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States vs US high court in arbitration tug-of-war

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The U.S. Supreme Court's efforts to enforce and protect arbitration agreements are of particular relevance to California, where courts have been especially active in seeking to limit the enforceability of such agreements.

Although the Federal Arbitration Act was enacted nearly a century ago — in 1925 — the U.S. Supreme Court has, in recent years, issued major pronouncements expanding the FAA's reach. In particular, the court has systematically rejected efforts by states to limit the enforcement of arbitration agreements, noting that the FAA was intended to combat "judicial hostility to arbitration agreements." *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2001). Under the FAA, such hostility is prohibited, and courts are required to place arbitration agreements "on equal footing with all other contracts." *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463 (2015).

In its efforts to uphold the FAA's twin goals — "enforcement of private agreements and encouragement of efficient and speedy dispute resolution," as the court stated in *Concepcion* — the Supreme Court has taken a broad approach. In *Concepcion*, the court said rules having a "disproportionate [negative] impact on arbitration agreements," or that are "inconsistent" with the enforcement of arbitration agreements are not allowed. "[T] he FAA," after all, "was designed to promote arbitration."

This past year, the U.S. Supreme Court issued another important decision underscoring its efforts to protect arbitration agreements against state efforts to curb their availability. In *Kindred Nursing Ctrs. Ltd. v. Clark*, 137 S. Ct. 1421 (2017), the court rejected Kentucky's attempt to require that power-of-attorney holders receive special authority before "waiv[ing] a principal's fundamental constitutional rights" — a set of rights that just so happened to include the "right to trial by jury" and little else. In rejecting the Kentucky Supreme Court's rule, the U.S. Supreme Court made two key clarifications regarding the FAA's sweeping scope.

First, a state rule that demonstrates "hostility to arbitration" will be struck down, even if the rule is cast in "broader terms" and does not specifically mention arbitration agreements. The court made clear that it would look closely at the practical scope of any purportedly neutral rule impacting arbitration agreements. If, as in *Clark*, the rule applies only to "arbitration agreements and black swans," the court will treat it as an arbitration-specific rule.

Second, the court held that the FAA's protection of arbitration agreements precludes both rules limiting the enforcement of such agreements and rules restricting the ability to enter into such agreements in the first place. The FAA, the court held, cares not just about enforcement of arbitration agreements, but also "about what it takes to enter into them." To hold otherwise, the court explained, would "make it trivially easy for States to undermine the Act — indeed, to wholly defeat it."

The U.S. Supreme Court's efforts to enforce and protect arbitration agreements are of particular relevance to California, where courts have been especially active in seeking to limit the enforceability of such agreements. Indeed, the landmark *Concepcion* decision was a thorough rejection of the California Supreme Court's "*Discover Bank* rule" — a rule that invalidated as unconscionable arbitration agreements that contained waivers of class action procedures. In so holding, the *Concepcion* court noted the judicial hostility toward arbitration has manifested itself in "a great variety" of "devices and formulas" and that California courts had been at the forefront of this hostility. The California Court of Appeal vindicated this observation a few years later in *DIRECTV* when it characterized *Concepcion* as not being the "law of California," prompting the U.S. Supreme Court to state that "the Supremacy Clause forbids state courts to dissociate themselves from federal law because of disagreement with its content or a refusal to recognize the superior authority of its source."

But California has nonetheless searched for other ways to limit the reach of the FAA and allow cases seeking classwide or similar relief to proceed in state court despite agreements to arbitrate. Just this year, in *McGill v. Citibank, N.A.*, 2 Cal. 5th 945 (2017), the California Supreme Court held that, under California law, a contract may not waive the right to seek public injunctive relief — that is, an injunction on behalf of the public.

In *McGill*, the plaintiff filed a class action against Citibank, asserting that Citibank's marketing of a "credit protector" plan violated California's Unfair Competition Law, false advertising law, and Consumers Legal Remedies Act. She sought, among other things, "an injunction prohibiting Citibank from continuing to engage in its allegedly illegal and deceptive practices." Citibank's arbitration agreement contained relatively common terms stating that the arbitrator could "determine the rights and obligations

between the named parties only" and "will not award relief for or against anyone who is not a party." Both Citibank and the plaintiff agreed that these clauses meant that, under this agreement, the plaintiff was precluded from seeking public injunctive relief in any forum.

The California Supreme Court explained that the injunction sought by the plaintiff was a form of "public injunctive relief" because the injunction would have "the primary purpose and effect of prohibiting unlawful acts that threaten future injury to the general public." And the court held that, as a matter of California law, Citibank's arbitration provision was invalid "insofar as it purport[ed] to waive McGill's statutory right to seek public injunctive relief in any forum." Following *McGill*, arbitration provisions that limit a plaintiff's ability to seek public injunctive are unenforceable under California law.

What we see from these recent decisions are two sides in a legal tug-of-war: The U.S. Supreme Court has wielded the FAA to strike down state-created obstacles to arbitration and allow for broader enforcement of arbitration agreements; but, at the same time, state courts have been just as persistent in attempting to stem the tide of arbitration and maintain access to the courts. For parties and practitioners this means that understanding the nuances of FAA jurisprudence is essential. The case law allows for creative arguments both *for* and *against* enforcement of arbitration agreements.

But however the battles over the FAA play out in the short term, there can be little doubt that arbitration's ascent is inevitable.

In one recent example of this, the 9th U.S. Circuit Court of Appeals rejected a First Amendment challenge to enforcement of an arbitration agreement, holding that, by merely giving parties "the private choice to arbitrate," the FAA does not convert private contracting to state action. *Roberts v. AT&T Mobility LLC*, 2017 DJDAR 11737 (9th Cir. Dec. 11, 2017) (stating that "[w]hile the post-*Concepcion* increase in arbitration could 'in some sense be seen as encouraging [AT&T to arbitrate,] ... this kind of subtle encouragement is no more significant than that which inheres in the State's creation or modification of any legal remedy'") (quoting *Am. Mfrs. Mut. Ins. Co. v. Sullivan*, 526 U.S. 40, 53 (1999)). Hence, practitioners will need to be well-versed in the current state of FAA law to assert or rebut these arguments.

But however the battles over the FAA play out in the short term, there can be little doubt that arbitration's ascent is inevitable. Given the costs and delays that come with court litigation, more and more parties will choose to enter into arbitration agreements, and — absent some major infirmity in the contract — those agreements will ultimately be enforceable under the FAA. Because arbitrations involve unique procedural and substantive aspects (as well as opportunities), experience in this world is fundamental. As litigation increasingly shifts to private forums, parties and practitioners must know the state of play.

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