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CONSUMER PROTECTION

N.J. Courts Waste No Time in Applying New Class-Action Waiver Ruling

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On April 27, the U.S. Supreme Court decided *AT&T Mobility LLC v. Concepcion et ux.*, 131 S.Ct. 1740 (2011), a monumental 5-4 decision holding California's *Discover Bank* rule to be inconsistent with the Federal Arbitration Act (FAA), and therefore pre-empted by that statute. (The California rule had required class-action waivers in arbitration agreements to be found unconscionable and therefore unenforceable.) Less than six months after the Supreme Court's ruling, two appellate decisions from New Jersey have applied *Concepcion*.

Concepcion

Concepcion, which arose out of a dispute between a cell phone company (AT&T) and two of its consumers (the Concepcions), held that the FAA pre-empts California's so-called *Discover Bank* rule, which had classified most class-action waivers contained in consumer contracts as unconscionable and therefore unenforceable. In invalidating the *Discover Bank* rule, *Concepcion* expressly approved arbitration clauses that contain class-action waivers in consumer contracts. The Court held that the *Discover Bank* rule was pre-empted by the FAA because, in the words of the majority, the rule presented "an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." According to the majority, the *Discover Bank* rule's fatal flaw was its interference with the twin goals of the FAA: 1) the enforcement of private agreements according to their terms and 2) the encouragement of efficient dispute resolution.

The Concepcions invoked the FAA's so-called saving clause, which permits arbitration agreements to be declared unenforceable "upon such grounds as exist at law or in equity for the revocation of any contract," including unconscionability. They argued that the *Discover Bank* rule, which originated from California's unconscionability jurisprudence, constituted "grounds as exist at law" for revoking the class-action waiver clause in AT&T's agreement. In rejecting that argument, the Supreme Court noted that both the District Court and the Circuit Court had emphasized how fair AT&T's agreement is to consumers. The majority then favorably described many aspects of the arbitration agreement, and appeared most impressed by AT&T's willingness to assume the costs of arbitration, including its agreement to pay for all costs of nonfrivolous claims, and to pay claimants a minimum of $7,500 and twice their legal fees if they obtained an arbitration award greater than AT&T's last settlement offer.

Litman

In *Litman v. Cellco P'ship*, the Third Circuit addressed whether the FAA pre-empted New Jersey's equivalent to the *Discover Bank* rule, a rule announced in *Muhammad v. County Bank of Rehoboth Beach, Del.*, which required the availability of class-wide arbitration for New Jersey consumers. The sole issue before the Third Circuit was whether the class-waiver provision alone invalidated the agreement. The court concluded that, under *Concepcion*, it did not.


Elliot D. Ostrove

Like *Concepcion*, the *Litman* decision arose out of a dispute between a cell phone company (Verizon) and two of its customers. The plaintiffs objected to Verizon's monthly administrative charges, which they alleged violated Verizon's contractual obligation to provide cell phone service at a fixed price. They filed a putative class action alleging breach of contract, unjust enrichment and violations of the New Jersey Consumer Fraud Act.

Verizon moved to compel individual arbitration pursuant to its agreements with plaintiffs, but the plaintiffs argued that the agreements' class-arbitration waiver was unconscionable and therefore unenforceable under *Muhammad*. Verizon responded that *Muhammad* was pre-empted by the FAA. The District Court agreed, holding that the class-arbitration waiver was valid, and granting Verizon's motion to compel

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individual arbitration. The plaintiffs timely appealed, and while the appeal was pending, the Third Circuit decided *Homa v. Am. Express Co*., which specifically held that *Muhammad* was not pre-empted by the FAA. The plaintiffs moved for summary reversal based on *Homa*, and the Third Circuit granted the motion.

The plaintiffs' victory proved short-lived. The U.S. Supreme Court granted Verizon's petition for writ of certiorari and remanded the case to the Third Circuit for it to review in light of *Concepcion*. On remand, the Third Circuit concluded that *Concepcion* had both abrogated *Homa* and provided that *Muhammad* is pre-empted by the FAA. The Third Circuit therefore dismissed the case and compelled individual arbitration. Unlike the *Concepcion* court, the *Litman* court did not analyze the terms of the arbitration agreement before it in detail. Indeed, it appears from the decision that, apart from the class-waiver provision, the fairness of the arbitration terms was not challenged.

Foulke

In *NAACP of Camden County East and Thomas v. Foulke Mgmt. Corp*., New Jersey's Appellate Division declined to enforce an arbitration agreement, concluding that "the cumulative effect of the many inconsistencies and unclear passages in the arbitration terms…compel us to declare them unenforceable for lack of mutual assent." In so holding, the Appellate Division emphasized that post-*Concepcion*,

> [S]tate courts remain free to decline to enforce an arbitration provision by invoking traditional legal doctrines governing the formation of a contract and its interpretation. . . . As part of that assessment, we must examine whether the terms of the provisions were stated with sufficient clarity and consistency to be reasonably understood by the consumer who is being charged with waiving her right to litigate a dispute in court.

Foulke arose out of the purchase of a new car, and the subsequent dispute between an owner and operator of several motor vehicle dealerships (Foulke), and one of its customers, Geraldine Thomas. When the parties could not resolve their dispute, Thomas and the NAACP of Camden County East sued the dealership. The trial court ruled the class-action waiver provisions contained in the agreement between Foulke and Thomas did not violate public policy and were thus enforceable. The lawsuit was dismissed and the matter referred to arbitration. The plaintiffs appealed.

After oral argument had been held before the Appellate Division, the U.S. Supreme Court decided *Concepcion*, and the Appellate Division therefore considered supplemental letter briefs from the parties addressing the impact of that decision. In holding the arbitration agreement to be unenforceable, the Appellate Division explained that *Concepcion* had "acknowledged that the FAA does not require an arbitration provision to be enforced if the provision is defective for reasons other than public policy or unconscionability," including principles governing "the formation and interpretation of an agreement…subject to the overarching objectives of the FAA." This meant that "an agreement to arbitrate must be the product of mutual assent, as determined under customary principles of contract law."

In analyzing the arbitration provisions before it, the court noted the provisions were not contained in a single document but rather, were "spread across three different documents," including a retail installment contract (RIC), a so-called GAP addendum and a separate arbitration document (the SAD). The Appellate Division explained that "[v]iewed in their totality, the arbitration provisions . . . are too plagued with confusing terms and inconsistencies to put a reasonable consumer on fair notice of their intended meaning."

The court criticized at length the many contradictory arbitration provisions contained in the three documents, which pertained to such central terms as the venue of arbitration, time limitations for initiating arbitration, and who would bear the cost of arbitration. Critically, the court observed that in light of the many inconsistencies, it was even unclear whether there was a class waiver at all. The Appellate Division ultimately severed all of the arbitration clauses from the agreements, concluding that they were "unenforceable for lack of mutual assent."

What This Means for Companies

The lessons learned from the New Jersey courts' application of *Concepcion* are as straightforward as they are important. The narrow issue before the *Litman* court was whether the presence of a class-waiver could singlehandedly invalidate an otherwise clear and internally consistent arbitration agreement. The Third Circuit correctly concluded that, under *Concepcion*, it cannot. Like *Litman*, *Foulke* also concluded that the mere presence of a class-waiver provision in an arbitration agreement cannot alone invalidate that agreement. However, the Appellate Division did not hesitate to invalidate the dealership's *entire* arbitration agreement, in light of the murky and inconsistent terms spread across three separate documents. *Foulke* demonstrates that where feasible, it is preferable for companies to consolidate all arbitration terms within a single document. Where multiple documents are necessary, however, companies must be vigilant in ensuring that arbitration terms are consistent.

In light of these recent appellate decisions, it cannot be overstated that any arbitration agreement and its attendant class-action waiver must be both clearly written, internally consistent and, most importantly, fair if it is to be enforced by New Jersey courts. Together, *Litman* and *Foulke* confirm that *Concepcion* provides companies with an opportunity to avoid the quagmire of class-action litigation and its attendant cost by requiring both the arbitration of certain grievances and the waiver of class actions. *Foulke* however, also stands as a stark reminder that the FAA's saving clause survived *Concepcion*, and that it remains a viable option for consumers seeking to invalidate class waivers. Contrasting *Concepcion* and *Foulke* further reveals that courts may pay special attention to the costs of forced arbitration, and specifically, who is required to bear those costs. Proper application of these decisions to consumer and employee contracts, and beyond, can ensure that those who believe they have been aggrieved are provided with a fair forum in which to address their grievance, while at the same time, shield companies from the extreme costs and uncertainties of class-action litigation. ■