

United States Supreme Court Says Courts Cannot Compel Classwide Arbitration Absent Affirmative Contractual Agreement

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In a 5-4 decision authored by Chief Justice Roberts on April 24, 2019, the United States Supreme Court held that the Federal Arbitration Act (“FAA”) precludes a court from compelling class arbitration when an agreement is ambiguous on the availability of such arbitration. *Lamps Plus Inc. et al. v. Varela*, No. 17-988, 587 U.S. ___ (2019). In doing so, the Court reversed a decision by the United States Court of Appeals for the Ninth Circuit that applied California law to construe an ambiguity against the drafter (Lamps Plus) and permit class arbitration. The Court held that the FAA requires an affirmative contractual basis to compel class arbitration, which was indisputably absent here, and that a state law contract principle could not be applied to the extent it was inconsistent with FAA principles.

Relevant Background

A Lamps Plus employee, Frank Varela, filed a putative class action, on behalf of himself and other “similarly situated” employees whose tax information had allegedly been compromised by Lamps Plus, in federal court. Because Varela’s employment agreement contained an arbitration provision with no mention of class proceedings, Lamps Plus sought to compel arbitration on an individual basis. The district court, however, compelled classwide arbitration. Lamps Plus appealed that decision, but the Ninth Circuit affirmed (in a 2-1 decision), relying on state contract principles to hold that an ambiguity in the parties’ arbitration agreement as to class arbitration should be construed against the drafter (here, Lamps Plus). Lamps Plus then filed a petition for a writ of certiorari with the United States Supreme Court.

The Supreme Court’s Decision

The Supreme Court agreed with Lamps Plus and held that a court may not compel classwide arbitration when an agreement is ambiguous on its availability. The Court reiterated its reasoning in *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010), that the FAA bars courts from inferring “consent to participate in class arbitration absent an affirmative contractual basis for concluding that the party agreed to do so.” Although *Stolt-Nielsen* involved an arbitration agreement that was silent on the issue of class arbitration, the Court found that the same reasoning controlled here.

The Court’s rationale was driven, in part, by the critical differences between class arbitration and the individualized form of arbitration envisioned by the FAA. The Court explained that individual arbitration boasts lower costs, greater efficiency and speed, and the ability to select expert arbitrators to resolve each dispute. On the other hand, class arbitration is slower, more costly, and can raise significant due process concerns, such as litigating the rights of absent class members without the right to full appellate review. The Court concluded that neither silence nor ambiguity provides a sufficient basis to conclude that the parties agreed to forego the central benefits of individual arbitration in favor of a classwide proceeding.

It is also significant that the Court rejected the Ninth Circuit’s application of the California contract-law principle that courts should construe an ambiguity against the drafter. To the extent the application of that principle permitted classwide arbitration, a term that was not contained in the arbitration agreement, the Court held that such a principle was inconsistent with the FAA. The Court disclaimed that its holding was new or novel and said that it was “consistent with a long line of cases holding that the FAA provides the default rule for resolving certain ambiguities in arbitration agreements.”

The Court also confirmed that parties to an arbitration agreement are free to authorize arbitrators to resolve “gateway” issues, such as whether the parties have a valid arbitration agreement and whether a specific dispute is covered by the arbitration agreement. The parties to the agreement in this case, however, did not so authorize. As a result, the Court did not decide whether the issue of “class arbitration” falls into this category.

It is also of note that the Court confirmed its jurisdiction under 9 U.S.C. § 16(a)(3) to hear appeals of any final order that both compels arbitration and dismisses the underlying claims. But in a footnote, the Court distinguished cases wherein the District Court has compelled arbitration and entered a stay, as is often the case.

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The Supreme Court's decision reaffirms the force of the FAA in interpreting arbitration agreements and solidifies its importance over state-law principles that conflict with its fundamental principles, at least in the context of class arbitration. As a result, the decision likely presents an obstacle to those who seek to invoke state-law contract principles in an attempt to modify or invalidate arbitration agreements. Although the outcome will likely depend on the language in the arbitration agreement, the issue being challenged, and the state-law principle being invoked, it is clear that, at least where the dispute involves classwide arbitration, the FAA will govern and require an affirmative contractual basis before such arbitration can proceed.

Notably, in arriving at its ultimate holding that the FAA requires an affirmative contractual basis to compel class arbitration, the Court accepted without deciding that the agreement in *Lamps Plus* should be regarded as ambiguous. The Court did not analyze what language constitutes an affirmative contractual basis sufficient to allow for class arbitration. It is thus for future courts to consider what language might satisfy that standard.

Justice Thomas filed a concurring opinion, and Justices Ginsburg, Breyer, Sotomayor, and Kagan filed dissenting opinions.

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