U.S. Supreme Court Limits Class Arbitration

May 1, 2019

Last Wednesday, in *Lamps Plus Inc. v. Varela*, the U.S. Supreme Court ruled that classwide arbitration is barred unless the arbitration agreement expressly authorizes it. The Court held that classwide arbitration interferes with the fundamental attributes of arbitration and the Federal Arbitration Act ("FAA") preempts state contract law principles that construe ambiguous agreements as authorizing classwide arbitration. In light of this decision, businesses that wish to permit classwide arbitration should review the wording of their arbitration agreements, including in employment and consumer contracts, to confirm that they explicitly provide for class procedures.

Background. The Court's decision is the latest in a series of cases where the Court has narrowed the availability of classwide arbitration. In 2010, the Court ruled in *Stolt-Nielsen v. Animal Feeds Int'l Corp*. that classwide arbitration cannot be compelled if the arbitration agreement is silent on the issue. In 2018, the Court held in *Epic Systems Corp. v. Lewis* that class action waivers in employment agreements are enforceable under federal law.

The present case also involves employment agreements. After Lamps Plus inadvertently disclosed the tax information of 1,300 of its employees, an employee filed a class action lawsuit in federal court. Lamps Plus sought to compel individual arbitration on the basis of the employment agreement's arbitration provision. The Ninth Circuit compelled arbitration. Since Lamps Plus' arbitration provision did not expressly mention class proceedings and was thus ambiguous as to the availability of classwide arbitration, the Ninth Circuit applied the *contra proferentem* doctrine under California contract law and construed the ambiguity against the drafter, allowing the employees to proceed as a class.

The Supreme Court's Decision. In a 5-4 decision, with Justice Thomas concurring, the Court held that classwide arbitration cannot be compelled when an agreement is ambiguous. This decision extends the holding of *Stolt-Nielsen*, foreclosing classwide arbitration if agreements are either "silent" or ambiguous as to the parties' intent.

Writing for the majority, Chief Justice Roberts argued that "arbitration is a matter of consent." And unlike the individual arbitration proceedings contemplated by the FAA, classwide arbitration "makes the process slower, more costly, and more likely to generate procedural morass than final judgment" and "sacrifices the principal advantage of arbitration—its informality." These fundamental differences prevent a court from

compelling classwide arbitration absent a clear expression of mutual consent to classwide arbitration.

The Court also held that the FAA preempted the state law doctrine of *contra proferentem*. Courts frequently apply this doctrine to employment and consumer agreements and other contexts of unequal bargaining power. The doctrine is a "rule of last resort" that construes contractual ambiguity against the drafter of the contract. The Court argued that the doctrine's "policy" purpose to incentivize the drafter to be as clear as possible "seeks ends other than the intent of the parties." Thus, the Court concluded that the application of the doctrine conflicted with the "traditional" arbitration contemplated by the FAA.

In a dissent joined by Justices Ginsburg and Breyer in full and Justice Sotomayor in part, Justice Kagan argued that the arbitration provision at issue unambiguously provides for classwide arbitration and, in any event, under the *contra proferentem* doctrine, the Court should resolve any ambiguity in the employee's favor. According to the dissent, the majority's "policy view" that classwide arbitration contravenes the benefits of arbitration cannot justify displacing general state contract law principles.

Justice Ginsburg wrote a separate dissent joined by Justices Breyer and Sotomayor in order to "emphasize once again how treacherously the Court has strayed from the principle that 'arbitration is a matter of consent'" by imposing individual arbitration on employees who would clearly prefer to proceed as a class. Justice Ginsburg argued that the majority's decision marked the latest effort to "hobble[] the capacity of employees and consumers to band together in a judicial or arbitral forum."

Looking Forward. In light of this decision, companies should carefully consider whether they want to provide for classwide arbitration in agreements with employees, consumers and others. To the extent that classwide arbitration is desired, it must be specifically provided for. Broad language mandating the arbitration of "any and all disputes, claims or controversies" or permitting the arbitrator to "award any remedy allowed by applicable law" will not be enough.

Several arbitral institutions, including the American Arbitration Association ("AAA") and JAMS, have published supplementary classwide rules and procedures. Prior to *Lamps Plus*, an incorporation by reference to the general, rather than supplementary, rules may have been sufficient to constitute consent to have an arbitrator resolve disputes concerning the availability of classwide arbitration. However, the Court now requires a more explicit statement that classwide arbitration is specifically intended by the parties. Whether this can be accomplished by incorporating rules that specifically provide for classwide arbitration is an open question.

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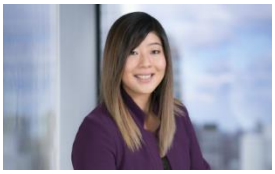
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