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LEGAL ALERT

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Supreme Court: If Clearly Delegated the Task, Arbitrator Decides When Arbitration Agreement is Unconscionable

The Supreme Court handed proponents of arbitration another victory today in *Rent-A-Center, West, Inc. v. Jackson*, a case involving an unconscionability challenge to an arbitration agreement. The Court held, in a 5-4 opinion authored by Justice Scalia, that the unconscionability challenge was for the arbitrator to decide. The Court's opinion sets the rules for determining, in future cases, the question of who decides such challenges.

At issue in *Rent-A-Center* was a contention by an employee resisting arbitration of a discrimination claim that the arbitration agreement he signed was unconscionable, and thus invalid. The Court held that, where the parties have clearly agreed to delegate enforceability questions (including unconscionability questions) to the arbitrator, an unconscionability challenge should be decided by the arbitrator—unless the challenge specifically targets the *delegation* itself as unconscionable. The Court's decision appears to resolve the conflict between the Ninth Circuit, which held that basic questions of enforceability must be decided by a court,[1] and the Eighth and Eleventh Circuits, which have held that a determination of enforceability may be delegated to the arbitrator.[2] The Court's ruling makes it more difficult for parties resisting arbitration to have their unconscionability arguments decided by the court, rather than by the arbitrator.

The underlying litigation arose from an arbitration agreement that Antonio Jackson signed in conjunction with his employment by Rent-A-Center, West in Nevada in 2004. The agreement required any dispute between Jackson and Rent-A-Center to be submitted to arbitration and exclusively delegated to the arbitrator the right to resolve any claim that all or part of the agreement was void or voidable. In 2007, Jackson was terminated, and he filed an action in federal district court against Rent-A-Center, alleging that he was the victim of racial discrimination and also that the arbitration agreement was unconscionable. The district court granted Rent-A-Center's motion to dismiss and to compel arbitration under Section 4 of the Federal Arbitration Act (FAA), 9 U.S.C.S. § 1 *et seq.*, which provides that courts must give full effect to valid arbitration agreements. The court held that because the agreement "clearly and unmistakably provides the arbitrator with the exclusive authority to decide whether the agreement to arbitrate is enforceable," the question of unconscionability must be decided by the arbitrator.[3] On appeal, the Ninth Circuit reversed, holding that an unconscionability challenge was a question of whether an

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[1] *Jackson v. Rent-a-Center, West, Inc*, 581 F.3d 912 (9th Cir. 2009).

[2] *See Terminix Int'l Co., LP v. Palmer Ranch Ltd. P'ship*, 432 F.3d 1327, 1333 (11th Cir. 2005)(holding that while the validity of an arbitration clause was "by default an issue for the court" the parties could "contract[] around that default rule" and allow the arbitrator to decide this); *Sadler v. Green Tree Servicing, LLC,* 466 F.3d 623 (8th Cir. 2006)(holding that the arbitrability of issues and enforceability of an arbitration agreement should be determined by an arbitrator where the parties have so agreed). *See also Anwuah v.Coverall North America, Inc.*, 554 F.3d 7, 11-13 (1st Cir. 2009)(holding that the court could determine the gateway question of whether the agreement prevented the litigant from having access to arbitration, but explicitly not reserving unconscionability—"essentially a fairness issue"—for judicial decision.)

[3] *Jackson v. Rent-A-Center, West, Inc.*, 2007 U.S. Dist. LEXIS 99067 (D. Nev. June 6, 2007).

agreement to arbitrate was valid in the first place. As a threshold question of whether a party was even required to submit to arbitration, validity of the agreement was a determination for the court.[4]

Rent-A-Center's petition for certiorari to the Supreme Court noted the conflict between the circuits and argued that the Ninth Circuit's holding was contradictory to the Supreme Court's decisions in *AT&T Technologies v. Communication Workers of America*[5] and *First Options of Chicago v. Kaplan*,[6] two cases addressing the limits of the FAA's broad arbitration agreement enforcement provisions. Section 2 of the FAA provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Section 4 provides that where an arbitration agreement is challenged in court, "upon being satisfied that the making of the agreement for arbitration . . . is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement." In *AT&T*, the Court held that arbitrability, or "whether a[n] . . . agreement creates a duty for the parties to arbitrate the particular grievance" is a question for a court, unless the parties "clearly and unmistakably provide otherwise," in which case, the arbitrator may determine arbitrability.[7] In *First Options*, the Court held that "a court must defer to an arbitrator's arbitrability decision when the parties submitted that matter to arbitration," but whether the parties had agreed to do so was a question for the court, absent "clear and unmistakable language."[8]

In its merits brief, Rent-A-Center argued that there was no challenge to the making of the arbitration agreement; thus, Section 4 of the FAA required the court to order arbitration in the manner of the agreement. Because the agreement "clearly and unmistakably" delegated to the arbitrator exclusive ability to rule on validity, the Court's decisions in *AT&T* and *First Options* required that the arbitrator address the unconscionability challenge. Jackson argued that under Section 2 of the FAA, courts should decide enforceability—a possible ground for revocation—as a gateway issue. Jackson distinguished between challenges to the scope of an arbitration agreement, which could be delegated to arbitrators under *AT&T* and *First Options*, and challenges to the enforceability of the agreement, which could not.

Justice Scalia's opinion, joined by Justices Alito, Kennedy, Thomas, and Chief Justice Roberts, began with a discussion of contract principles applied to arbitration agreements, noting that the FAA "places arbitration agreements on an equal footing with other contracts," and that Section 2 subjects arbitration agreements to general contract defenses. (Slip op. at 3-4). The Court also noted that its decisions in *First Options* and *AT&T* allowed the parties to delegate "gateway" questions of arbitrability under the FAA to the arbitrator. However, rather than engaging in extended analysis of where to draw the line between permissible and impermissible "gateway" delegations, as the parties had in briefing and oral argument, the Court held that "an agreement to arbitrate a gateway issue is simply an additional, antecedent agreement the party seeking arbitration asks the federal court to enforce, and the FAA operates on this additional arbitration agreement just as it does any other." (Slip Op. at 6). Thus, the Court analyzed the delegation provision as an arbitration agreement in itself.

Addressing whether the delegation provision was valid under Section 2, the majority relied on precedents addressing challenges to contracts with arbitration provisions, which distinguish between challenges to

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[4] *Jackson*, 581 F.3d at 915-919.

[5] 475 U.S. 643, 649 (1986).

[6] 514 U.S. 938 (1995).

[7] 475 U.S. at 649.

[8] 514 U.S. at 943-45.

"the validity of the agreement" to arbitrate and challenges "to the contract as a whole." (Slip. Op. at 6 (*quoting Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 444 (2006)(holding that a challenge to validity of a service contract as a whole, not to the arbitration clause within it, must go to the arbitrator))). In the leading case, *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, the Court held that a challenge to an arbitration agreement that is included in another agreement, such as an employment contract, must target the arbitration provision itself, rather than the contract as a whole. If it does not, then the challenge to enforceability of the entire agreement is to be decided by the arbitrator.[9] The Court had applied the *Prima Paint* rule most recently in *Buckeye Check Cashing*.[10]

The Court's opinion in *Rent-A-Center* takes *Prima Paint* to another level. *Rent-A-Center* involved a stand-alone arbitration agreement, rather than an arbitration provision within another contract. On the surface, it might have appeared that *Prima Paint* would not apply. But the Court held that "it makes no difference" whether an arbitration agreement within a contract is at issue or whether the arbitration agreement is itself the contract at issue. (Slip. Op. at 8.) Because Jackson did not raise a specific challenge to the arbitration agreement's concededly clear *delegation* of questions concerning validity of the arbitration agreement to the arbitrator, his unconscionability attack on the arbitration provision must be decided by the arbitrator. The Court pointed out possible grounds for attacking the delegation provision itself as unconscionable—for example, by citing the agreement's limitations on discovery as hindering litigation of the question—but concluded that Jackson had not done so. Justice Stevens's dissent noted that neither party had argued for the rule adopted by the majority.

Rent-A-Center is the second victory this term for arbitration proponents. In *Stolt-Nielson S.A. et. al. v. AnimalFeeds International Corp.*,[11] in holding that arbitrators may not impose class arbitration on parties who have not agreed to class arbitration, the court enunciated a "high hurdle" for vacating a panel's decision under Section 10(a)(4) of the FAA—"[i]t is only when an arbitrator strays from interpretation and application of the agreement and effectively dispenses his own brand of industrial justice that his decision may be unenforceable."[12] Next term may include another important decision, as the Court has granted certiorari to decide *AT&T Mobility v. Concepcion*, a case considering whether states can condition enforcement of an arbitration agreement on the availability of class-wide arbitration under the FAA. *Rent-A-Center* also seems likely to roil the politics of arbitration in connection with legislation pending before Congress.

Please contact us if you would like a copy of the opinion.

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[9] *Id.*

[10] 546 U.S. at 444.

[11] 559 U.S.L.W. 4328 (U.S. April 27, 2010).

[12] *Id.*

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If you have questions regarding this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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