

No. 08-15612

**IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT**

ZOLTAN STIENER and YNEZ STIENER,
Plaintiffs – Appellees,

v.

APPLE COMPUTER, INC. and DOES 1 through 50, inclusive,
Defendants,

and

AT&T MOBILITY LLC,
Defendant-Appellant.

Appeal From an Order of the United States District Court
for the Northern District of California, No. C 07-04486 SBA

OPENING BRIEF OF APPELLANT AT&T MOBILITY LLC

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CORPORATE DISCLOSURE STATEMENT

AT&T Mobility LLC has no parent company. Its members are all privately held companies that are wholly owned subsidiaries of AT&T Inc., which is the only publicly held company with a 10 percent or greater ownership stake in AT&T Mobility LLC.

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JURISDICTIONAL STATEMENT

The district court has jurisdiction under 28 U.S.C. § 1332(d)(2)(A). The diversity-of-citizenship requirement is satisfied because plaintiffs-appellees Zoltan and Ynez Stiener are citizens of California and the members of the putative class are citizens of all 50 states and the District of Columbia, while defendant-appellant AT&T Mobility LLC (“ATTM”) is a limited liability company of Delaware, Georgia, and Texas citizenship.¹

The amount-in-controversy requirement is satisfied because the aggregate claims of members of the putative class exceed the sum or value of \$5 million, exclusive of interests and costs. Specifically, the Stieners allege that each member of the putative class, which they allege has more than 500,000 members, has suffered about \$115 in damages from allegedly hidden fees. ER193–94.

The district court issued its order denying ATTM’s motion to compel arbitration on March 12, 2008. ER1. ATTM timely filed a notice of appeal on March 18, 2008. ER29. This Court has jurisdiction under 9 U.S.C. § 16(a)(1)(B), which authorizes an immediate appeal from the denial of a motion to compel arbitration.

¹ ATTM has five members: two Delaware corporations with principal places of business in Georgia, a Delaware corporation with its principal place of business in Texas, a Georgia corporation with its principal place of business in Georgia, and a Delaware limited liability company whose sole member is a Delaware corporation with its principal place of business in Texas.

ISSUES PRESENTED FOR REVIEW

On the very day that Apple first made the iPhone available for sale, plaintiffs Zoltan and Ynez Stiener obtained two iPhones and activated them online for use with ATTM's network. When they did so, they agreed to ATTM's standard wireless service agreement, the terms of which require the Stieners to bring their disputes in arbitration on an individual basis or in small claims court. Under the terms of ATTM's arbitration provision, the customer may choose whether arbitration will be conducted in person (in the county of his or her billing address), by telephone, or by mail, and ATTM must pay all arbitration costs. In addition, if the arbitrator awards a customer greater relief than ATTM's written settlement offer, ATTM must pay the customer a minimum of \$7,500, plus double attorneys' fees.

Despite these unprecedentedly consumer-friendly features, the district court refused to enforce ATTM's arbitration provision, holding that the requirement that arbitration be conducted on an individual basis is unconscionable under California law.

ATTM's appeal presents two issues:

(1) Whether, notwithstanding the incentives to pursue individual arbitration in ATTM's arbitration provision, the provision is unconscionable under California law merely because it precludes class actions.

(2) If so, whether such an application of California law is preempted by the Federal Arbitration Act (“FAA”), 9 U.S.C. §§ 1–16.

STATEMENT OF THE CASE

Plaintiffs-appellees Zoltan and Ynez Stienner filed this putative class action against ATTM and Apple Computer, Inc. in the United States District Court for the Northern District of California. ER191. ATTM moved to compel arbitration under 9 U.S.C. § 4. ER188. The district court denied ATTM’s motion, holding that ATTM’s arbitration provision is unconscionable under California law and that the FAA does not preempt this aspect of California law. ER1.

STATEMENT OF THE FACTS

A. The Stieners Agree To Arbitrate Their Disputes With ATTM.

ATTM provides wireless phone and data services to its customers pursuant to wireless service agreements. ER81.² The Stieners are California residents and have been ATTM customers since June 29, 2007. ER192. On that day—the first day that the iPhone was available—they purchased two iPhones at a retail store. ER81. They subsequently used the Apple iTunes program to activate their iPhones for use with ATTM’s network. ER82, 194. During that activation process, the Stieners were required to click a check box next to the statement “I have read and agree to the AT&T Service Agreement.” ER82. The text of that Agreement,

² Until January 2007, ATTM was known as Cingular Wireless LLC (“Cingular”).

including its Terms of Service, was displayed immediately above the check box in a printable text box. ER116. The first sentence in the text box advised the Stieners that, by clicking on the check box below, they agreed to be “bound” to “the Terms of Service, including the *binding arbitration clause*.” *Id.* (emphasis added).

After a customer has activated an iPhone by accepting ATTM’s wireless service agreement through iTunes, ATTM also sends that customer a booklet that contains the Terms of Service of the customer’s agreement, including the arbitration provision. ER82, 102–06. Customers generally have 14 days after purchasing an iPhone to cancel service without paying an early-termination fee. ER88, 93.³

The arbitration provision in the Stieners’ Terms of Service states that “[ATTM] and you agree to arbitrate **all disputes and claims** between us” or to pursue such disputes in small claims court. ER103 (emphasis in original). The provision also specifies that arbitration must be conducted on an individual rather than class-wide basis. ER102, 106.

B. ATTM’s Consumer-Friendly Arbitration Provision.

ATTM has revised its arbitration provision on a number of occasions in an effort to make individual arbitration more attractive for its customers and to address criticisms of certain features that were common to earlier generations of

³ In addition, unopened iPhones may be returned for a complete refund. Certain open-box iPhone returns are subject to a ten percent restocking fee. ER88.

arbitration provisions. ER83–84. First-generation arbitration provisions typically required consumers to pay an equal share of arbitration fees; required that arbitration be kept confidential; specified that arbitration would take place near the company’s principal place of business; precluded important substantive remedies, such as punitive damages and attorneys’ fees; and/or permitted the business to bring its claims in court. Invoking state unconscionability principles, several courts struck down these provisions, concluding that they impeded consumers’ ability to receive full redress for their claims.⁴ For example, the Illinois Supreme Court declined to enforce ATTM’s first-generation arbitration provision—which has not been in use since the spring of 2003—because it required the plaintiff to pay \$125 in arbitration fees to pursue a \$150 claim and barred the recovery of punitive damages. *See Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 267–68, 278 (Ill. 2006). *But see, e.g., Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 F.3d 159, 171–76 (5th Cir. 2004) (upholding ATTM’s first-generation provision under Louisiana law).

ATTM (and many other companies) responded by revising their arbitration agreements to address the concerns expressed in these decisions. In general, the

⁴ *See, e.g., Ting v. AT&T*, 319 F.3d 1126, 1150–52 (9th Cir. 2003) (invalidating long distance provider’s arbitration provision that required customers to pay half the costs of individual arbitration and required that arbitration be kept confidential); *Leonard v. Terminix Int’l Co.*, 854 So. 2d 529, 535, 538–39 (Ala. 2002) (invalidating pesticide company’s arbitration provision that required homeowners to pay over \$1,000 in arbitration fees to pursue a claim worth only \$500).

second-generation arbitration provisions require companies to pay most or all of the costs of individual arbitration, authorize arbitrators to award all substantive remedies available in court, eliminate confidentiality requirements, and specify that hearings will take place near the customer's residence. Many courts have upheld such provisions, rejecting arguments that they are unconscionable merely because they require that arbitration be conducted on an individual basis. *See, e.g., Jenkins v. First Am. Cash Advance*, 400 F.3d 868, 878 (11th Cir. 2005). For example, a Missouri trial court and the U.S. District Court for the Eastern District of Pennsylvania upheld the version of ATTM's arbitration provision that was first introduced in mid-2003. *See Blitz v. AT&T Wireless Servs., Inc.*, No. 054-00281 (Mo. Cir. Ct. Nov. 28, 2005) (attached); *Weinstein v. AT&T Mobility Corp.*, 2008 WL 1914754 (E.D. Pa. Apr. 30, 2008). Likewise, the Florida District Court of Appeal and the U.S. District Court for the Southern District of Illinois have upheld an arbitration provision that AT&T Wireless Services (a predecessor of ATTM) used in 2003. *See Fonte v. AT&T Wireless Servs., Inc.*, 903 So. 2d 1019 (Fla. Dist. Ct. App. 2005); *Crandall v. AT&T Mobility, LLC*, 2008 WL 2796752 (S.D. Ill. July 18, 2008). But other courts, including this one, have invalidated ATTM's 2003 provision and similar provisions drafted by other companies, concluding that those provisions still did not go far enough to make individual arbitration a realistic means of resolving small claims. *See Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976 (9th Cir. 2007); *Scott v. Cingular Wireless*, 161 P.3d 1000

(Wash. 2007); *see also, e.g., Lowden v. T-Mobile USA, Inc.*, 512 F.3d 1213 (9th Cir. 2008), *pet. for cert. filed*, No. 07-1330 (Apr. 18, 2008); *Ford v. Verisign, Inc.*, 252 F. App'x 781 (9th Cir. 2007), *cert. denied sub nom. T-Mobile USA, Inc. v. Ford*, 128 S. Ct. 2503 (2008).

In an effort to respond to the criticisms leveled against the second generation of arbitration provisions—and in particular, the California Supreme Court's decision in *Discover Bank v. Superior Court*, 113 P.3d 1100 (Cal. 2005)—ATTM promulgated the current version of its arbitration provision in late 2006. The current provision is part of the wireless service agreement that the Stieners accepted when they activated their iPhones in June 2007. ER102–06. To ATTM's knowledge, its current arbitration provision is the most pro-consumer arbitration provision in the country. In creating the provision, ATTM consulted with, among others, Richard Nagareda, a law professor at Vanderbilt University whose scholarship focuses on aggregate dispute resolution. ER83. In a declaration filed in this case, Professor Nagareda observed that he has “never seen an arbitration provision that has gone as far as this one to provide incentives for consumers and their prospective attorneys to bring claims” on an individual basis. ER169.

ATTM's current arbitration provision includes the following pro-consumer features (ER120–21):

- **Potential for \$7,500 premium award:** If the arbitrator awards a California customer relief that is greater than ATTM's “written settlement offer made before an arbitrator was selected” but less than \$7,500, ATTM will pay the

customer \$7,500 rather than the smaller arbitral award;⁵

- **Double attorneys' fees:** If the arbitrator awards the customer more than ATTM's written settlement offer, then "[ATTM] will * * * pay [the customer's] attorney, if any, twice the amount of attorneys' fees, and reimburse any expenses, that [the] attorney reasonably accrues for investigating, preparing, and pursuing [the] claim in arbitration";⁶
- **Cost-free arbitration:** "[ATTM] will pay all [American Arbitration Association ("AAA")] filing, administration and arbitrator fees" unless the arbitrator determines that the claim "is frivolous or brought for an improper purpose (as measured by the standards set forth in Federal Rule of Civil Procedure 11(b))";⁷
- **ATTM disclaims right to seek attorneys' fees:** "Although under some laws [ATTM] may have a right to an award of attorneys' fees and expenses if it prevails in an arbitration, [ATTM] agrees that it will not seek such an award [from the customer]";
- **Small claims court option:** Either party may bring a claim in small claims court;
- **No confidentiality requirement:** The parties need not keep the arbitration confidential;
- **Full remedies available:** The arbitrator can award the same remedies to individual consumers (including punitive damages and injunctions) that a

⁵ The amount of the minimum payment varies from state to state because it is tied to the jurisdictional maximum of the customer's local small claims court. ER121. In California, the jurisdictional limit for small claims court is \$7,500. *See* Cal. Code Civ. Proc. § 116.221.

⁶ This attorney premium "supplements any right to attorneys' fees and expenses [that the customer] may have under applicable law." ER121. Thus, even if an arbitrator were to award a customer less than ATTM's last settlement offer, the customer would be entitled to an attorneys' fee award to the same extent as if the claim had been brought in court.

⁷ In the event that an arbitrator concludes that a consumer's claim is frivolous, the AAA's consumer arbitration rules would cap a consumer's arbitration costs at \$125. *See* ER158 (AAA, *Supplementary Procedures for Consumer-Related Disputes* § C-8).

court could award;

- **Flexible consumer procedures:** Arbitration will be conducted under the AAA’s Commercial Dispute Resolution Procedures and the Supplementary Procedures for Consumer-Related Disputes, which the AAA designed with consumers in mind;
- **Conveniently located hearing:** Arbitration will take place “in the county * * * of [the customer’s] billing address”; and
- **Choice of in-person, telephonic, or no hearing:** For claims of \$10,000 or less, customers have the exclusive right to choose whether the arbitrator will conduct an in-person hearing, a hearing by telephone, or a “desk” arbitration in which “the arbitration will be conducted solely on the basis of documents submitted to the arbitrator.”⁸

C. ATTM’s Dispute-Resolution Process In Practice.

A formal arbitration proceeding between ATTM and one of its customers (or an action in small claims court) is the last step of ATTM’s dispute resolution process. Indeed, that step is rarely taken because most disputes are resolved to the customer’s and ATTM’s mutual satisfaction after the customer has called or e-mailed ATTM’s customer care department. ER83–84. ATTM’s arbitration provision is an important factor contributing to this early resolution of disputes: Because the provision makes dispute resolution through arbitration quick and convenient—and because the provision may require ATTM to pay the customer \$7,500 and double attorneys’ fees—ATTM’s customer service representatives

⁸ Under the AAA rules that would otherwise apply, either party may insist on a hearing in cases involving claims of \$10,000 or less. *See* ER156 (AAA, *Supplementary Procedures for Consumer-Related Disputes* §§ C-5, C-6). For claims exceeding \$10,000, a hearing would be held unless both parties agreed to forgo it. *See id.*

have a strong incentive to accommodate any reasonable request. Thus, as ATTM demonstrated in its submission to the district court, in September 2007 alone, ATTM's representatives dispensed over \$119 million in credits for customer concerns and complaints. ER84. Over the 12-month period from October 2006 to September 2007, ATTM representatives dispensed over \$1 billion in credits. *Id.*

A customer who is dissatisfied with the resolution offered by the customer care department can take the next step—as required by ATTM's arbitration provision—of providing ATTM's legal department with notice of the dispute. ER120–21. That is as simple as sending a letter to ATTM or filling out and mailing a one-page Notice of Dispute form that ATTM has posted on its web site at <http://www.att.com/arbitration-forms>. ER83.

ATTM's legal department generally responds to a notice of dispute with a written settlement offer—including an offer to pay the customers' attorneys' fees whenever a customer indicates that he or she is represented by counsel and has requested reimbursement. ER68. As with ATTM's customer service representatives, the goal of ATTM's legal department is to resolve any colorable claim quickly, efficiently, and to the customer's satisfaction without the need for a customer to initiate arbitration proceedings. ER84.

If the dispute cannot be resolved within 30 days, the customer may begin the arbitration process. ER120–21. To do so, the customer need only fill out a one-page Demand for Arbitration form and send copies to the AAA and to ATTM.

Customers may obtain a copy of the form from the AAA's web site or use a simplified form that ATTM has posted on its web site, at <http://www.att.com/arbitration-forms>. ER83. To further assist its customers, ATTM's web site includes a layperson's guide on how to arbitrate a claim (<http://www.att.com/arbitration-information>). *Id.*

Many ATTM customers have found individual arbitration to be a viable dispute resolution mechanism. In the ten months before ATTM moved to compel arbitration in this case, ATTM received over 500 notices of dispute or demands for arbitration. ER84. Moreover, in 2005 and 2006, about 850 customers exercised their right under ATTM's arbitration provisions to sue ATTM in their local small claims court. ER85.

D. The Stieners File A Putative Class Action Against ATTM Notwithstanding Their Agreement To Arbitrate.

Despite their agreement to arbitrate (or to bring disputes in small claims court), the Stieners filed a putative class action against ATTM and the manufacturer of the iPhone, Apple Computer, Inc. ("Apple"). ER191. In their lawsuit, the Stieners alleged that ATTM and Apple did not adequately disclose the details of the iPhone battery-replacement program, thus violating California's Unfair Competition Law, Cal. Bus. & Prof. Code §§ 17200 *et seq.*, and breaching an implied warranty of merchantability, Cal. Com. Code § 2314. ER197–98. Plaintiffs also raise a variety of common-law claims, including breach of contract

and fraudulent concealment. ER196–98. They seek to represent a class consisting of “all individuals or entities who at any time from June 29, 2007 to the date of judgment in this action bought and implemented the iPhone and sustained damages as a result.” ER194.

ATTM responded to the complaint by moving to compel arbitration under the Stieners’ arbitration agreement. ER188–89. The district court (Armstrong, J.) denied ATTM’s motion. ER1. The court first held that ATTM’s arbitration provision is unconscionable under California law as construed by this Court in *Shroyer*. According to the court, the Stieners’ arbitration agreement is procedurally unconscionable because (i) it is part of an “adhesive contract” that is “without market alternatives,” given “the iPhone’s uniqueness” (ER13–14), and (ii) the Stieners first learned of ATTM’s arbitration provision after purchasing their Apple iPhones, when they activated the iPhones at home using the iTunes software (ER15–16). The court then held that the prohibition of class arbitration in ATTM’s arbitration provision renders it substantively unconscionable because ATTM could not show “that *all* iPhone consumers would recover more, on average, if the Court let the Arbitration Agreement stand rather than allowing the Stieners’ class action to proceed.” ER21 (emphasis in original). Last, the court held that the FAA did not preempt application of California’s unconscionability doctrine to invalidate ATTM’s arbitration provision. ER25–27.

STANDARD OF REVIEW

“The validity * * * of an arbitration clause [is] reviewed de novo.”
Nagrampa v. MailCoups, Inc., 469 F.3d 1257, 1267 (9th Cir. 2006) (en banc).

SUMMARY OF ARGUMENT

The Federal Arbitration Act requires courts to enforce arbitration agreements as written. The sole exception is when the party resisting arbitration demonstrates the existence of a generally-applicable contract defense—*i.e.*, a ground “for the revocation of *any* contract.” 9 U.S.C. § 2 (emphasis added).

Here, the district court determined that such a ground exists because, in its view, ATTM’s current arbitration provision is unconscionable under California law. That holding is fundamentally mistaken as a matter of California law and, in any event, preempted by the FAA.

1. Both this Court and the California Supreme Court have made clear that California law *does not* impose an across-the-board rule barring class waivers in arbitration provisions. The district court’s holding that ATTM’s arbitration provision is unconscionable runs counter to those decisions because it leaves no room for any consumer contract to require disputes to be resolved through individual arbitration.

a. To begin with, the district court erred in holding that ATTM’s provision exhibits any more than a minimal amount of procedural unconscionability. True, courts in California have held that arbitration provisions

in non-negotiable form contracts are procedurally unconscionable, albeit only to a “minimal” or “modest” extent. But the district court determined that the circumstances under which the Stieners accepted the terms of ATTM’s service agreement implicated a heightened degree of procedural unconscionability. The court’s holding on that point rests on two flawed premises: (1) that the iPhone is so unique that there is no acceptable substitute for it; and (2) that there is something unfair about providing the full legal terms to a customer after the point of sale. The first defies common sense: No one is under compulsion to buy an iPhone. And the second is not generally applicable to all contracts, nor could it be without causing much of modern commerce to grind to a halt. Accordingly, it may not be applied to an arbitration provision under Section 2 of the FAA.

b. The district court also erred in holding that ATTM’s current arbitration provision is substantively unconscionable. The court chiefly relied on *Shroyer*, in which this Court struck down an earlier version of ATTM’s arbitration provision, holding that class waivers are unconscionable “when the potential for individual *gain* is small.” 498 F.3d at 986 (emphasis in original).

The arbitration provision at issue here directly addresses the concerns expressed in *Shroyer* by providing for a minimum award of \$7,500, plus double attorneys’ fees if the arbitrator awards the customer more than the amount of ATTM’s written settlement offer, by specifying that ATTM will pay the full cost of arbitration, and by giving the customer sole discretion to choose between an in-

person arbitration (in the county of his or her billing address), arbitrating by telephone, or submitting the matter for decision on the papers. *See* pages 7–9, *supra*. Together these pathbreaking features of ATTM’s arbitration provision provide powerful incentives for consumers to pursue their disputes with ATTM in individual arbitration, and for ATTM to resolve those disputes to the customers’ satisfaction.

Deviating from *Shroyer*, the district court nevertheless held that ATTM’s arbitration provision was unconscionable because ATTM had “failed to establish [that] its Arbitration Agreement is as efficient a dispute resolution mechanism as class actions are” (ER23–24) and that, on average, *all* putative class members would recover more in individual arbitration than they would receive if the Stieners’ class action were to proceed (ER21).

That reliance on speculation about hypothetical proceedings produces a standard that is virtually impossible to satisfy, particularly when, as here, the district court has indulged unrealistically sanguine assumptions about class actions, while taking a baselessly negative view of how individual arbitration works. The district court’s principal concern appeared to be that, under ATTM’s dispute resolution system, any consumer who complained would be too likely to receive full relief quickly and without cost, rather than the pennies-on-the-dollar settlement (and large attorneys’ fee award) that a successful class action would produce. As a result, the district court effectively imposed an across-the-board ban on arbitration

provisions that require individual arbitration. That outcome is directly contrary to the case-by-case approach to unconscionability (not to mention the focus on whether the customer has an adequate incentive to arbitrate) required by *Shroyer* and *Discover Bank*.

2. Not only is the district court's interpretation of California law mistaken as a matter of state law, it also is preempted by the FAA.

a. Under California's generally applicable unconscionability standard, only contractual terms that shock the conscience are unenforceable. There is nothing conscience-shocking, however, about trading the little-used right to bring a class action for lower-priced wireless service and a subsidized means of resolving individual disputes—especially because the vast majority of disputes could never be brought as a class action in the first place and thus would be infeasible to pursue in court. Accordingly, in holding ATTM's arbitration provision to be unconscionable simply because it provides for individual arbitration, the district court necessarily distorted the generally applicable standard for unconscionability. That violates the FAA's command that arbitration provisions be enforced "save upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added).

b. Because the district court's holding conditions the enforceability of arbitration provisions on the availability of class arbitration, it directly conflicts with the FAA's purpose of fostering agreements to arbitrate. As the Supreme

Court has recently reiterated, “[a] prime objective of an agreement to arbitrate is to achieve streamlined proceedings and expeditious results.” *Preston v. Ferrer*, 128 S. Ct. 978, 986 (2008) (internal quotation marks omitted). Class arbitration frustrates that objective by eliminating the efficiencies of individual arbitration. Because nothing could more clearly frustrate the purpose of the FAA, the rule embraced by the district court is preempted.

ARGUMENT

The FAA provides that written agreements to arbitrate disputes “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” 9 U.S.C. § 2. Congress enacted the FAA to “reverse the longstanding judicial hostility to arbitration agreements * * *[,] to place [these] agreements upon the same footing as other contracts[,] * * * [and to] manifest a liberal federal policy favoring arbitration agreements.” *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 289 (2002) (internal quotation marks omitted). Accordingly, “questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration.” *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

There is no dispute here that the FAA applies and that the Stieners’ claims fall within the scope of their agreement to arbitrate. *See* ER5–6. The district court held, however, that the requirement of individual arbitration is unconscionable under California law, which, it concluded, is a valid ground “for the revocation of

any contract.” As we discuss in Part I, the district court was wrong that the class waiver in ATTM’s arbitration provision is unconscionable under California law. Moreover, as we discuss in Part II, the district court’s interpretation of California law is preempted by the FAA.

I. THE STIENERS’ AGREEMENT TO ARBITRATE IS FULLY ENFORCEABLE UNDER CALIFORNIA LAW.

The district court erred in holding that ATTM’s current arbitration provision is unconscionable under California law. In California, a party wishing to avoid enforcement of a contractual provision on unconscionability grounds bears the burden of proving both procedural and substantive unconscionability. *See, e.g., Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 690 (Cal. 2000); *Engalla v. Permanente Med. Group, Inc.*, 938 P.2d 903, 915–16 (Cal. 1997). Procedural unconscionability involves “oppression” or “surprise” in the making of the agreement (*Armendariz*, 6 P.3d at 690), while substantive unconscionability focuses on whether the contractual term in question is so “overly harsh” or “one-sided” (*id.*) as to “shock the conscience.” *Belton v. Comcast Cable Holdings, LLC*, 60 Cal. Rptr. 3d 631, 649–50 (Ct. App. 2007); *Aron v. U-Haul Co.*, 49 Cal. Rptr. 3d 555, 564 (Ct. App. 2006). Put another way, the bargain that the term represents must be one that “no man in his senses, and not under delusion, would make on the one hand, and [that] no honest and fair man would accept on the other.” *Herbert v. Lankershim*, 71 P.2d 220, 257 (Cal. 1937) (quoting *Odell v. Moss*, 62 P.

555, 557 (Cal. 1900) (quoting in turn 1 JOSEPH STORY, COMMENTARIES ON EQUITY JURISPRUDENCE § 244 (14th ed. 1918)); see also *Cal. Grocers Ass’n, Inc. v. Bank of Am.*, 27 Cal. Rptr. 2d 396, 402 (Ct. App. 1994).

In performing the unconscionability inquiry, California courts employ a “sliding scale”: “the more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa.” *Armendariz*, 6 P.3d at 690 (internal quotation marks omitted). In other words, if “the procedural unconscionability, although extant, [is] not great,” the party attacking the term must prove “a greater degree of substantive unfairness.” *Marin Storage & Trucking, Inc. v. Benco Contracting & Eng’g, Inc.*, 107 Cal. Rptr. 2d 645, 656–57 (Ct. App. 2001). Under California’s sliding-scale approach, the Stieners’ agreement to arbitrate their disputes with ATTM is fully enforceable.

A. The Manner In Which The Stieners Agreed To Arbitrate Involves At Most A Minimal Degree Of Procedural Unconscionability.

We acknowledge that, under this Court’s interpretation of California law, the manner in which the Stieners agreed to ATTM’s arbitration provision involves a modest degree of procedural unconscionability. Although the Stieners readily could have obtained wireless service elsewhere, this Court held in *Shroyer* that “a contract may be procedurally unconscionable under California law when the party with substantially greater bargaining power presents a ‘take-it-or-leave-it’ contract

to a customer—even if the customer has a meaningful choice as to service providers.” 498 F.3d at 985 (internal quotation marks omitted).⁹ As the California Court of Appeal has made clear, however, the non-negotiable nature of an agreement suffices only to establish “a minimal degree of procedural unconscionability.” *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 356 (Ct. App. 2007), *cert. denied*, 128 S. Ct. 2501 (2008).

The district court concluded, however, that the agreement here goes beyond this “minimal degree of procedural unconscionability” in two ways. First, it held that there was additional “oppression” because the iPhone is “apparently unique

⁹ Although the panel in the present case is bound by this aspect of *Shroyer*, we submit that the *Shroyer* court erred in “follow[ing] the [California] courts that reject the notion that the existence of ‘marketplace alternatives’ bars a finding of procedural unconscionability,” instead of following the conflicting line of California cases that have held that there can be no procedural unconscionability when the customer has alternatives to contracting with the defendant. 498 F.3d at 985. The two competing lines of published decisions reveal an unmistakable pattern. The cases finding procedural unconscionability all involve arbitration provisions. *See Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 353–56 (Ct. App. 2007), *cert. denied*, 128 S. Ct. 2501 (2008); *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862, 867 (Ct. App. 2002); *Villa Milano Homeowners Ass’n v. Il Davorge*, 102 Cal. Rptr. 2d 1, 5–6 (Ct. App. 2000). The decisions that do not all involve other types of contractual provisions. *See Belton*, 60 Cal. Rptr. 3d at 650 (requirement that cable music subscribers receive basic cable television); *Wayne v. Staples, Inc.*, 37 Cal. Rptr. 3d 544, 556 (Ct. App. 2006) (declared-value insurance for package shipping); *Aron*, 49 Cal. Rptr. 3d at 564 (rental truck refueling policy); *Morris v. Redwood Empire Bancorp*, 27 Cal. Rptr. 3d 797, 807 (Ct. App. 2005) (termination fee); *Dean Witter Reynolds, Inc. v. Super. Ct.*, 259 Cal. Rptr. 789, 795 (Ct. App. 1989) (termination and annual fee). Because the conflict hinges on whether an arbitration provision is at issue, reliance on the arbitration-specific rule violates the FAA’s requirement that state unconscionability law cannot single out arbitration for suspect status. *See Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987).

among wireless products, and thus without market alternatives.” ER14. Second, the court determined that the Stieners were “surprised” because ATTM’s terms of service were not furnished to them when they purchased their iPhones, but rather when they signed up for ATTM service and activated their iPhones for use with ATTM’s network. ER15–16.

Each of these conclusions is mistaken as a matter of California law.

1. The Stieners’ Contracting Process Was Not Oppressive.

The Stieners in fact had ample market alternatives. Under California law, one product or service can be a market alternative to another even if it is not a perfect substitute in each and every respect. For example, in *Belton* the California Court of Appeal rejected a Comcast customer’s argument that the non-negotiable terms of service of Comcast’s cable television music service involved “oppression” because “FM radio,” internet radio broadcasts, “compact disc player[s],” and satellite music services were all acceptable alternatives, even though “the satellite service was expensive” and “the quality of sound when listening to FM radio over the Internet was inferior.” 60 Cal. Rptr. 3d at 650.¹⁰ Although the iPhone is a top-

¹⁰ Similarly, the California Supreme Court has held that an employee’s ability to select another health plan that did not require arbitration prevented the arbitration provision in the one he chose from being “oppressive.” *Madden v. Kaiser Found. Hosps.*, 552 P.2d 1178, 1186 (Cal. 1976). Although the opinion does not disclose how the alternative health plans compared to the plan that the plaintiff had selected, they almost certainly were not perfect substitutes, as the point of offering multiple health plans is to provide an array of choices as to price, coverage, and other terms.

notch product (ER13–14 & n.9), the Stieners certainly could have obtained other wireless phones with Internet and music capabilities and could have used those devices with other wireless carriers. Under California law, those options qualify as reasonable market alternatives.¹¹

Even if there were no adequate substitutes for ATTM service with an iPhone, however, that would not warrant a finding of oppression because an iPhone plainly is a “nonessential recreational” good, which the Stieners “always ha[d] the option of simply forgoing.” *Belton*, 60 Cal. Rptr. 3d at 650 (cable music service is non-essential); *see also Provencher v. Dell, Inc.*, 409 F. Supp. 2d 1196, 1202 (C.D. Cal. 2006) (personal computers are non-essential); *cf. Riensche v. Cingular Wireless LLC*, 2007 WL 3407137, at *8 (W.D. Wash. Nov. 9, 2007) (“telephone service, particularly cellular service, is not a necessity”).¹² The district court thought otherwise because of “the *breakthrough* iPhone’s uniqueness.” ER14 (emphasis in original). But under that logic, a transaction involving any product or service with unique features would be regarded as procedurally

¹¹ One popular Internet review web site posted 55 reviews of cell phones with digital music players before the release of the iPhone. *See* http://reviews.cnet.com/4566-6454_7-0-10.html?filter=501994_9116115 (listing reviews by date).

¹² *Accord Enderlin v. XM Satellite Radio Holdings, Inc.*, 2008 WL 830262, at *16 (E.D. Ark. Mar. 25, 2008) (satellite radio service “is a non-essential luxury entertainment item”); *Auto Style Leasing Ltd. v. Evans*, 1995 WL 144812, at *5 (S.D.N.Y. Mar. 31, 1995) (“the significance of plaintiff’s superior bargaining power is diminished when one considers [that] the subject of the contract—a luxury automobile—is something the defendant “could simply have foregone” if he “did not like the terms of the agreement”).

“oppressive.” Such an innovation-chilling outcome is a far cry from traditional unconscionability law.

2. The Stieners’ Contracting Process Did Not Unduly “Surprise” Them Under California Law.

The district court also erred in concluding that, because the Stieners were not handed a copy of the terms of service at the time they purchased their iPhones, they were “surprised.” ER15–16. If that holding really were an accurate reflection of California law, it would condemn at the threshold the vast majority of retail sales, as well as many other types of transactions. As the Seventh Circuit has explained, “[p]ractical considerations support allowing vendors to enclose the full legal terms with their products” because the alternative—requiring cashiers “to read legal documents to customers before ringing up sales”—would be hopelessly inefficient. *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1149 (7th Cir. 1997); *see also Bischoff v. DirecTV, Inc.*, 180 F. Supp. 2d 1097, 1105 (C.D. Cal. 2002) (applying California law) (“the economic and practical considerations involved in selling services to mass consumers * * * make it acceptable for terms and conditions to follow the initial transaction”). Indeed, by activating their service through the iTunes program, the Stieners were able to read the terms of AT&T service online, presumably in their own home. And it is undisputed that the Stieners checked a box on their screen next to the statement: “I have read and agree to the AT&T Service Agreement.” ER82, 116. If they had disagreed with

the terms of ATTM service, they were under no compulsion to proceed with activating service.

Moreover, the Stieners were sent a booklet containing the service terms in hard-copy format and had ample opportunity to peruse the booklet, which highlighted the arbitration provision. *See* page 4, *supra*. They had 14 days to cancel service without having to pay an early-termination fee. *See* page 4, *supra*. As Judge Hamilton recently has explained, “providing a consumer with an opportunity to rescind an agreement greatly diminishes any aspect of procedural unconscionability” under California law. *Omstead v. Dell, Inc.*, 533 F. Supp. 2d 1012, 1036–37 (N.D. Cal. 2008).¹³

¹³ In addition to canceling their service without penalty, the Stieners could have returned the iPhones at that point for a 90 percent refund. ER88. The district court held that “consumers who decline to activate [their iPhones] to preserve their legal right to a jury trial” should not be required to pay a restocking fee. ER16 n.10. But the Stieners have never alleged that, if not for the prospect of having to pay a restocking fee, they would have rejected ATTM’s arbitration provision and returned the iPhones that they had wanted so badly as to buy on the very first day the phones became available. *See Engalla*, 983 P.2d at 915–16 (burden of proving facts underlying defense of unconscionability on proponent of unconscionability). The “hypothetical” possibility that some other customer might have been dissuaded is “irrelevant” to whether the Stieners (who made no such factual assertion) can void their agreement on unconscionability grounds. *West v. Henderson*, 278 Cal. Rptr. 570, 576 (Ct. App. 1991). Moreover, consumers routinely must pay the cost of shipping or restocking returned goods. *See, e.g.*, Amazon.com General Return Policy, <http://www.amazon.com/gp/help/customer/display.html?nodeId=15015711>; Best Buy Store Return Policy, <http://www.bestbuy.com/site/olspage.jsp?type=page&contentId=1117177044087&id=cat12098>; Circuit City, Returns and Exchanges, <http://www.circuitcity.com/rpsm/cat/-13414/edOid/105452/rpem/ccd/lookLearn.do>; Target, Online Return & Exchange Policy for Purchases & Gifts, [24](http://www.target.com/b/602-2734622-</p></div><div data-bbox=)

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In short, that ATTM’s arbitration provision is contained in a form contract implicates, at most, only a minimal quantum of procedural unconscionability. Accordingly, under California’s sliding-scale approach, the Stieners must “make a *strong showing* of substantive unconscionability to render [their] arbitration provision unenforceable.” *Gatton*, 61 Cal. Rptr. 3d at 356 (emphasis added). As we next explain, the Stieners failed to demonstrate that ATTM’s arbitration provision is substantively unconscionable at all, much less that it was severely so.

B. ATTM’s Arbitration Provision Is Not Substantively Unconscionable At All, Much Less Extremely So.

The district court held that the Stieners’ arbitration agreement is substantively unconscionable under California law because ATTM did not prove “that *all* iPhone consumers would recover more, on average, if the Court let the Arbitration Agreement stand rather than allowing the Stieners’ class action to proceed.” ER21 (emphasis in original). That holding is mistaken in several respects.

First, the court reversed the burden of proof. It is settled that the party *opposing* arbitration bears the burden of proving unconscionability. *Engalla*, 938 P.2d at 915–16.

7205415?ie=UTF8&node=10665391. Millions of contracts would be unsettled if that commonplace practice were condemned as procedurally unconscionable.

More fundamentally, the district court misunderstood this Court's interpretation of California law in *Shroyer*. What matters under that decision is whether the Stieners *themselves* have sufficient incentive to pursue claims in individual arbitration, not the fate of hypothetical third parties who are not before the court. If agreements to arbitrate on an individual basis are presumptively unconscionable unless a company proves that all of the members of a putative class would, on average, receive a greater payout in individual arbitration than each putative class member would be entitled to recover as a result of class-wide proceedings, that burden would be impossible to meet without extravagant speculation as to likely outcomes, and thus no class waiver could be enforceable—an outcome disavowed by the California Supreme Court. Moreover, even if the district court were correct in its assumption that the enforceability of the Stieners' arbitration agreement turns on the hypothetical outcomes for ATTM's other customers, the court's conclusion that the absent class members would be best served by invalidating ATTM's arbitration provision reflects a seriously flawed understanding of the empirics of class actions.

- 1. ATTM's Arbitration Provision Is Enforceable Under California Law, As Interpreted By This Court In *Shroyer*, Because The Stieners Have The Potential For Substantial Individual Gain In Arbitration.**

In *Discover Bank*, the California Supreme Court held that a credit-card issuer's arbitration provision—one that was far less favorable to consumers than

ATTM's current provision—was substantively unconscionable because its class waiver effectively “*insulate[d]*” *the company from liability* for the \$29 claims at issue in that case. 113 P.3d at 1109. The court explained that class actions can ““overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights”” by ““aggregating the relatively paltry recoveries into something worth someone’s (usually an attorney’s) labor.”” *Id.* at 1105–06 (quoting *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997)). But the court made clear that it was not holding “that *all* class action waivers are necessarily unconscionable.” *Id.* at 1110 (emphasis added). Rather, whether such a provision is substantively unconscionable turns on a case-by-case analysis of whether the plaintiff may feasibly vindicate “small” claims without using the class-action mechanism and, conversely, whether the class waiver threatens to insulate the company from liability for cheating its customers. *Id.*

In *Shroyer*, this Court held that ATTM's now-superseded arbitration provision was substantively unconscionable under *Discover Bank*. 498 F.3d at 986–87. As interpreted by this Court, the earlier arbitration provision specified that ATTM (then Cingular) would pay the full cost of arbitration and, in addition, would pay the plaintiff's attorneys' fees if the arbitrator awarded the plaintiff the amount of his or her demand or more. *Id.* at 986. The *Shroyer* Court held that those features were insufficient to render the class waiver enforceable under

Discover Bank because “when the potential for individual *gain* is small, very few plaintiffs, if any, will pursue individual arbitration or litigation * * *. [*Discover Bank*] did not suggest that a [class action] waiver is unconscionable only when or because a plaintiff in arbitration may experience a net loss (including attorneys’ fees and costs).” *Id.* (emphasis in original; citation omitted).

ATTM’s revised arbitration provision, which applies to the Stieners, resolves these concerns. As noted above, ATTM has built the necessary “individual gain” into its arbitration provision by providing that any California customer who obtains an arbitral award in excess of ATTM’s written settlement offer will receive at least **\$7,500**, while the customer’s counsel (if any) will receive **double** attorneys’ fees. *See* pages 7–8, *supra*. These amounts far exceed the level of damages that Congress and the California Legislature have deemed sufficient to encourage individuals and their counsel to pursue statutory claims.¹⁴ Even the prospect of recovering \$7,500 alone would be enough to make pursuing a claim

¹⁴ *See* ER171 (citing \$500 statutory damages provision in Telephone Consumer Protection Act and \$1,000 statutory damages provision in Cable Act); 15 U.S.C. § 1681n(a) (statutory damages of between \$100 and \$1,000 available under Fair Credit Reporting Act); Cal. Civ. Code § 54.3(a) (\$1,000 statutory damages under Disabled Persons Act). These legislative determinations of the amount needed to encourage vindication of statutory rights are entitled to great (if not dispositive) weight. *See Santisas v. Goodin*, 951 P.2d 399, 413 (Cal. 1998) (noting court’s “reluctan[ce] to declare contractual provisions void or unenforceable on public policy grounds without firm legislative guidance”); *People v. Mun. Ct.*, 574 P.2d 425, 427 (Cal. 1978) (the courts’ “common law powers * * * should never be exercised in such a manner as to * * * frustrate legitimate legislative policy”) (internal quotation marks omitted).

worthwhile for the Stieners, as real-world evidence confirms: Each year, Californians file hundreds of thousands of small claims court actions even though California law caps damages in such cases at \$7,500.¹⁵

The premiums available under ATTM's current arbitration provision also substantially exceed the typical incentive payments awarded to class representatives as part of court-approved class settlement agreements.¹⁶ Thus, the Stieners are on balance better off in individual arbitration than as putative class representatives in court. Not only does arbitration take much less time than judicial dispute resolution,¹⁷ but consumers and employees typically prevail more often in arbitration than in litigation. For example, the most recent statistics

¹⁵ See Cal. Code Civ. Proc. § 116.221; see also Judicial Council of California, *2007 Court Statistics Report: Statewide Caseload Trends 1996–1997 through 2005–2006* 46, available at <http://www.courtinfo.ca.gov/reference/documents/csr2007.pdf>.

¹⁶ See Theodore Eisenberg & Geoffrey P. Miller, *Incentive Awards to Class Action Plaintiffs: An Empirical Study*, 53 UCLA L. REV. 1303, 1333 & tbl. 5 (2006) (finding median incentive award for class representatives in consumer and consumer credit cases to be \$2,089 and \$1,045, respectively).

¹⁷ Consumer arbitrations administered by the AAA proceed to an award in an average of four to six months. See AAA, *Analysis of the American Arbitration Association's Consumer Arbitration Caseload*, available at <http://www.adr.org/si.asp?id=5027>. By contrast, federal civil cases average 23.2 months before reaching trial. See *United States District Court—Judicial Caseload Profile* (2007), available at <http://www.uscourts.gov/cgi-bin/cmsd2006.pl>. A study of state courts' dockets showed that contract suits averaged 25 months before a verdict was obtained. See Bureau of Justice Statistics, *Contract Trials and Verdicts in Large Counties, 2001*, at 2 (Jan. 2005), available at <http://www.ojp.usdoj.gov/bjs/pub/pdf/ctv1c01.pdf>. Of course, class actions take even longer to reach a final resolution.

compiled by the AAA show that consumers prevail in almost half (48 percent) of the approximately 40 percent of arbitrations that are not settled or withdrawn.¹⁸ AAA, *Analysis of the American Arbitration Association's Consumer Arbitration Caseload*, available at <http://www.adr.org/si.asp?id=5027>.¹⁹ By contrast, in court, virtually all consumer actions that are not settled or voluntarily withdrawn are dismissed on the pleadings or on summary judgment, with only 1.3 percent of federal civil cases ever even reaching trial, much less a verdict for the plaintiff.²⁰

Moreover, the effort required to pursue a claim is substantially lower in arbitration than in litigation. Customers like the Stieners are likely to obtain a successful resolution of their claims with little effort—perhaps only a few hours—simply by providing ATTM with notice of their dispute. That is because the terms of the arbitration provision create strong incentives for ATTM to resolve claims to its customers' satisfaction, so that it can avoid the risk of having to pay the

¹⁸ Presumably, a substantial number of settlements in consumer-initiated arbitrations benefit the consumer.

¹⁹ Data from the employment context reflect that employees enjoy a similar advantage in AAA arbitrations. See Nat'l Workrights Inst., *Employment Arbitration: What Does the Data Show?* (2004) (employees were almost 20 percent more likely to win employment cases in AAA arbitrations than in court), at http://www.workrights.org/current/cd_arbitration.html; see also Michael Delikat & Morris M. Kleiner, *An Empirical Study of Dispute Resolution Mechanisms: Where Do Plaintiffs Better Vindicate Their Rights?*, DISP. RESOL. J. 56, 56–68 (Nov. 2003–Jan. 2004) (plaintiffs who pursue employment arbitration in the securities industry were 12 percent more likely to win than employees litigating in the federal district court for the Southern District of New York).

²⁰ See Admin. Office of U.S. Courts, *2006 Judicial Facts and Figures* tab. 4.10, at <http://www.uscourts.gov/judicialfactsfigures/2006/Table410.pdf>.

premiums and the substantial costs of arbitration.²¹ And if the Stieners were dissatisfied with ATTM's settlement offer, ATTM's arbitration procedures reduce the burdens on them by allowing them to choose to arbitrate by telephone or even by mail. *See* page 9, *supra*. By contrast, if the Stieners are not held to their arbitration agreement, they will have to invest much more time to pursue their claim. Working with a lawyer, filling out affidavits, being deposed, and attending the class certification hearing will doubtless entail many days of missed work—and that lost time may stretch into weeks should the case actually proceed to trial.

In light of the opportunities for “individual gain” that are built into ATTM's arbitration provision and the ease of pursuing claims under its procedures, the concerns that caused the California Supreme Court and this Court to invalidate the class-arbitration prohibitions in *Discover Bank* and *Shroyer*, respectively, do not apply here. ATTM has not immunized itself from liability to the Stieners because its arbitration provision adequately substitutes for the class-action device by providing affirmative inducements for the Stieners to pursue their claims in arbitration and for a lawyer to represent them.

²¹ If a customer selects an in-person hearing, ATTM must pay at least \$1,700 in arbitration costs: \$750 in administrative fees, a \$200 case service fee, and \$750 in arbitrator fees. *See* ER158 (AAA, *Supplementary Procedures for Consumer-Related Disputes* § C-8).

2. The District Court Erred In Effectively Converting The Case-By-Case Analysis Required By *Shroyer* Into A Per Se Ban Of Individual-Arbitration Requirements.

The district court refused to consider the Stieners' ability to vindicate their own claims in individual arbitration. Instead, it reasoned that "the operative comparison * * * is between how the Arbitration Agreement and a class action might resolve a dispute between *all* iPhone consumers and AT&T." ER21 (emphasis added). From that vantage point, the court held that ATTM's arbitration provision is substantively unconscionable unless ATTM could show that individual arbitration "functions *as well as* a class action would" in providing recovery to absent class members. ER18 (emphasis added). The district court invalidated the arbitration provision under this newly minted standard because ATTM had "not presented any evidence that *all* iPhone consumers would recover more, on average, if the Court let the Arbitration Agreement stand rather than allowing the Stieners' class action to proceed." ER21 (emphasis in original).

The district court erred in focusing its analysis on ATTM's other customers rather than on the Stieners themselves, especially given the court's lack of any basis for assuming that the Stieners' claims are subject to class-wide treatment. Under California law, as elsewhere, a contractual term is unconscionable only if the party challenging that term can show that enforcing it under the specific circumstances of the case would shock the conscience, not simply that applying the term to other, imagined persons under other, "hypothetical situation[s]" might be

“unconscionable.” *West v. Henderson*, 278 Cal. Rptr. 570, 576 (Ct. App. 1991) (rejecting tenant’s argument that contractual six-month limitations period would unjustifiably limit the assertion of defenses to potential lawsuit by landlord as a “hypothetical observation” “irrelevant to this case”); *cf. Am. Software, Inc. v. Ali*, 54 Cal. Rptr. 2d 477, 480 (Ct. App. 1996) (rejecting employee’s procedural unconscionability attack on her employment agreement because employee was sophisticated and “had the benefit of counsel” before accepting the agreement); *accord, e.g., Cline v. H.E. Butt Grocery Co.*, 79 F. Supp. 2d 730, 733 (S.D. Tex. 1999) (arbitration agreement imposing some costs on plaintiff is not unconscionable because “[p]laintiff offers no information as to * * * **his** ability to pay for the costs of arbitration”) (emphasis added). The Stieners have never denied that, if **they** were to pursue arbitration, they would be likely to obtain full relief for themselves, or at least fare better than they would in litigation. ATTM’s arbitration provision therefore is not unconscionable as applied to them.

More importantly, the standard that the district court imposed is erroneous because it places the onus on ATTM to prove the unknowable. Even if a company could demonstrate that its customers **could** vindicate their claims in individual arbitration, no company could ever demonstrate that **all** of its customers would, on average, receive greater relief in arbitration than they would garner from a class action that has not yet been certified, much less proceeded to judgment. To satisfy that standard, ATTM would have to predict, for example, (i) whether the Stieners

would succeed in their efforts to certify a class; if so, (ii) whether the case would result in a judgment on the merits for plaintiffs, a dismissal on the merits for defendants, or a class settlement; (iii) what the value of any settlement or judgment would be; and (iv) what percentage, if any, of the absent class members would make the effort to seek benefits under a particular settlement or judgment. This task would thus require prejudging both the class certification issue and the merits—without the benefit of discovery and in contravention of the Supreme Court’s admonition that “Congress’ clear intent, in the Arbitration Act, [was] to move the parties to an arbitrable dispute out of court and into arbitration as quickly and easily as possible.” *Moses H. Cone*, 460 U.S. at 22.

In short, the standard that the district court erected is virtually impossible to meet. The problem is exacerbated by the district court’s decision to place the burden of proof on ATTM rather than the parties opposing arbitration—a holding that directly contravenes California law. *See Engalla*, 938 P.2d at 915–16. By creating this essentially insuperable standard, the district court effectively imposed a categorical ban on arbitration agreements that require individual resolution of disputes. Yet that is not what *Discover Bank* and *Shroyer* say. In *Discover Bank*, the California Supreme Court made clear that it was not holding “that all class action waivers are necessarily unconscionable.” 113 P.3d at 1110. And this Court in *Shroyer* confirmed that arbitration provisions with such waivers are “not necessarily in all cases” unconscionable under California law. 498 F.3d at 982.

The district court’s requirement that ATTM *prove* that all putative class members would fare better, on average, in individual arbitration than in class litigation accordingly cannot be squared with *Discover Bank* and *Shroyer*.

3. The District Court Misapplied Its Own Standard.

Even accepting the district court’s requirement that ATTM must prove that “*all* iPhone consumers would recover more, on average,” in individual arbitration than in a class action (ER21 (emphasis in original)), the district court’s conclusion that ATTM failed to carry this (unwarranted) burden is incorrect for two reasons.

First, the district court erred in concluding that “as a practical matter the Premium is illusory” precisely because the customer is too likely to get full relief. ER20. The court stated that, because ATTM predictably will offer any putative class member who invokes the arbitration process “a ‘settlement payment’ equal to his or her loss” so as to avoid the risk of paying the premiums (ER19), some customers will be *discouraged* from commencing arbitration (ER20). In essence, the district court treated the fact that ATTM’s arbitration provision creates strong incentives to respond to most dispute notices with a make-whole settlement offer (see pages 9–10, 30–31, *supra*) as a sign of *unfairness*. That concept of “unfairness”—that it is too easy for the consumer to obtain relief—bears no resemblance to traditional unconscionability doctrine.²²

²² See, e.g., *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 450 n.12 (D.C. Cir. 1965) (“The traditional test” for unconscionability “is ‘such as no man

Second—and more important—the district court failed to compare apples to apples. Although the court assessed the likelihood that customers would step forward and obtain relief in individual arbitrations with a skeptical eye, it uncritically assumed that the Stieners’ class action would be certified and would culminate in a money judgment or class settlement that provides all absent class members with meaningful relief.²³ But the reality of class action litigation falls far short of that rosy depiction.

To begin with, most class actions are not certified. A recent Federal Judicial Center study of class actions that terminated between July 1999 and 2002 found that federal and state courts granted motions for class certification only about 22 and 20 percent of the time, respectively—and that figure includes motions joined in by defendants in order to implement a class settlement. Thomas W. Willging & Shannon R. Wheatmann, *Attorney Choice of Forum in Class Action Litigation:*

in his senses and not under delusion would make on the one hand, and as no honest or fair man would accept on the other.”) (quoting *Greer v. Tweed*, 13 Abb. Pr. (N.S.) 427 (N.Y. Ct. C.P. 1872)) (quoting in turn 1 STORY, *supra*, § 244); *see also* *Herbert*, 71 P.2d at 257 (reflecting same view); *see generally* Susan Randall, *Judicial Attitudes Toward Arbitration and the Resurgence of Unconscionability*, 52 BUFF. L. REV. 185 (2004) (describing how the traditional test of unconscionability has been selectively applied in recent years to invalidate arbitration agreements at twice the rate of other contracts).

²³ *See generally* Harold Demsetz, *Information and Efficiency: Another Viewpoint*, 12 J.L. & ECON. 1, 1–4 (1969) (describing the “nirvana fallacy” of comparing an actual system to an idealized alternative).

What Difference Does It Make?, 81 NOTRE DAME L. REV. 591, 635 (2006). Stated another way, roughly four-fifths of class actions are not certified.

Moreover, those class actions that are certified almost always result in settlements (*see, e.g., id.* at 638), and when they do the class members rarely receive more than pennies on the dollar.²⁴ Unsurprisingly, studies of consumer class action settlements show that very few consumers bother to file a claim when the amount that they would receive is small—as it inevitably would be if this case were certified as a class action and then settled.²⁵ Indeed, in several recent cases, far fewer than one percent of the absent class members submitted claims.²⁶ This

²⁴ *See, e.g.,* John Bronsteen, *Class Action Settlements: An Opt-In Proposal*, 2005 U. ILL. L. REV. 903, 911; Jill E. Fisch, *Class Action Reform, Qui Tam, and the Role of the Plaintiff*, 60 L. & CONTEMP. PROBS. 167, 168 (1997); Susan P. Koniak & George M. Cohen, *Under Cloak of Settlement*, 82 VA. L. REV. 1051, 1053–89 (1996).

²⁵ *See, e.g.,* James Tharin & Brian Blockovich, *Coupons and the Class Action Fairness Act*, 18 GEO. J. LEGAL ETHICS 1443, 1445–46 (2005) (noting that the redemption rate of class action coupons ranges from one to three percent); Christopher R. Leslie, *A Market-Based Approach to Coupon Settlements in Antitrust and Consumer Class Action Litigation*, 49 UCLA L. REV. 991, 1035 (2002) (reporting a study of ten consumer class action settlements in which the redemption rates varied from 3 to 13.1 percent); Gail Hillebrand & Daniel Torrence, *Claims Procedures in Large Consumer Class Actions and Equitable Distribution of Benefits*, 28 SANTA CLARA L. REV. 747, 753 (1988) (discussing three settlements in which the claims rates were 3, 10.5, and 18 percent);

²⁶ *See, e.g., Palamara v. Kings Family Rests.*, 2008 WL 1818453, at *2 (W.D. Pa. Apr. 22, 2008) (“approximately 165 class members” out of 291,000 “had obtained a voucher” under the settlement, yielding a take rate of under 0.06 percent); *Yeagley v. Wells Fargo & Co.*, 2008 WL 171083, at *2 (N.D. Cal. Jan. 18, 2008) (“less than one percent of the class chose to participate in the settlement”); *Moody v. Sears, Roebuck & Co.*, 2007 WL 2582193, at *5 (N.C.

phenomenon caused Congress to find that “[c]lass members often receive little or no benefit from class actions, and are sometimes harmed.” Class Action Fairness Act of 2005, PUB. L. NO. 109-2, 119 Stat. 4, § 2(a)(3).

As Congress’s findings illustrate, these features of the modern consumer class action are widely recognized. But the district court did not take them into account in drawing what it termed the “operative comparison * * * between how the Arbitration Agreement and a class action might resolve a dispute between all iPhone customers and AT&T.” ER21. Accordingly, even if the district court’s new standard were a valid interpretation of California unconscionability law, its application of that standard is plainly erroneous.

* * * * *

In short, ATTM’s current arbitration provision resolves the concerns identified with earlier provisions in *Discover Bank* and *Shroyer* by providing affirmative inducements to customers and their attorneys to pursue individual claims. Because of those inducements and the “simplicity, informality, and expedition” (*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985)) of ATTM’s arbitration procedures, the Stieners would be better off in arbitration than as class representatives. Accordingly, ATTM’s arbitration

Super. Ct. May 7, 2007) (“only 337 valid claims were filed out of a possible class of 1,500,000,” yielding a take rate of just over 0.02 percent), *rev’d*, 2008 WL 2726628 (N.C. Ct. App. July 15, 2008); *see also, e.g., Synfuel Techs., Inc. v. DHL Express (USA), Inc.*, 463 F.3d 646, 649–50 (7th Cir. 2006) (noting that only a “paltry three percent” of class members had filed claims under the settlement).

provision does not operate to insulate it from liability to the Stieners. Nor does the provision operate to insulate ATTM from the claims of any other customer. To the contrary, the combination of making arbitration cost-free and including unprecedented premiums in the provision ensures that ATTM has a powerful incentive to resolve a dispute to the customer's satisfaction whenever a customer goes to the minimal effort of making a complaint. And the fact that ATTM's provision does not require the results of arbitrations to be kept confidential means that individual consumers (and their lawyers) who pursue arbitration are free to publicize the results to other ATTM customers, who may then use them as precedent in future arbitrations. By contrast, few of ATTM's customers can be expected to obtain relief in a class action. Accordingly, ATTM's arbitration provision is not substantively unconscionable at all. At minimum, taking into account the (at most) modest level of procedural unconscionability, this unprecedentedly pro-consumer arbitration provision does not rise sufficiently high on the spectrum of substantive unconscionability to warrant refusing to enforce it.

II. THE FAA PREEMPTS THE DISTRICT COURT'S HOLDING THAT ATTM'S ARBITRATION PROVISION IS UNENFORCEABLE UNDER CALIFORNIA LAW.

For the reasons we have just explained, the district court erred in holding that ATTM's arbitration provision is unconscionable under California law despite the opportunities for "individual gain" that ATTM built into the provision. But even if the district court's holding were correct as a matter of California law, the

FAA preempts that interpretation of California law, both expressly and impliedly under the doctrine of conflict preemption.

A. The FAA Expressly Preempts The Novel Variation Of Unconscionability Doctrine That The District Court Applied.

Section 2 of the FAA specifies that arbitration provisions “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of *any* contract.” 9 U.S.C. § 2 (emphasis added). As the Supreme Court has recently reiterated, Section 2 forbids states from “impos[ing] prerequisites to enforcement of an arbitration agreement that are not applicable to contracts generally.” *Preston*, 128 S. Ct. at 985. Accordingly, a court may not “rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable.” *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987); *see also Iberia*, 379 F.3d at 167 (Section 2 preempts even “general principle[s] of contract law, such as unconscionability” if “those general doctrines” are “employ[ed] * * * in ways that subject arbitration clauses to special scrutiny”). As this Court itself has recognized, this principle means that a law that applies only to “a limited set of transactions * * * is not a law of ‘general applicability’” and therefore is preempted by Section 2. *Ting*, 319 F.3d at 1148. That is precisely the situation here, given the district court’s holding that the class-arbitration prohibition in ATTM’s arbitration provision is unconscionable under

California law even though it provides ample opportunities for “individual gain” (*Shroyer*, 498 F.3d at 986 (emphasis omitted)).

As discussed above, under California’s generally applicable unconscionability principles, a contractual term is substantively unconscionable only if it so “shock[s] the conscience” (*Belton*, 60 Cal. Rptr. 3d at 650) that a person would have to be “under delusion” (*Herbert*, 71 P.2d at 257) to agree to it. We recognize that, in *Shroyer*, this Court held that “[t]he rule announced in *Discover Bank* is simply a refinement of the unconscionability analysis applicable to contracts generally in California.” 498 F.3d at 987. We respectfully disagree with that holding. But even if both *Discover Bank* and this Court’s decision in *Shroyer*—which struck down an earlier version of ATTM’s arbitration provision—entailed mere “refinement[s]” of California’s generally applicable “shock the conscience” standard, the same could not be said of the district court’s holding that ATTM’s *new* arbitration provision, with its unprecedented opportunities for “individual gain,” is unconscionable.

The trade-off that ATTM’s customers make in accepting ATTM’s revised arbitration provision is hardly an unreasonable one, much less “delusional” or conscience-shocking. First, in the absence of arbitration—and in particular, without the affirmative inducements to pursue individual claims that are contained in ATTM’s provision—ATTM’s customers would be left without any realistic means to pursue the vast majority of their disputes, which are individualized and

not susceptible to class-wide adjudication. As the Supreme Court has observed, without enforceable arbitration agreements, “the typical consumer who has only a small damages claim (who seeks, say, the value of only a defective refrigerator or television set)” would be left “without any remedy but a court remedy, the costs and delays of which could eat up the value of an eventual small recovery.” *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 281 (1995). As we explain below (at pages 49–51), neither ATTM nor any other rational business would provide subsidized individual arbitration to its customers if class arbitration must also be made available.

Second, all of ATTM’s customers, including the millions who never have a dispute of any kind, benefit from ATTM’s arbitration provision in the form of lower prices for wireless services. As the Seventh Circuit has explained, “arbitration offers cost-saving benefits * * * and these benefits are reflected in a lower cost of doing business that in competition [is] passed along to customers.” *Boomer v. AT&T Corp.*, 309 F.3d 404, 419 (7th Cir. 2002) (internal quotation marks omitted); *see also* Stephen J. Ware, *The Case for Enforcing Adhesive Arbitration Agreements—With Particular Consideration of Class Actions and Arbitration Fees*, 5 J. AM. ARB. 251, 254–56 (2006) (arbitration “lower[s] [businesses’] dispute-resolution costs,” and this “benefit to businesses is also a benefit to consumers” because “whatever lowers costs to businesses tends over

time to lower prices to consumers”). If ATTM’s arbitration provision is not enforced, those cost savings will be lost.

Accordingly, the district court’s holding that ATTM’s exceptionally pro-consumer arbitration provision is unconscionable distorts what it means to “shock the conscience”—affording courts an open-ended means for striking down virtually any contractual provision that they think (in hindsight) has turned out to be unfair to one of the contracting parties (or, in this case, some other unidentified customers). That is manifestly not California law—at least not with respect to any contractual provisions other than ones agreeing to resolve disputes on an individual basis. As the California Court of Appeal has put it, “with a concept as nebulous as ‘unconscionability,’ it is important that courts not be thrust in the paternalistic role of intervening to change contractual terms that the parties have agreed to merely because the court believes the terms are unreasonable.” *Koehl v. Verio, Inc.*, 48 Cal. Rptr. 3d 749, 769 (Ct. App. 2006) (internal quotation marks omitted) (quoting *Ali*, 54 Cal. Rptr. 2d at 480).

In short, to deem ATTM’s current arbitration provision substantively unconscionable merely because it incorporates a traditional characteristic of arbitration—the lack of class relief—is to condemn the provision on the impermissible ground that traditional, individual arbitration is a second-class form of adjudication. *See Carbajal v. H & R Block Tax Servs., Inc.*, 372 F.3d 903, 906 (7th Cir. 2004) (“The cry of ‘unconscionable!’ just repackages the tired assertion

that arbitration should be disparaged as second-class adjudication. It is precisely to still such cries that the Federal Arbitration Act equates arbitration with other contractual terms.”). Because the district court engaged in far more than a mere “refinement” of California’s “shock the conscience” standard in invalidating ATTM’s path-breaking arbitration provision, *Shroyer*’s holding that California law is compatible with Section 2 of the FAA does not control the application of FAA preemption to *this* case.

B. By Precluding The Enforcement Of Agreements To Arbitrate Disputes Individually, The District Court’s Holding Conflicts With The Objective Of The FAA And Is Preempted On That Ground As Well.

In addition, the district court’s interpretation of California law as precluding ATTM from requiring individual arbitration, notwithstanding ATTM’s efforts to make individual arbitration a realistic alternative for its customers, “stands as an obstacle to the accomplishment and execution of the full purposes and objective of Congress” in enacting the FAA, and thus is preempted under the doctrine of conflict preemption. *United States v. Locke*, 529 U.S. 89, 109 (2000) (internal quotation marks omitted). When federal law encourages private parties to engage in or refrain from a certain activity, as the FAA does in “declar[ing] * * * a liberal federal policy favoring arbitration agreements” (*Moses H. Cone*, 460 U.S. at 24), state laws producing contrary incentives must yield.²⁷

²⁷ See, e.g., *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 157, (1989) (state-law protection of unpatentable inventions was preempted because it

We recognize that this Court rejected a similar argument in *Shroyer*, concluding that Congress did not intend the FAA to “encourage individual arbitration and disfavor class arbitration.” 498 F.3d at 990. But *Preston* supersedes *Shroyer*’s reasoning on this point—reasoning that would equally exclude from preemption a state requirement that all arbitrations fully conform to the rules of civil procedure. *Preston* makes clear that even a state-law rule that applies equally to arbitration and litigation is preempted if it conflicts with a “prime objective” of the FAA.²⁸

In *Preston*, the Supreme Court held that the FAA preempted a provision of California’s Talent Agencies Act “grant[ing] the Labor Commissioner exclusive jurisdiction to decide an issue that the parties agreed to arbitrate”—in that case, whether a person is a “talent agent” for purposes of the Act. 128 S. Ct. at 982, 984–85. In an effort to salvage the California statute, the respondent contended

“could essentially redirect inventive efforts away from the careful criteria of patentability developed by Congress over the last 200 years”); *Edgar v. MITE Corp.*, 457 U.S. 624, 635 (1982) (holding that federal securities laws preempt state tender offer regulation, which gave “incumbent management * * * a powerful tool to combat tender offers,” because “[t]hese consequences are precisely what Congress determined should be avoided”); *see also New York State Conf. of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 668 (1995) (ERISA, which has the purpose of promoting regulated plans’ flexibility in providing coverage, would preempt a state law that “produce[s] such acute, albeit indirect, economic effects, by intent or otherwise, as to force an ERISA plan to adopt a certain scheme of substantive coverage”).

²⁸ This Court is bound to follow *Preston* rather than *Shroyer*, as a court of appeals decision is abrogated whenever a Supreme Court decision “undercut[s] the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable,” even if “the issues” in the two cases are not “identical.” *Miller v. Gammie*, 335 F.3d 889, 900 (9th Cir. 2003).

that the Talent Agencies Act was “compatible with the FAA because” it was no more than an exhaustion requirement—*i.e.*, it “merely postpones arbitration until after the Labor Commissioner has exercised her primary jurisdiction.” *Id.* at 985. Because the statute allowed for a *de novo* appeal of the Labor Commissioner’s decision to California superior court, the respondent contended that “either party could move to compel arbitration” following the Commissioner’s determination (*id.*). Accordingly, the respondent argued that the delay imposed by “[r]equiring initial reference of the parties’ dispute to the Labor Commissioner” (*id.* at 986) would apply equally to litigation *and* arbitration, and that such equal treatment was consistent with the FAA.

The Supreme Court disagreed. It explained that “[a] prime objective of an agreement to arbitrate is to achieve ‘streamlined proceedings and expeditious results.’” *Id.* at 986 (quoting *Mitsubishi*, 473 U.S. at 633). It then reasoned that this objective “would be frustrated” by the California Talent Agencies Act because “[r]equiring initial reference of the parties’ dispute to the Labor Commissioner would, at the least, hinder speedy resolution of the controversy.” *Id.*

Similar reasoning applies here. There can be no doubt that engrafting class proceedings onto arbitration would “hinder speedy resolution of the controversy” (*id.*) between plaintiffs and ATTM: Superimposing class-action procedures on arbitration “brings the burdens of litigation into the arbitral forum” and “lessens the distinction between the two processes.” Jonathan R. Bunch, Note, *To Be*

Announced: Silence from the United States Supreme Court and Disagreement Among Lower Courts Suggest an Uncertain Future for Class-Wide Arbitration, 2004 J. DISP. RESOL. 259, 272. Indeed, resolving a case like this one as a class arbitration would take years.

Class actions invariably begin with a lengthy collateral proceeding to determine the propriety of class certification, which generally entails (i) substantial discovery, including depositions of all class representatives (and often other witnesses) for purposes of determining such statutory prerequisites as typicality and adequacy of the class representatives and commonality of the claims across class members; (ii) plenary briefing of the class certification issue; (iii) an evidentiary hearing; (iv) a written ruling; and (v) the interlocutory appeal that inevitably follows.

If, after all of that, a class is certified, there would have to be full and adequate notice to class members and an opportunity to opt out. Discovery commensurate with the now-increased stakes of the litigation would then begin and likely continue for years. Should the defendant then yield to the hydraulic pressure to settle that class certification creates, due process would necessitate another round of notice followed by a fairness hearing, complete with extensive briefing by both sides and by any objectors. And if the defendant chooses not to settle, there would need to be a class-wide trial—one in which the plaintiffs are required to

establish any individualized elements of their claims and the defendant is afforded the opportunity to put on any individualized defenses.

All of the procedures necessary to the fair administration of a class action make class arbitration more expensive and time-consuming—and, in the process, eradicate the distinction between arbitration and litigation. The procedures for class arbitrations promulgated by the AAA bear out the distinctly non-arbitral character of class arbitration. Those rules first require the arbitrator to make a written “class determination award,” addressing a long list of criteria equivalent to those identified in Federal Rule of Civil Procedure 23. The AAA rules then call for a proceeding in court to confirm or vacate that interim award. In the next step, the arbitrator presides over the notification of class members. And the rules ultimately anticipate a full-blown proceeding on the merits and a carefully reasoned “final award” once the class determination award becomes final and class members have been given notice and an opportunity to opt out. *See generally* AAA, *American Arbitration Association Policy on Class Arbitrations*, at <http://www.adr.org/Classarbitrationpolicy>. In short, this process is every bit as burdensome as a judicial class action and precludes “effectively ‘streamlined proceedings and expeditious results’” (*Preston*, 128 S. Ct. at 986 (quoting

Mitsubishi, 473 U.S. at 633) at least as much as the initial-reference requirement invalidated in *Preston*.²⁹

Moreover, conditioning the enforceability of arbitration agreements on the availability of class arbitration would do more than “hinder” arbitration’s “speedy resolution” (*Preston*, 128 S. Ct. at 986): Such a requirement would force companies to abandon arbitration altogether. When a business decides whether to include an arbitration provision in its agreements with its customers, it must consider the advantages and disadvantages of doing so. The advantages of arbitration are that it “saves time, saves trouble, saves money.” *Joint Hearings on S. 1005 and H.R. 646 Before the Subcomms. of the Comms. on the Judiciary*, 68th Cong., 1st Sess. 7 (1924) (statement of Charles Bernheimer, N.Y. Chamber of Commerce); *see also Allied-Bruce*, 513 U.S. at 280 (arbitration’s “advantages often would seem helpful to individuals, say, complaining about a product, who need a less expensive alternative to litigation”). The risk is that the arbitrator will

²⁹ Of course, parties may *agree* to arbitrate under such cumbersome and self-defeating procedures without running afoul of the FAA. *See Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 451 (2003) (remanding for arbitrator to decide whether an arbitration provision that was not “completely obvious” on the point implicitly authorized class-wide arbitration); *Shroyer*, 498 F.3d at 992. “[T]he FAA lets *parties* tailor some, even many features of arbitration by contract * * * .” *Hall Street Assocs., Inc. v. Mattel, Inc.*, 128 S. Ct. 1396, 1404 (2008) (emphasis added). Under *Preston*, however, neither courts nor state legislatures may impose procedural requirements that impede the swift and efficient use of arbitration when the parties’ agreement precludes those very impediments in language that *is* as “completely obvious” (*Bazzle*, 539 U.S. at 451) as the individual arbitration requirement here.

render an erroneous—yet unreviewable—decision. As the Tenth Circuit has observed, the standard for vacating an arbitral award is “among the narrowest known to law.” *Dominion Video Satellite, Inc. v. Echostar Satellite L.L.C.*, 430 F.3d 1269, 1275 (10th Cir. 2005) (internal quotation marks omitted). Such awards may be vacated only for fraud, bias, or “manifest disregard” of the law. *See* 9 U.S.C. § 10; *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396, 1404 (2008). Many businesses are willing to take that risk in an individual arbitration because of the cost savings and their desire for a less adversarial method of resolving disputes with customers.

The calculus changes dramatically, however, if the arbitration provision must allow for class-wide arbitration. As noted above, in a class arbitration the efficiencies of individual arbitration are lost. More importantly, the stakes of a class arbitration are exponentially higher than those of an individual arbitration. No business could afford to subject itself to the risk that an arbitrator subject to only very limited judicial review would render a massive class award. As one Supreme Court Justice has put it, “[y]ou might not want to put your company’s entire future in the hands of one arbitrator.” Tr. of Oral Argument, *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003) (No. 02-634), 2003 WL 1989562, at *29.

In short, the inevitable consequence is that businesses will stop including arbitration provisions in their contracts with their customers and employees—two

categories that each represent a large proportion of all contracts. Nothing could more clearly “frustrate the purpose” (*Livadas v. Bradshaw*, 512 U.S. 107, 116 (1994)) of the FAA to “achieve ‘streamlined procedures and expeditious results.’” *Preston*, 128 S. Ct. at 986 (quoting *Mitsubishi*, 473 U.S. at 633). Accordingly, under *Preston*, any state-law rule requiring the availability of class arbitration is preempted by the FAA. *See also Gay v. CreditInform*, 511 F.3d 369, 395 (3d Cir. 2007) (Pennsylvania rule that arbitration provisions that prohibit class arbitration are unconscionable “interfere[s] with the appropriate application of the FAA”); *accord Schultz v. AT&T Wireless Servs., Inc.*, 376 F. Supp. 2d 685, 691 (N.D. W. Va. 2005); *Blitz*, slip. op. at 6; *Pyburn v. Bill Heard Chevrolet*, 63 S.W.3d 351, 365 (Tenn. Ct. App. 2001).³⁰

³⁰ The *Shroyer* Court rejected this argument because, in its view, ATTM was required to show affirmatively that businesses were already abandoning arbitration. 498 F.3d at 993. That understanding of conflict-preemption doctrine is mistaken. Such a rule would all but preclude parties from challenging state laws before the damage is done. No doubt for that reason, the Supreme Court has never required proof of the actual adverse effects of a state statute. Rather, it has itself relied on commonsense assumptions. For example, in *Bonito Boats* it found conflict preemption where state law “could pose a substantial threat to the patent system’s ability to accomplish its mission of promoting progress in the useful arts” and refused to dismiss the conflict as a “hypothetical * * * possibility.” 489 U.S. at 161. In any event, at least one major company—Comcast—has abandoned arbitration in its contracts with its millions of California customers. *See* <http://www.comcast.net/terms/subscriber/>.

CONCLUSION

The district court's order denying the motion to compel arbitration should be reversed.

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August 4, 2008

CERTIFICATE OF COMPLIANCE PURSUANT TO FED. R. APP. P. 32(A)(7)(C) AND CIRCUIT RULE 32-1 FOR CASE NUMBER 08-15612

I certify that:

X 1. Pursuant to Fed. R. App. P. 32 (a)(7)(C) and Ninth Circuit Rule 32-1, the attached opening/answering/reply/cross-appeal brief is

Proportionately spaced, has a typeface of 14 points or more and contains 13,204 words (opening, answering, and the second and third briefs filed in cross-appeals must not exceed 14,000 words; reply briefs must not exceed 7,000 words),

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Monospaced, has 10.5 or fewer characters per inch and contains _____ words or _____ lines of text (opening, answering, and the second and third briefs filed in cross-appeals must not exceed 14,000 words or 1,300 lines of text; reply briefs must not exceed 7,000 words or 650 lines of text).

 2. The attached brief is **not** subject to the type-volume limitations of Fed. R. App. P. 32(a)(7)(B) because

This brief complies with Fed. R. App. P. 32(a)(1)-(7) and is a principal brief of no more than 30 pages or a reply brief of no more than 15 pages;

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- Pursuant to Fed. R. App. P. 29(d) and 9th Cir. R. 32-1, the attached amicus brief is proportionally spaced, has a typeface of 14 points or more and contains 7000 words or less,

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DATED: August 4, 2008

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Evan M. Tager

STATEMENT OF RELATED CASES

Counsel for ATTM is aware of one related case pending in this Court: *Kaltwasser v. Cingular Wireless LLC*, No. 08-15962. *Kaltwasser* is an appeal from the denial of ATTM's motion to compel arbitration under the same arbitration provision involved in this case, and therefore raises closely related issues.

Addendum 1

CERTIFICATE OF FILING AND SERVICE

I hereby certify that on this 4th day of August 2008, I caused the original and 15 copies of the foregoing brief and 5 copies of the Excerpts of Record to be deposited with a third-party commercial carrier for overnight delivery to the Clerk of the Court, and I served copies of the foregoing brief and one copy of the Excerpts of Record by third-party commercial carrier for overnight delivery on the parties herein, at each of the following addresses:

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Addendum 2