The United States Supreme Court Adopts Severability Analysis in Rent-A-Center v. Jackson

Yesterday the United States Supreme Court decided Rent-A-Center West v. Jackson, ___ U.S. ___, slip op. (June 21, 2010). Rent-A-Center raised the question whether "a district court may decide a claim that an arbitration agreement is unconscionable, where the agreement explicitly assigns that decision to the arbitrator." The United States Court of Appeals for the Ninth Circuit had said "yes," but the Supreme Court said "no."

In a 5-4 opinion by Associate Justice Antonin Scalia, joined in by Chief Justice John G. Roberts, Jr. and Associate Justices Anthony M. Kennedy, Clarence Thomas and Samuel A. Alito, Jr , the Court held that the employee had to arbitrate its claim that certain provisions of an arbitration agreement were allegedly unconscionable because the parties clearly and unmistakably agreed to arbitrate arbitrability questions, and the employee did not specifically claim that that agreement was unconscionable. The Court said that the parties' clear and unmistakable agreement to arbitrate arbitrability was, as a matter of federal law, severable from the other provisions of the arbitration agreement, including the ones the employee said were unconscionable.

Prior to the decision we had advocated in the Forum (here and here), and in our cover story published in the March 2010 issue of Alternatives to the High Cost of Litigation (blogged **here**), that the Court should resolve the case in favor of Rent-A-Center using a severability analysis of sorts derived from Buckeye Check Cashing v. Cardegna, 546 U.S. ___ (2006) and Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967). And that's exactly what happened, even though neither side advocated or addressed the severability argument before the Court, a point made by Associate Justice Stevens' dissenting opinion, which was joined in by Associate Justices Ruth Bader Ginsburg, Stephen G. Breyer and Sonia Sotomayor. See Dissenting Op. at 1. (The district court's analysis, however, which was reversed by the Ninth Circuit, was, according to the Court, consistent with the Buckeye Check Cashing and Prima Paint severability principle. See Slip op. at 9.)

Readers may recall that before certiorari was granted in Rent-a-Center we argued:

There is logic to the rule adopted by the [Court of Appeals for the Ninth Circuit]. . . in that unconscionability is a state law defense that goes to the enforceability of an agreement. When a party challenges the enforceability of an arbitration agreement, the court ordinarily decides it ? unless the parties clearly and unmistakably agree otherwise. And while the parties clearly and unmistakably agreed to arbitrate arbitrability, that agreement was ? as is often the case ? simply a component of the rest of the arbitration agreement. If the entire arbitration agreement is unenforceable because of unconscionability, then so too must be the agreement to arbitrate arbitrability.

The problem with the majority's logic is that it does not distinguish between the enforceability of the clear and unmistakable agreement to arbitrate arbitrability and the enforceability of the parties' agreement to arbitrate all other disputes. The Rent-A-Center parties envisioned that a dispute concerning the enforceability of their agreement to arbitrate all other disputes would be decided by the arbitrators. That is what the parties' agreement said, and the United States Supreme Court has said that parties can enter into such agreements, provided they are clear and unmistakable.

We think courts would better advance the purposes of the Federal Arbitration Act by engaging in a severability analysis of sorts when confronting questions like the one in Rent-A-Center. When parties agree not only to arbitrate the merits of controversies unrelated to the arbitration clause, but also clearly and unmistakably agree to arbitrate arbitrability, the latter agreement is tantamount to an arbitration agreement within an arbitration agreement. One agreement concerns who decides disputes concerning the existence, formation or enforceability of the other agreement. And the other agreement concerns the parties' obligation to arbitrate all other disputes. Each should be analyzed separately under Federal Arbitration Act Section 2.

What the court did in Rent-A-Center was assume that, if any part of the arbitration agreement was unenforceable for any reason, then the entire arbitration agreement ? including the clear and unmistakable agreement to arbitrate arbitrability ? must fail. Perhaps ironically, the Court found support for this analysis in the Prima Paint/Buckeye Check Cashing line of cases that hold that an enforceability challenge directed at the contract as a whole ? as opposed to the arbitration agreement specifically ? must be decided by the arbitrators rather than the court. Because the challenge here was to a stand-alone arbitration agreement that included a clear and unmistakable agreement to arbitrate arbitrability, the Court simply assumed that Federal Arbitration Act Section 2 required the Court to decide it. But doing so was inconsistent with the parties' clearly expressed intent that the arbitrators would decide arbitrability questions, at least arbitrability questions that did not concern the enforceability of the parties' agreement to arbitrate

arbitrability.
The Court should have limited its inquiry to whether the parties' agreement to arbitrate arbitrability was substantively unconscionable. If not, then the Court should have directed that the arbitrators decide the question whether the remainder of the arbitration clause was substantively unconscionable. Had the Court looked at the problem from that perspective, we believe it would have concluded that the unconscionability defense did not apply to the parties' clear and unmistakable agreement to arbitrate, and that, accordingly, the arbitrators had to decide whether the challenge to the remainder of the arbitration clause had merit.
. . . .
So we think the Court should have enforced the agreement to arbitrate arbitrability by committing to the arbitrators the question whether the parties' agreement to arbitrate all other claims was unconscionable because it was allegedly one-sided. Had it done so, it would have given full force and effect to the parties' clearly expressed intentions, the pro-enforcement policies of Federal Arbitration Act Section 2, and the letter and spirit of First Options.

(See Jackson v. Rent-A-Center West, Inc.: Who Gets to Decide Whether an Arbitration Agreement is Unconscionable when the Parties Clearly and Unmistakably Say the Arbitrators Decide Arbitrability?, Loree Reinsurance and Arbitration Law Forum (Sept. 23, 2009) (emphasis added)).

In a similar vein, the Supreme Court explained:
The Agreement here contains multiple "written provision[s]" to "settle by arbitration a controversy." Two are relevant to our discussion. First, the section titled "Claims Covered By The Agreement" provides for arbitration of all "past, present or future" disputes arising out of Jackson's employment with Rent-A-Center. Second, the section titled "Arbitration Procedures" provides that "[t]he Arbitrator . . . shall have exclusive authority to resolve any dispute relating to the . . . enforceability . . . of this Agreement including, but not limited to any claim that all or any part of this Agreement is void or voidable." The current "controversy" between the parties is whether the Agreement is unconscionable. It is the second provision, which delegates resolution of that controversy to the arbitrator, that Rent-A-Center seeks to enforce. . . .
The delegation provision is an agreement to arbitrate threshold issues concerning the arbitration agreement. . . .
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 on any other. The additional agreement is valid under §2 "save upon such grounds as exist in law or in equity for the revocation of any contract," and federal courts can enforce the agreement by staying federal litigation under §3 and compelling arbitration under §4. The question before us, then is whether the delegation provision is valid under §2.
. . . .
Here, the "written provision. . . to settle by arbitration a controversy," 9 U.S.C. §2, that Rent-a-Center asks us to enforce is the delegation provision -- the provision that gave the arbitrator "exclusive authority to resolve any dispute relating to the . . . enforceability . . . of this Agreement[.]". . . The "remainder of the contract[]" [as that term was used in Buckeye Check Cashing,] is the rest of the agreement to arbitrate claims arising out of Jackson's employment with Rent-A-Center. To be sure this case differs from Prima Paint, Buckeye, and [Preston v. Ferrer, 552 U.S. 346 (2008)] in that the arbitration provisions sought to be enforced in those cases were contained in contracts unrelated to arbitration -- contracts for consulting services, check cashing services, and "personal management" or "talent agent" services. In this case the underlying contract itself is an arbitration agreement. But that makes no difference. Application of the severability rule does not depend on the substance of the remainder of the contract. Section 2 operates on the specific "written provision" to "settle by arbitration a controversy" that the party seeks to enforce. Accordingly, unless Jackson challenged the delegation provision specifically, we must treat it as valid under §2 and must enforce it under §§3 and 4, leaving any challenge to the validity of the Agreement as a whole for the arbitrator.

Slip op. at 4-6 & 8 (citations and footnote omitted). The Court concluded that the District Court correctly found that Jackson had challenged only the arbitration agreement as a whole, not the delegation provision specifically, and accordingly reversed the Ninth Circuit's judgment. See Slip op. at 9 & 12.

The Supreme Court has now decided two arbitration cases this term ? this one and **Stolt-Nielsen, S.A. v. AnimalFeeds Int'l Corp.,** ___ U.S. ___, slip op. (April 27, 2010) ? in favor of the party-autonomy principle inherent in the Federal Arbitration Act, even though the effect of those decisions may not necessarily lead to the fairest result for parties of limited bargaining power. Both cases

were decided 5-4 along ideological lines (with Justice Kennedy supplying the swing vote). These decisions may provide fodder for those in Congress that favor anti-arbitration legislation designed to protect consumers, employees and other claimants.

And, as most readers are aware, the United States Supreme Court recently granted certiorari in another Ninth Circuit case, AT&T Mobility v. Concepcion, No. 09-893 (see report in our good friend Karl Bayer's Disputing Blog **here**), a case that will test whether Stolt-Nielsen's reasoning that consent to class arbitration cannot be implied applies in the adhesive context, and, if so, whether the FAA rules of "fundamental importance" discussed in Stolt-Nielsen supercede a state law invalidating class arbitration waivers on unconscionability grounds. That will surely be a closely-watched case next term, and one you will hear more about in the future here at the Forum.