No. 09-893

In the
Supreme Court of the United States

AT&T MOBILITY LLC,

Petitioner,

v.

VINCENT AND LIZA CONCEPCION,

Respondents.

On Petition for Writ of Certiorari
to the United States Court of Appeals
for the Ninth Circuit

BRIEF AMICUS CURIAE OF PACIFIC LEGAL FOUNDATION, AMAZON.COM, INC., AND EARTHLINK, INC., IN SUPPORT OF PETITIONER

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QUESTION PRESENTED

Whether the Federal Arbitration Act preempts States from conditioning the enforcement of an arbitration agreement on the availability of particular procedures—here, class-wide arbitration—when those procedures are not necessary to ensure that the parties to the arbitration agreement are able to vindicate their claims.

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INTEREST OF AMICI CURIAE

Pacific Legal Foundation (PLF)[1] was founded more than 35 years ago and is widely recognized as the largest and most experienced nonprofit legal foundation of its kind. PLF litigates matters affecting the public interest at all levels of state and federal courts and represents the views of thousands of supporters nationwide. Among other things, PLF's Free Enterprise Project defends the freedom of contract, including the right of parties to agree by contract to the process for resolving disputes that might arise between them. To that end, PLF has participated as amicus curiae in many important cases involving the Federal Arbitration Act (FAA) and contractual arbitration in general, including *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, Docket No. 08-1198; *Athens Disposal Co., Inc. v. Franco*, --- S. Ct. ---, No. 09-272, 2010 WL 58763 (Jan. 11, 2010); *DHL Express (USA), Inc. v. Ontiveros*, 129 S. Ct. 1048 (2009); *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008); *Preston v. Ferrer*, 552 U.S. 346 (2008); *Circuit City Stores, Inc. v. Gentry*, 128 S. Ct. 1743 (2008); and *Cingular Wireless, LLC v. Mendoza*, 547 U.S. 1188 (2006).

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[1] Pursuant to this Court's Rule 37.2(a), all parties have consented to the filing of this brief. Counsel of record for all parties received notice at least 10 days prior to the due date of the Amici Curiae's intention to file this brief. Letters evidencing such consent have been filed with the Clerk of the Court.

Pursuant to Rule 37.6, Amici Curiae affirm that no counsel for any party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than Amici Curiae, their members, or their counsel made a monetary contribution to its preparation or submission.

Amazon.com, Inc., based in Seattle, Washington, is one of the largest and best known online retailers, opening its virtual doors on the World Wide Web in July, 1995. Amazon seeks to be the Earth's most customer-centric company, where customers can find and discover anything they might want to buy online at the lowest possible prices. During its history, Amazon.com, Inc., has relied on arbitration clauses in a variety of online contracts that govern its relationships with millions of consumers as well as with hundreds of thousands of vendors and other companies with which it does business. Amazon.com, Inc., supports the arguments favoring individual arbitration.

EarthLink, Inc. (EarthLink), is a national Internet service provider headquartered in Atlanta, Georgia. EarthLink offers access to the Internet for millions of subscribers through narrowband and broadband access services, including dial-up, DSL and cable Internet service, as well as other Internet-based services like home networking, Web hosting, and online security products. EarthLink's subscribers agree to arbitrate, on an individual basis, any disputes they have with the company in connection with their subscription to EarthLink's services. Thus, EarthLink has an interest in ensuring that the courts continue to properly and fairly enforce and construe arbitration clauses in consumer contracts.

INTRODUCTION AND SUMMARY OF REASONS FOR GRANTING THE PETITION

This case was brought under diversity jurisdiction in the federal courts, but the Ninth Circuit below applied California law and it is, in fact, the California

courts' open hostility to arbitration that is the crux of the problem exemplified by this case.

In *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 443 (2006), this Court reaffirmed that Congress enacted the Federal Arbitration Act (FAA), 9 U.S.C. §§ 1-16, to overcome judicial resistance to arbitration and that the savings clause of Section 2 embodies the national policy favoring arbitration and places arbitration agreements on equal footing with all other contracts. Applying this federal substantive law to the states, this Court held that arbitration contracts are to be construed as any other contract, not subjected to more stringent review or disfavor because the subject matter is arbitration. The Court thus confirmed the holding of *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984).

These matters have been settled law for 25 years. California courts, however, still scrutinize arbitration with suspicion and dislike, and invalidate arbitration contracts with distressing regularity. Most commonly, California courts invoke unconscionability principles to invalidate the contracts. However, the unconscionability doctrine is not applied neutrally among all types of contracts, resulting in the disproportionate invalidation of arbitration provisions as opposed to other contracts. This feature of California jurisprudence, applied by federal courts exercising diversity jurisdiction, as in this case, as well as other federal and state courts, interferes with the normal and proper functioning of the California marketplace, injuring businesses and consumers alike. Because consumer contracts—including arbitration clauses—are ubiquitous throughout California and the Ninth Circuit, and because California courts are invalidating arbitration

clauses at a rate far exceeding that of any other state, this case presents an important question that can be resolved only by this Court. The petition for writ of certiorari should be granted.

ARGUMENT

I

CALIFORNIA'S UNCONSCIONABILITY DOCTRINE UNIQUELY DISFAVORS ARBITRATION CONTRACTS

This Court has recognized that the freedom to make and enforce contracts is a fundamental element of free choice and should be protected for that reason. *See, e.g., Advance-Rumely Thresher Co., Inc. v. Jackson*, 287 U.S. 283, 288 (1932) ("[F]reedom of contract is the general rule and . . . [t]he exercise of legislative authority to abridge it can be justified only by the existence of exceptional circumstances."); *Twin City Pipe Line Co. v. Harding Glass Co.*, 283 U.S. 353, 356 (1931) ("The general rule is that competent persons shall have the utmost liberty of contracting and that their agreements voluntarily and fairly made shall be held valid and enforced in the courts."). This Court declared that state law grounds for invalidation must not "take[] [their] meaning precisely from the fact that a contract to arbitrate is at issue . . . . 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) (holding that the FAA preempts California Labor Code section 229 insofar as the statute allowed litigation in court to collect wages without regard to the existence of any private arbitration agreement). Or, as the Court rephrased the point in

Doctor's Associates, Inc. v. Casarotto, 517 U.S. 681, 687 (1996), "Courts may not . . . invalidate arbitration agreements under state laws applicable only to arbitration provisions." Yet this is *exactly* the tactic adopted by the Ninth Circuit below, applying California law.

The court below began its analysis by finding that the arbitration agreement was a contract of adhesion (defined simply as a "standardized contract" with non-negotiable terms). *Laster v. AT&T Mobility LLC*, 584 F.3d 849, 854-55 (9th Cir. 2009). This Court, however, has refused to invalidate arbitration agreements solely on the grounds that an individual must take-it-or-leave-it. *See Gilmer v. Interstate/ Johnson Lane Corp.*, 500 U.S. 20, 33 (1991) ("Mere inequality in bargaining power, however, is not a sufficient reason to hold that arbitration agreements are never enforceable in the employment context."); *see also Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 7 F.3d 1110, 1118 (3d Cir. 1993) (arbitration agreements are enforceable even if they involve unequal bargaining power). *Cf. Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 596-97 (1991) (upholding a forum-selection clause in cruise-line ticket). Even California has no such requirement outside the context of arbitration. *Cubic Corp. v. Marty*, 185 Cal. App. 3d 438, 449 (1986) ("The determination that a contract is adhesive is only 'the beginning and not the end of the analysis insofar as enforceability of its terms is concerned.'") (citation omitted). As the Seventh Circuit noted in *IFC Credit Corp. v. United Bus. & Indus. Fed. Credit Union*, 512 F.3d 989, 992-93 (7th Cir. 2008), form contracts are "common and enforceable" and serve an economically efficient purpose: "As long as the price is

negotiable and the customer may shop elsewhere, consumer protection comes from competition rather than judicial intervention." *Id.* at 993.

Thus, to be unenforceably adhesive, a contract must also include some element of duress or lack of free choice. *See Marty*, 185 Cal. App. 3d at 449 ("[T]he weaker party may have no realistic opportunity *to look elsewhere* for a more favorable contract." (emphasis added)); *accord*, *Madden v. Kaiser Found. Hosps.*, 17 Cal. 3d 699, 712 (1976) ("[T]he principles of adhesion contracts . . . do not bar enforcement of terms of a negotiated contract which neither limit the liability of the stronger party nor bear oppressively upon the weaker."); *Spinello v. Amblin Entm't*, 29 Cal. App. 4th 1390, 1396-97 (1994); *Dean Witter Reynolds, Inc. v. Superior Court*, 211 Cal. App. 3d 758, 766-67 (1989). In *Spinello*, the court of appeal found that a form arbitration agreement was not adhesive because the plaintiff "had the opportunity to go elsewhere . . . [by] submitt[ing] his script to . . . other producers." 29 Cal. App. 4th at 1397. And in *Dean Witter*, the court recognized that the "availability of alternative products in the market . . . demonstrates that any claim based on unconscionability lacks merit." *Spinello*, 211 Cal. App. 3d at 767.

Adhesiveness has never been held sufficient to render a contract unenforceable under California law; there must be some element of substantive unconscionability as well. *See Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d 807, 819-20 (1981). However, unconscionability is a notoriously flexible concept. *See* Joseph M. Perillo, *Corbin on Contracts: Avoidance & Reformation* § 29.1 (rev. ed. 2002) ("Unconscionability is one of the most amorphous terms in the law of contracts."). The

flexibility no doubt stems from the original purpose of the unconscionability doctrine: to protect consumers. Richard A. Epstein, *Unconscionability: A Critical Reappraisal*, 18 J. L. & Econ. 293, 302 (1975) ("Ideally, the unconscionability doctrine protects against fraud, duress and incompetence, without demanding specific proof of any of them."). However, the doctrine was not written to enable courts to do justice by rewriting contracts. In fact, in the official comments to Uniform Commercial Code § 2-302 (2003), the drafters explained that the unconscionability principle "is one of prevention of oppression and unfair surprise and not of disturbance of allocation of risks because of superior bargaining power." *See id.*, official comment 1; *accord* Cal. Civ. Code § 1670.5, Legis. Comm. Cmt. (same).

While the FAA permits state courts to apply "ordinary principles of unconscionability," the FAA forbids state courts from implementing substantive state policies that undermine arbitration clauses. Moreover, "a state cannot evade FAA preemption simply by labeling procedures which are inconsistent with its substantive policies as unconscionable." Alan S. Kaplinsky & Mark J. Levin, *The Gold Rush of 2002: California Courts Lure Plaintiffs' Lawyers (but Undermine Federal Arbitration Act) by Refusing to Enforce "No-Class Action" Clauses in Consumer Arbitration Agreements*, 58 Bus. Law. 1289, 1295 (2003). Similarly, this Court's arbitration jurisprudence does not permit a state to use unconscionability as a ground for voiding arbitration agreements in certain classes of disputes just because the state court believes those disputes are better handled by some other means of dispute resolution. *See Preston v. Ferrer*, 552 U.S. at 359 ("When parties agree to arbitrate all questions arising under a contract, the FAA supersedes state laws

lodging primary jurisdiction in another forum, whether judicial or administrative."). As one commentator noted:

> [T]he United States Supreme Court surely would review state courts' unconscionability rulings to the extent necessary to prevent the unconscionability doctrine from effectively nullifying the FAA with respect to a huge class of contracts. Indeed, the Court has twice stated that state courts may not "rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what . . . the state legislature cannot."

Stephen J. Ware, *Alternative Dispute Resolution* § 2.25(b), at 58 (West 2001) (citing *Doctor's Assocs.*, 517 U.S. at 687-88 n.3); *Perry*, 482 U.S. at 492 n.9. That is, a court may not "decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause." *Allied-Bruce Terminix Cos., Inc. v. Dobson*, 513 U.S. 265, 281 (1995).

Nonetheless, California courts have found the unconscionability doctrine to be a valuable tool to invalidate arbitration contracts. In so doing, California has developed a deserved reputation as "hostile" to arbitration. A recent empirical analysis conducted by Stephen Broome revealed that unconscionability challenges in California succeed against arbitration provisions with far greater frequency than any other type of contract provision. Stephen A. Broome, *An Unconscionable Application of the Unconscionability Doctrine: How the California Courts Are Circumventing*

the Federal Arbitration Act, 3 Hastings Bus. L.J. 39 (2006). Broome identified 114 cases in which the California Courts of Appeal considered the unconscionability of arbitration contracts; in fifty-three of those cases, the arbitration provision was held unconscionable and unenforceable and another thirteen found some aspect of the arbitration provision to be unconscionable and severed it. *Id.* at 44-45.[2]

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[2] Broome's survey included cases decided from 1982 to 2006. The starting date was set by California's adoption of the currently existing unconscionability doctrine in *A & M Produce Co. v. FMC Corp.*, 135 Cal. App. 3d 473, 486 (1982). Broome, 3 Hastings Bus. L.J. at 44 n.33. Since 2006, court invalidation of arbitration clauses on grounds of unconscionability has, if anything, accelerated. *See Lhotka v. Geographic Expeditions, Inc.*, --- Cal. Rptr. 3d ---, No. A123725, 2010 WL 325491, at *5 (Cal. Ct. App. Jan. 29, 2010); *Borison v. Gibbs, Giden, Locher, Turner & Senet*, No. B216428, 2010 WL 398448, at *5 (Cal. Ct. App. Feb. 5, 2010); *Parada v. Superior Court*, 176 Cal. App. 4th 1554, 1585 (2009); *Geller v. Wedbush Morgan Securities, Inc.*, No. B211579, 2009 WL 4894961, at *5 (Cal. Ct. App. Dec. 21, 2009); *Vu v. Superior Court*, No. B123988, 2009 WL 3823383, at *5 (Cal. Ct. App. Nov. 17, 2009); *Aguilar v. F.S. Hotels (L.A.) Inc.*, No. B210159, 2009 WL 2712298, at *4 (Cal. Ct. App. Aug. 28, 2009); *Olvera v. El Pollo Loco, Inc.*, 173 Cal. App. 4th 447, 457 (2009); *Duran v. Discover Bank*, No. B203338, 2009 WL 1709569, at *7 (Cal. Ct. App. June 19, 2009); *Sanchez v. W. Pizza Enters., Inc.*, 172 Cal. App. 4th 154, 181 (2009); *Murphy v. Check 'N Go of Cal., Inc.*, 156 Cal. App. 4th 138, 149 (2007); *Fuentes v. Rent-A-Center, Inc.*, No. A121673, 2009 WL 2351605, at *11 (Cal. Ct. App. July 31, 2009); *Stiglich v. Jani-King of Cal., Inc.*, No. D051811, 2008 WL 4712862, at *11 (Cal. Ct. App. Oct. 28, 2008), *rev. denied*; *Kim v. Francesca's Collections of Cal., Inc.*, No. B207572, 2009 WL 1016599, at *5 (Cal. Ct. App. Apr. 16, 2009); *Tourangeau v. LBL Ins. Servs., Inc.*, No. G038637, 2008 WL 1952377, at *4 (Cal. Ct. App. May 6, 2008). *Cf. D.C. v. Harvard-Westlake Sch.*, 176 Cal. App. 4th 836, 869 (2009) (no procedural unconscionability where parents had opportunity to

(continued...)

Forty-eight cases upheld the arbitration contract. By way of contrast, of the forty-six unconscionability claims made outside the context of arbitration, forty-one of the contracts were upheld by the courts, while only five were struck down as unconscionable. *Id.* at 47. By targeting arbitration provisions for exceptionally harsh review under the unconscionability doctrine, California courts violate Section 2 of the FAA, which demands that arbitration contracts be considered on "equal footing" with any other contract. *Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 225-26 (1987). *See also Gilmer*, 500 U.S. at 36.

II

CALIFORNIA COURTS APPLY SPECIAL TESTS TO ARBITRATION CONTRACTS, BUT NOT OTHER TYPES OF CONTRACTS

California courts and the Ninth Circuit below restate the definition that unconscionability means "shocks the conscience," traditionally meaning something no man would contemplate unless he were delusional. *California Grocers Ass'n v. Bank of America*, 22 Cal. App. 4th 205, 214 (1994) (a substantively unconscionable contract is one that "[n]o man in his

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[2] (...continued)
convince private school administrators to remove offending provision from enrollment contract containing an arbitration clause). The single exception to this trend is *Dotson v. Amgen, Inc.*, --- Cal. Rptr. 3d ---, No. 212965, 2010 WL 189653, at *7-*8 (Cal. Ct. App. Jan. 21, 2010), but as of this writing, the decision is not yet final and may be depublished or accepted for review by the California Supreme Court.

senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other" (citations omitted)); *Davis v. O'Melveny & Myers*, 485 F.3d 1066, 1075 (9th Cir. 2007). But these formulations are drained of all meaning if they can be applied to the extremely consumer-friendly arbitration contract in this case, containing provisions that "essentially guarantee that the company will make any aggrieved customer whole who files a claim." *AT&T Mobility*, 584 F.3d at 856 n.9.

A. California Uniquely Employs a "Mutuality Test" to Arbitration Contract Challenges

What accounts for the California courts' willingness to invalidate arbitration contracts as unconscionable as opposed to contracts in other contexts? Mostly, the culprit is a special test that California courts apply to unconscionability claims brought only against arbitration contracts. This test—the "mutuality test"—first appeared in *Stirlen v. Supercuts, Inc.*, 51 Cal. App. 4th 1519 (1997), in which the court held that a contract that requires one party to arbitrate but not the other is so "one-sided" as to be unconscionable. *Id.* at 1532. The *Stirlin* court repeatedly labeled the contract between the parties as a "contract of adhesion," implicitly contradicting earlier California law by assuming that the label would be dispositive of the legal issues. *Id.* at 1533; *see also Kinney v. United Healthcare Servs.*, 70 Cal. App. 4th 1322, 1332 (1999) (invalidating "unilateral obligation to arbitrate"). Yet this disdain of adhesion contracts itself betrays a certain bias.

> "The contract of adhesion is a part of the fabric of our society. It should neither be praised nor denounced . . . ." That is because

> there are important advantages to its use despite its potential for abuse. These advantages include the fact that standardization of forms for contracts is a rational and economically efficient response to the rapidity of market transactions and the high costs of negotiations, and that the drafter can rationally calculate the costs and risks of performance, which contributes to rational pricing.

Goodwin v. Ford Motor Credit Co., 970 F. Supp. 1007, 1015 (M.D. Ala. 1997) (quoting *Roberson v. The Money Tree of Alabama, Inc.*, 954 F. Supp. 1519, 1526 nn.9-10 (M.D. Ala. 1997)).[3]

While expressing a purported concern for public policy, however, none of those advantages were even acknowledged by the California Supreme Court, and

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[3] Richard Epstein explains why the "mutuality argument" cannot be a legitimate basis for declaring a contract unconscionable:

> A could not complain if B decided not to make him any offer at all; why then is he entitled to complain if B decides to make him *better off* by now giving him a choice when before he had none? If A does not like B's offer, he can reject it; but to allow him to first accept the agreement and only thereafter to force B to work at a price which B finds unacceptable is to allow him to resort (with the aid of the state) to the very form of duress that on any theory is prohibited. There is no question of "dictation" of terms where B refuses to accept the terms desired by A. There is every question of dictation where A can repudiate his agreement with B and hold B to one to which B did not consent; and that element of dictation remains even if A is but a poor individual and B is a large and powerful corporation. To allow that to take place is to indeed countenance an "inequality of bargaining power" between A and B, with A having the legal advantage as he is given formal legal rights explicitly denied B.

Epstein, 18 J.L. & Econ. at 297.

that court adopted the mutuality test in *Armendariz v. Found. Health Psychcare Servs., Inc.*, 24 Cal. 4th 83, 117 (2000), announcing that arbitration agreements must contain a "modicum of bilaterality." Since *Armendariz*, more than two-thirds of the courts that invalidated arbitration provisions did so because the provisions lacked mutuality. Broome, 3 Hastings Bus. L.J. at 50-51; *see also* Michael Schneidereit, Note, *A Cold Night: Unconscionability as a Defense to Mandatory Arbitration Clauses in Employment Agreements*, 55 Hastings L.J. 987, 1002 (2004) ("[I]n *Armendariz*, the court honed California unconscionability law into a weapon that could be used against mandatory arbitration agreements."). Indeed, in *Discover Bank v. Superior Court*, 36 Cal. 4th 148, 161 (2005), the California Supreme Court employed a form of the mutuality test to strike down class-arbitration waivers. In the court's view:

> [C]lass action or arbitration waivers are indisputably one-sided. "Although styled as a mutual prohibition on representative or class actions, it is difficult to envision the circumstances under which the provision might negatively impact Discover [Bank], because credit card companies typically do not sue their customers in class action lawsuits."

Id. (quoting *Szetela v. Discover Bank*, 97 Cal. App. 4th 1094, 1101 (2002), *cert. denied*, 537 U.S. 1226 (2003)). The court in *Gentry v. Superior Court*, 42 Cal. 4th 443, 470-72 (2007), *cert. denied*, 128 S. Ct. 1743 (2008), also relied on what it perceived as the one-sided nature of the contract in striking down Circuit City's class-arbitration waiver. Although some language in *Armendariz* suggests that lack of mutuality can be

justified by "business realities," *Armendariz*, 24 Cal. 4th at 117, no lower California court has yet identified a business reality sufficient to justify lack of mutuality in an arbitration agreement. Broome, 3 Hastings Bus. L.J. at 54 (citing Michael G. McGuinness & Adam J. Karr, *California's "Unique" Approach to Arbitration: Why This Road Less Traveled Will Make All the Difference on the Issue of Preemption Under the Federal Arbitration Act*, 2005 J. Disp. Resol. 61, 81 (2005)).[4] *See also* Thomas H. Riske, *No Exceptions: How the Legitimate Business Justification for Unconscionability Only Further Demonstrates California Courts' Disdain for Arbitration Agreements*, 2008 J. Disp. Resol. 591, 602-04 (2008) (The supposed "business realities" exception to the mutuality test, which uses terminology associated with general contract law, but which has been factually impossible to successfully invoke, provides another illustration of how California courts hold arbitration agreements to a unique standard.). The mutuality test thus makes it significantly easier to challenge arbitration agreements as unconscionable.

Yet this Court held that "[t]he 'goals and policies' of the FAA . . . are antithetical to threshold limitations placed specifically and solely on arbitration provisions." *Doctor's Assocs., Inc.*, 517 U.S. at 688. Given this straightforward holding, jurisdictions other than California have been unwilling to adopt a requirement

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[4] Some federal district courts, applying California law, will occasionally find that the mutuality requirement was met and uphold an arbitration agreement. *See Rutter v. Darden Restaurants, Inc.*, No. CV-08-6106, 2008 WL 4949043, at *9 (C.D. Cal. Nov. 18, 2008); *Rodriguez v. Sim*, No. C-08-3982, 2009 WL 975457, at *9-*10 (N.D. Cal. Apr. 10, 2009); *Ramirez-Baker v. Beazer Homes, Inc.*, No. CV-F-008-601, 2008 WL 2523368, at *6-*7 (E.D. Cal. June 20, 2008).

of mutuality for arbitration agreements. *See, e.g., McNaughton v. United Health Care Servs., Inc.*, 728 So. 2d 592, 598-99 (Ala.), *cert. denied,* 528 U.S. 818 (1999) (A mutuality approach relies on the "uniqueness of the concept of arbitration," "assigns a suspect status to arbitration agreements," and therefore "flies in the face of *Doctor's Associates.*"). *See also Harris v. Green Tree Fin. Corp.*, 183 F.3d 173, 180 (3d Cir. 1999) ("substantive federal law stands for the proposition that parties to an arbitration agreement need not equally bind each other with respect to an arbitration agreement if they have provided each other with consideration beyond the promise to arbitrate"); *In re Pate*, 198 B.R. 841, 844 (S.D. Ga. 1996) (same result under Georgia law); *Munoz v. Green Tree Fin. Corp.*, 542 S.E.2d 360, 365 (S.C. 2001) ("[T]he doctrine of mutuality of remedy does not apply here. An agreement providing for arbitration does not determine the *remedy* for a breach of contract but only the *forum* in which the remedy for the breach is determined.").[5]

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[5] *See also State ex rel. Vincent v. Schneider*, 194 S.W.3d 853, 859 (Mo. 2006) ("There is no reason to create a different mutuality rule in arbitration cases. Both parties to this contract exchanged consideration in this sale of a home. The contract will not be invalidated for lack of mutuality of obligation of the arbitration clause."); *Stenzel v. Dell, Inc.*, 870 A.2d 133, 144 (Me. 2005) ("[T]he agreement is not unconscionable because, even though the arbitration clause lacks mutuality of obligation, the underlying contract for the sale of Dell computers is supported by adequate consideration."); *McKenzie Check Advance of Mississippi, LLC v. Hardy*, 866 So. 2d 446, 453 (Miss. 2004); *Walther v. Sovereign Bank*, 386 Md. 412, 433 (2005); *In re Lyon Financial Services, Inc.*, 257 S.W.3d 228, 233 (Tex. 2008). Other than California, only Arkansas routinely invokes mutuality as a reason to invalidate arbitration contracts. *See, e.g., Advance America Servicing of Arkansas, Inc. v. McGinnis*, 375 Ark. 24, 35 (2008).

Meanwhile, outside the arbitration context, California courts do not demand mutuality either. *See Principal Mut. Life Ins. Co. v. Vars, Pave, McCord & Freedman*, 65 Cal. App. 4th 1469, 1488-89 (1998) (unilateral mortgage agreement upheld because "[w]here sufficient consideration is present, mutuality is not essential"); *Hillsman v. Sutter Cmty. Hosp.*, 153 Cal. App. 3d 743, 752 (1984) (upholding unilateral employment contract where consideration requirement is properly met; a "mutuality of obligation" is unnecessary). Thus, California's "mutuality" approach to determining substantive unconscionability in arbitration provisions differs from the standard used to analyze ordinary contractual provisions for unconscionability. Under the mutuality test, the court relies on its own speculation that the arbitral proceeding itself might impede a party's ability to obtain the requested relief.

For nonarbitration contractual provisions, California courts invalidate contracts as unconscionable only upon evidence of measurable, inevitable hardship if the disputed term is enforced. *See Phoenix Leasing Inc. v. Johnson*, No. A089871, 2001 WL 1324778, at *6 (Cal. Ct. App. Oct. 29, 2001) (invalidating provision that would have given lender $208,000 of unaccrued interest); *Ilkhchooyi v. Best*, 37 Cal. App. 4th 395, 411 (1995) (invaliding landlord's attempt to appropriate a portion of the sale price of a lease); *Carboni v. Arrospide*, 2 Cal. App. 4th 76, 83 (1991) (invalidating interest rate of 200% per annum on a secured $99,000 loan); *Ellis v. McKinnon Broadcasting Co.*, 18 Cal. App. 4th 1796, 1806 (1993) (invalidating contract that gave employer all of employee's sales commissions (which were the employee's sole compensation) that were received after the employee left the company when the

sales were generated by the employee prior to his voluntary departure); *Johnisee v. Kimberlite Corp.*, No. A107341, 2005 WL 1249198, at *8 (Cal. Ct. App. May 24, 2005) (same).[6]

B. California Courts Pay Lip Service to the Sliding Scale Test of Unconscionability, but Routinely Ignore It in Application

Under California law, a finding of unconscionability requires both procedural and substantive unconscionability, as measured on a sliding scale (the more substantively unconscionable the contract term, the less procedurally unconscionable it need be to be unenforceable and vice versa). The decision below recites this rule, and claims that *Discover Bank* merely refined, but did not alter it. *AT&T Mobility*, 584 F.3d at 853, 857 (citing *Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 981 (9th Cir. 2007)). Yet as a practical matter, California courts do not distinguish between greater or lesser levels of unconscionability—even the slightest hint of judicially perceived unfairness will suffice to meet either prong of the test. Contrary to the mandate to treat arbitration contracts the same as any other contracts, this approach does not prevail in unconscionability cases outside the context of arbitration.

An extreme example of the failure to apply the sliding scale was the California Supreme Court's

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[6] These five cases are the only ones identified by Stephen Broome where California appellate courts invalidated contracts as unconscionable outside the arbitration context. *See* Broome, 3 Hastings Bus. L.J. at 56-58. *See also Dalis v. Reinhard*, No. H031637, 2009 WL 932650, at *17-*18 (Cal. Ct. App. Apr. 18, 2009) (upholding nonrecourse provision of a promissory note).

decision in *Gentry v. Superior Court*, 42 Cal. 4th 443 (2007), *cert. denied sub nom. Circuit City Stores, Inc. v. Gentry*, 128 S. Ct. 1743 (2008). There, the California Supreme Court declared an arbitration agreement unconscionable because it waived an employee's right to bring a class action lawsuit. It did so despite the fact that the employees were given an information packet on the effect of the arbitration agreement, were required to watch a video providing information on the arbitration process, were told to consult an attorney before signing if they were unclear on its legal effect, and were not only *given the choice not to sign*, but were given a grace period in which to *change their minds after signing*. *See id.* at 474 (Baxter, J., dissenting). In addition, the court ignored the fact that California workers who disapprove of arbitration requirements have many other options for seeking employment. Theodore Eisenberg & Geoffrey P. Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 DePaul L. Rev. 335, 361 (2007).

The *Gentry* court admitted that the employer did not compel workers to sign, but concluded that the agreement was "not entirely free from procedural unconscionability" because employees "felt at least some pressure" to sign it. *Gentry*, 42 Cal. 4th at 472. Such minimal—one might argue, illusory—procedural unconscionability should have required an extremely high level of substantive unconscionability to result in an overall finding of unconscionability under the sliding scale test. But the court instead simply latched onto the class action waiver, which one would be hard pressed to describe as "extremely" unconscionable given

the number of jurisdictions that find it perfectly legitimate.

As the dissenting justice observed, the court's justifications for resisting the use of arbitration in lieu of class action litigation may have made good policy arguments, but the Legislature had chosen to enact a procedure allowing for arbitration, and declaring that public policy *favored* arbitration. The *Gentry* court simply "elevat[ed] a mere judicial affinity for class actions as a beneficial device for implementing the wage laws above the policy expressed by both Congress and our own Legislature." *Id.* at 477 (Baxter, J., dissenting). The court below similarly elevated California's preference for class action lawsuits to serve as a veto for any arbitration provision, no matter how pro-consumer in every other respect, if that provision required individual adjudication.

III

THIS CASE IS OF NATIONAL IMPORTANCE

The courts' greater receptivity to unconscionability arguments has led to the expected result: Where unconscionability challenges once appeared in less than 1% of all arbitration-related cases, more recently they have appeared in 15-20% of all cases involving arbitration. Aaron-Andrew P. Bruhl, *The Unconscionability Game: Strategic Judging and the Evolution of Federal Arbitration Law*, 83 N.Y.U. L. Rev. 1420, 1441 (2008). The issue presented by this case does not just affect California and the Ninth Circuit, although a rule that impacts the populations of just those two jurisdictions would justify review. The presumption of invalidity applied to arbitration

contracts extends far beyond the boundaries of both California and the Ninth Circuit, however, because federal courts also will invalidate any arbitration contract choice-of-law provision that does not specify California law as controlling. *Omstead v. Dell*, --- F.3d ---, No. 08-16479, 2010 WL 396089 (9th Cir. Feb. 5, 2010), adopting the reasoning of *Oestreicher v. Alienware Corp.*, 322 F. Appx. 489 (9th Cir. Apr. 2, 2009), *aff'g* 502 F. Supp. 2d 1061, 1065-69 (N.D. Cal. 2007). This is another maneuver targeted specifically to arbitration contracts.

The general rule is that where a choice of law provision exists in a private contract, California courts will honor the provision. *See Nedlloyd Lines B.V. v. Superior Court*, 3 Cal. 4th 459, 464-65 (1992) ("In determining the enforceability of arm's-length contractual choice-of-law provisions, California courts shall apply the principles set forth in Restatement section 187, which reflect a strong policy favoring enforcement of such provisions."). The contract challenged in *Omstead* had a choice-of-law provision that all disputes would be resolved under Texas law, but the Ninth Circuit held that "class action waiver is unconscionable under California law because it satisfies the *Discover Bank* test, and California has a materially greater interest than Texas in applying its own law." *Omstead*, 2010 WL 396089, at *4. *See also Hoffman v. Citibank (South Dakota), N.A.*, 546 F.3d 1078, 1083 (9th Cir. 2008) ("if Citibank's class arbitration waiver is unconscionable under California law, enforcement of the waiver under South Dakota law would be contrary to a fundamental policy of California" and remanding to district court for findings as to procedural unconscionability given the ability of cardholders to

opt-out of the arbitration provision); *Tamayo v. Brainstorm USA*, 154 Fed. Appx. 564, 566 (9th Cir. 2005) ("To the extent that Ohio law would enforce the class-action waiver at issue, . . . it would be contrary to California public policy and thus not applicable."); *Davis v. Chase Bank USA, N.A.*, 299 Fed. Appx. 662, 664 (9th Cir. 2008) (disregarding Delaware choice of law provision because it would permit a class action waiver in an arbitration agreement, contrary to California law).

Moreover, because class action waivers are upheld in most other courts, consumers (and their counsel) who wish to sue national corporations can circumvent those waivers by the simple mechanism of initiating a class action lawsuit in California. They need only to find a plaintiff in California to take the lead and file suit in state court, and then, once the lawsuit is under way, broaden the class action to include plaintiffs from around the country. *See* Aaron C. Gundzik & Rebecca Gilbert Gundzik, *Will California Become the Forum of Choice for Attacking Class Action Waivers?*, 25 Franchise L.J. 56, 59 (2005). Thus, although California consumers and businesses are most obviously affected by the California courts' refusal to enforce class action waivers in arbitration, the true impact is national in scope and warrants this Court's review.

CONCLUSION

The California courts consistently hold arbitration agreements to a different standard when it comes to unconscionability, and the decision below represents the latest, and most extreme, example. Seven years ago, then-Justice Janice Rogers Brown explained that "this

court appears to be 'chip[ping] away at' United States Supreme Court precedents broadly construing the scope of the FAA 'by indirection,' despite the high court's admonition against doing so" and "urge[d]" this Court "to clarify once and for all whether our approach to arbitration law comports with its precedents." *Little v. Auto Stiegler, Inc.*, 29 Cal. 4th 1064, 1095 (2003) (Brown, J., concurring and dissenting) (quoting *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 122 (2001)).

California courts, and federal courts applying California law, are employing a special unconscionability analysis to arbitration contracts to thwart the use of arbitration. This Court should review this case to enforce its pronouncements in *Perry* and *Doctor's Associates* that unconscionability analysis may not single out arbitration contracts and treat them differently than other kinds of contracts. This Court remains the only recourse to reestablish the validity of arbitration agreements in the nation's most populous state and Circuit.

The petition for writ of certiorari should be granted.

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Respectfully submitted,

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