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Ninth Circuit Provides Long-Awaited Guidance on Mass Arbitration Provisions

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Authors: David M. Krueger

In the long-awaited newest chapter of case law discussing the validity and enforceability of arbitration clauses and class action waivers, the Ninth Circuit on October 28, 2024, dealt a setback, though not a fatal blow, to companies attempting to create reasonable procedures to stem the tide of (often frivolous) mass arbitration. Specifically, in Heckman v. Live Nation, et al., No. 23-55770 (9th Cir.), the Court struck down an unusually company-friendly arbitration delegation clause and set of arbitral rules intended to stymie mass arbitrations as unconscionable. Although the decision should hopefully be distinguishable on its facts, and Defendants have requested a rehearing, the decision provides a helpful road map on provisions that-though attractive because of their defense-friendly nature-could end up rendering an arbitration agreement unconscionable.

Background of *Heckman v. Live Nation*

The Plaintiffs in *Heckman* bought tickets to live entertainment events - promoted by Live Nation Entertainment, Inc. and sold through Ticketmaster LLC's website - then later instituted a putative antitrust class action against Defendants Live Nation and Ticketmaster, alleging anticompetitive practices in online ticket sales. The Plaintiffs' agreement to purchase the tickets online through Ticketmaster's website subjected them to Ticketmaster's Terms of Use, which included an arbitration agreement stating that any claim arising out of a ticket purchase would proceed through a mandatory expedited/mass arbitration process by the newly created alternative dispute resolution entity New Era ADR. The Defendants filed a motion to compel arbitration, arguing that the underlying disputes should be decided by a New Era arbitrator, including any disputes regarding the enforceability of the arbitration agreement.

The Central District of California (Judge Wu) denied the Defendants' motion to compel arbitration, holding the arbitration agreement was unconscionable under California law, due in part to New Era's rules employing what the Court viewed as novel and unusual expedited/mass arbitration procedures. The Defendants appealed.

The Ninth Circuit in *Heckman* affirmed the district court's order, holding that the delegation clause and arbitration agreement were unconscionable. The Court further held that the application of California's unconscionability law to the facts of the case was not preempted by the Federal Arbitration Act ("FAA"). Finally, as an alternate and independent ground, it held that the FAA does not preempt California's prohibition of class action waivers contained in contracts of adhesion in large-scale, small-stakes consumer cases.

Ninth Circuit Finds Procedural and Substantive Unconscionability

Under California law, the doctrine of unconscionability of a contract requires satisfying both a procedural and a substantive element-the former focusing on oppression or surprise due to unequal bargaining power, the latter focusing on unfair or one-sided impacts of the contract's terms.

Procedural unconscionability generally occurs within a contract of adhesion, wherein a contract that is imposed and drafted by the party of superior bargaining strength relegates to the subscribing party only the opportunity to adhere to the contract or reject it. Substantive unconscionability requires a more subjective analysis of the terms of a contract.

The Ninth Circuit found procedural and substantive unconscionability in the Ticketmaster arbitration agreement. As to procedural unconscionability, the Court held that "[t]he contract between Plaintiffs and Ticketmaster is much more than a mere garden variety contract of adhesion" and pointed out that, due to the Defendants' industry dominance, users essentially had two options: (a) use Ticketmaster's website and accept its terms (thereby entering into a contract of adhesion), or (b) refuse to use the website and be entirely foreclosed from purchasing tickets on the primary market. The Court also took umbrage with the fact that the terms allow for unilateral modification without prior notice, retroactive application, and are "so dense, convoluted and internally contradictory to be borderline unintelligible." The Court noted that Defendants' own counsel struggled, at times, to explain the terms during oral argument.

As to substantive unconscionability, the Court focused on New Era's rules, which the arbitration clause provided would apply in any mass arbitration. The Court expressed extreme concern at New Era's bellwether provision, which allowed the outcomes of earlier arbitrations to bind subsequent arbitrations involving other claimants-an impact the Court noted would "violate basic principles of due process." The Court also found that New Era's procedural limits on discovery, limited appeal rights, arbitrator selection provisions, and terms allowing for unilateral retroactive changes were "overly harsh or one-sided" in favor of Defendants. In sum, "New Era's Rules provide to defendants many of the protections and advantages of a class action" while providing "virtually none of [a class action's] protections and advantages" to non-bellwether claimants. "Read together, the Rules and the Terms are so overly harsh and or one-sided as to unequivocally represent a systematic effort to impose arbitration as an inferior form designed to work to Live Nation's advantage."

The Court Further Held That the FAA Did Not Preempt Claims Brought Under New Era's Mass Arbitration Procedures

The Court also rejected the Defendants' argument that the FAA preempted California's law disfavoring arbitration and class action waivers.

The Court explained: "It is clear that Congress did not have class-wide arbitration in mind when it passed the FAA."

This part of the decision is based on two landmark cases: In *Discover Bank v. Superior Court* (2005), the California Supreme Court held that waiver of classwide arbitration in a consumer contract of adhesion is unconscionable under certain circumstances and should not be enforced, more or less creating a general prohibition on class action and class arbitration waivers under California law. In *AT&T Mobility LLC v. Concepcion* (2011), the United States Supreme Court held that the FAA preempts state courts' use of the unconscionability doctrine to invalidate arbitration agreements that preclude classwide proceedings and remedies.

In *Heckman*, the Ninth Circuit read *Concepcion* to "stand for the principle that state law may not create an obstacle to the FAA's purpose of protecting specifically *bilateral* arbitration"-this principle is "simply inapplicable" in the context of "[w]hat New Era calls 'mass arbitration.'" The Plaintiffs will no doubt attempt to use this portion of the decision to circumvent *Concepcion* in other mass arbitrations, though its applicability may be limited based on the extreme facts of the *Heckman* case.

Defendants Petition for Rehearing

On November 12, 2024, Live Nation and Ticketmaster filed a Petition for Panel Rehearing and/or Rehearing En Banc with the Ninth Circuit. In this petition, the Defendants argue that - rather than invalidating the entire arbitration agreement and denying the motion to compel arbitration - the Court should have merely severed the delegation portion of the arbitration agreement, leaving the rest of the arbitration agreement intact and sending the underlying dispute to a different tribunal (i.e., FairClaims, which is mentioned as a backup in the arbitration agreement, or another arbitration provider). Simultaneously, the petition aims at California's severability analysis in general and claims it violates the FAA by discriminating against arbitration agreements in failing to effectuate the parties' core bargain (e.g., arbitration). The petition also calls out what Defendants view as "uncertainty" created by the opinion on "whether the panel's holding applies beyond New Era's mass arbitration protocols" and lodges concerns that the decision could have a chilling effect on companies relying on any case consolidation protocol for mass arbitration filings.

Takeaways

While the Plaintiffs' bar may attempt to characterize *Heckman* as gutting all mass arbitration procedures, the decision is not nearly so broad. Rather, it is focused on one specific website (Ticketmaster), which is the dominant player in its industry, and the fact that its Terms of Use, and those of New Era, were too "opaque and unfair," "one-sided" and "overtly favor[ed] [the] defendants." The Ninth Circuit did *not* blanketly reject any attempts by companies or ADR forums to impose reasonable procedures on mass arbitration.

Regardless, using *Heckman* as a "what-not-to-do" guide, companies should closely evaluate the rules of any potential arbitration providers and their own terms, and be wary of any terms or rules that limit fair and equal bilateral arbitration processes and procedures (including when it comes to arbitral briefing, discovery, and appellate rights). While these terms may be attractive in the short term, they could tip the scales against conscionability. Finally, companies should use caution when establishing arbitration agreement update notice provisions (and when actively updating terms) to ensure that consumers receive adequate notice of their rights under these agreements and to minimize surprise, as well as providing meaningful opportunities for opt-out.

As the legal landscape continues to evolve, staying informed and proactive is the best defense.

For more information, please contact a member of Benesch's **Litigation Practice Group**, along with our **Retail & E-Commerce** industry team, please contact:

David Krueger at **dkrueger@beneschlaw.com** or 216.363.4683