at odds with the liberal policy favoring arbitration. *See Mitsubishi*, 473 U.S. at 633 ("[T]he factor of potential complexity alone does not persuade us that an arbitral tribunal could not properly handle an antitrust matter."). To be sure, because "the relative benefits of class-action arbitration" to businesses may be "less assured" than class-action litigation in court, *Stolt-Nielsen*, 30 S. Ct. at 1775, a business may decide to forgo class arbitration in favor of litigation. But, under the FAA, that choice is up to the business drafting the agreement. *Id.*

b. AT&T predicts that allowing courts to apply general contract law defenses to class-action bans will frustrate the "liberal policy favoring arbitration" because businesses will abandon arbitration entirely rather than face classwide proceedings in arbitration. That is a false choice: Businesses can easily retain all the benefits (speed, efficiency, informality, low cost) of individual arbitration, whether they choose to resolve classwide proceedings in arbitration or in court. California law is neutral as to whether classwide proceedings take place in arbitration or in court—the answer depends on the parties' agreement. *See Stolt-Nielsen*, 130 S. Ct. at 1775-76; *Fensterstock*, 611 F.3d at 140-41.

In this case, proceeding via litigation rather than arbitration once the class-action ban was deemed unenforceable was AT&T's choice. *See* Pet. App. 61a ("blowup clause"). AT&T, not California law, determined that if it could not enforce its class-action ban, it would prefer to proceed in court. AT&T and businesses like it are free to impose that decision on their customers if they prefer, even while continuing to arbitrate the vast range of

claims by consumers and employees—individual consumer billing issues, wrongful termination claims by employees—that may be suitable for arbitration on an individual rather than a classwide basis.

The securities industry has followed precisely that approach for the past 18 years—requiring individual arbitration for most disputes, but leaving classwide proceedings to court rather than arbitration.[29] The securities industry's experience shows that the status quo works: The regime established under the law of California and many other states—under which individual arbitration remains available for the types of claims in which it can provide an appropriate consensual remedy, and class proceedings in court or arbitration are available for claims where necessary to prevent the exculpation of defendants from wrongdoing—is in fact fully compatible with a healthy system of arbitration.

CONCLUSION

The decision below should be affirmed.

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[29] Securities industry rules preclude enforcement of an arbitration agreement "against a member of a certified or putative class action," until class certification is denied, the class is decertified, or the claimant is excluded or withdraws from the class. FINRA Code of Arbitration Procedure § 12204(d), *available* at http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4110 (last visited September 21, 2010); *see* Constitution of the New York Stock Exchange, Article IX, Section 2, Rule 600 (same).

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APPENDIX

Decisions Holding That Class-Action Bans May Be Found Unenforceable Under General Principles of State Contract Law

State Law	Decisions
Alabama	*Leonard v. Terminix, Co., L.P.*, 854 So. 2d 529, 538-39 (Ala. 2002)
Arizona	*Cooper v. QC Financial Services, Inc.*, 503 F. Supp. 2d 1266, 1279-80 (D. Ariz. 2007)
California	*Gentry v. Superior Court*, 165 P.3d 556 (Cal. 2008); *Discover Bank v. Superior Court*, 113 P.3d 1100, 1110 (Cal. 2005); *America Online Inc. v. Superior Court (Mendoza)*, 108 Cal. Rptr. 2d 699 (Cal. Ct. App. 2001)
Delaware	*Caban v. J.P. Morgan Chase & Co.*, 606 F. Supp. 2d 1361, 1371-72 (S.D. Fla. 2009) (applying Delaware law)
Florida	*S.D.S Autos, Inc. v. Chrzanowski*, 976 So. 2d 600, 610 (Fla. Ct. App. 2007); *America Online, Inc. v. Pasieka*, 870 So. 2d 170 (Fla. Ct. App. 2004); *Bell-south Mobility LLC v. Christopher*, 819 So. 2d 171, 173 (Fla. Ct. App. 2002); *Powertel v. Bexley*, 743 So. 2d 570, 576 (Fla. Ct. App. 1999); *Reuter v. Davis*, 2006 WL 3743016 (Fla. Cir. Ct. 2006)
Georgia	*Dale v. Comcast Corp.*, 498 F.3d 1216,

	1224 (11th Cir. 2007); *Gordon v. Branch Banking and Trust Co.*, 666 F. Supp. 2d 1347, 1351-52 (N.D. Ga. 2009)
Illinois	*Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 278 (Ill. 2006)
Massachusetts	*Feeney v. Dell, Inc.*, 908 N.E.2d 753, 762-68 (Mass. 2009); *Skirchack v. Dynamics Research Corp.*, 508 F.3d 49, 59-60 (1st Cir. 2007)
Michigan	*Wong v. T-Mobile USA, Inc.*, 2006 WL 2042512 (E.D. Mich. 2006); *Lazado v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087 (W.D. Mich. 2000)
Missouri	*Brewer v. Missouri Title Loans, Inc.*, --- S.W.3d ---, 2010 WL 3430411 (Mo. 2010); *Ruhl v. Lee's Summit Honda*, --- S.W.3d ----, 2010 WL 3441256 (Mo. 2010); *Woods v. QC Financial Services, Inc.*, 280 S.W.3d 90 (Mo. Ct. App. 2008); *Whitney v. Alltel Communications, Inc.*, 173 S.W.3d 300, 308-10 (Mo. Ct. App. 2005)
New Jersey	*Muhammad v. County Bank of Rehoboth*, 912 A.2d 88, 100 (N.J. 2006); *Homa v. American Express Co.*, 558 F.3d 225, 234 (3d Cir. 2009)
New Mexico	*Fiser v. Dell Computer Corp.*, 188 P.3d 1215, 1221 (N.M. 2008)

North Carolina	*Tillman v. Commercial Credit Loans, Inc.*, 655 S.E. 2d 362, 373 (N.C. 2008)
Ohio	*Eagle v. Fred Martin Motor Co.*, 809 N.E.2d 1161, 1183 (Ohio Ct. App. 2004)
Oregon	*Vasquez-Lopez v. Beneficial Oregon, Inc.*, 152 P.3d 940, 950-51 (Or. Ct. App. 2007)
Pennsylvania	*Thibodeau v. Comcast Corp.*, 912 A.2d 874, 886 (Pa. Super. Ct. 2006)
South Carolina	*Herron v. Century BMW*, 2010 WL 1541297 (S.C. 2010)
Washington	*Scott v. Cingular Wireless*, 161 P.3d 1000, 1006-08 (Wash. 2007); *McKee v. AT&T Corp.*, 191 P.3d 845, 858 (Wash. 2008); *Dix v. ICT Group, Inc.*, 161 P.3d 1016 (Wash. 2007)
West Virginia	*State ex rel. Dunlap v. Berger*, 567 S.E.2d 265, 282-83 (W. Va. 2002)
Wisconsin	*Coady v. Cross-County Bank*, 729 N.W.2d 732, 748 (Wis. Ct. App. 2007), *review denied*, 737 S.W.3d 432 (Wis. 2007)