No. 14-462

In the
Supreme Court of the United States

DIRECTV, INC.,

Petitioner,

v.

AMY IMBURGIA, et al.,

Respondents.

On Writ of Certiorari to the Court of Appeal of the State of California

BRIEF AMICUS CURIAE OF PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONER

ERNESTO J. SANCHEZ
Law Offices of
Ernesto J. Sanchez
1530 Catalonia Avenue
Coral Gables, Florida 33134
Telephone: (305) 215-3261

DEBORAH J. LA FETRA
Counsel of Record
Pacific Legal Foundation
930 G Street
Sacramento, California 95814
Telephone: (916) 419-7111
Facsimile: (916) 419-7747
E-mail: dlafetra@pacificlegal.org

Counsel for Amicus Curiae Pacific Legal Foundation

QUESTION PRESENTED

Whether the California Court of Appeal erred by holding, in direct conflict with the Ninth Circuit, that a reference to state law in an arbitration agreement governed by the Federal Arbitration Act requires the application of state law preempted by the Federal Arbitration Act.

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INTEREST OF AMICUS CURIAE

Pursuant to Supreme Court Rule 37, Pacific Legal Foundation respectfully submits this brief amicus curiae in support of Petitioner, DIRECTV, Inc.[1] Founded in 1973, Pacific Legal Foundation (PLF) is widely recognized as the largest and most experienced nonprofit legal foundation of its kind. 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 in this Court, the California courts, and many other state supreme courts involving the Federal Arbitration Act (FAA) and contractual arbitration in general. *See, e.g.*, *Oxford Health Plans LLC v. Sutter*, 133 S. Ct. 2064 (2013); *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011); *Rent-A-Center, W., Inc. v. Jackson*, 561 U.S. 63 (2010); *Stolt-Nielsen S. A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010); *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008); and *Preston v. Ferrer*, 552 U.S. 346 (2008).

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[1] Pursuant to this Court's Rule 37.3(a), all parties have consented to the filing of this brief. Letters evidencing such consent have been filed with the Clerk of the Court.

Pursuant to Rule 37.6, Amicus Curiae affirms 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 Amicus Curiae, its members, or its counsel made a monetary contribution to its preparation or submission.

INTRODUCTION AND SUMMARY OF ARGUMENT

Amy Imburgia's contract with DIRECTV included a provision that any disputes would be resolved "only by binding arbitration" and that the parties would not "arbitrate any claim as a representative member of a class or in a private attorney general capacity." It further stated that "[i]f, however, the law of your state would find this agreement to dispense with class action procedures unenforceable, then this entire Section [providing for arbitration] is unenforceable." Finally, it states that the arbitration provisions "shall be governed by the Federal Arbitration Act." *Imburgia v. DIRECTV, Inc.*, 225 Cal. App. 4th 338, 341-42 (2014).

In 2008, Imburgia filed a putative class action against DIRECTV, claiming violations of various California laws related to DIRECTV's assessment of early termination fees. *Id.* at 340. At that time, the rule created by the California Supreme Court in *Discover Bank v. Superior Court*, 36 Cal. 4th 148 (2005), was effectively invalidating all class action waivers in consumer contracts, deeming them unconscionable. DIRECTV did not move to compel arbitration, as it would have been futile under California law. In 2011, the legal landscape changed dramatically when this Court held the *Discover Bank* rule preempted in *Concepcion*, 131 S. Ct. 1740. DIRECTV immediately moved to compel arbitration, *Imburgia*, 225 Cal. App. 4th at 341, but the trial court denied the motion, based on the contract's "law of your state" provision above. The court of appeal affirmed, holding that it had to consider the law of the state, without regard to whether it was preempted. *Id.* at 347.

In so doing, the court below fundamentally misunderstood the meaning and effect of federal preemption. Under the Supremacy Clause, state law—whether statutory or common law—must yield completely when it is preempted by federal law. U.S. Const., art. VI, cl. 2 (the laws of the United States "shall be the supreme Law of the Land . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." In *Concepcion*, this Court expressly held the *Discover Bank* rule preempted, rendering it a legal nullity upon which no court or party may rely. As the Ninth Circuit held in *Murphy v. DirecTV, Inc.*, 724 F.3d 1218, 1226 (9th Cir. 2013), "Section 2 of the FAA, which under *Concepcion* requires the enforcement of arbitration agreements that ban class procedures, *is* the law of California and of every other state."[2]

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[2] The court below did not explicitly rest its decision on *Discover Bank*, citing both that case as well as an anti-waiver provision in the Consumers Legal Remedies Act, Cal. Civ. Code § 1751. Amicus does not address that statute directly because the Question Presented in this case focuses on the lower court's broad holding that it must review contract language referring to state law without regard to whether that state law is preempted. In any event, *Concepcion*'s holding has already been held, even in California, to apply to class action waivers outside the consumer context presented in that case and in *Discover Bank*. *See, e.g.*, *Iskanian v. CLS Transp. Los Angeles, LLC*, 59 Cal. 4th 348, 364 (2014), *cert. denied*, 135 S. Ct. 1155 (2015) ("Under the logic of *Concepcion*, the FAA preempts *Gentry*'s rule against employment class waivers."); *McKenzie Check Advance of Florida, LLC v. Betts*, 112 So. 3d 1176, 1183, 1188 (Fla. 2013) (consumers' claims brought under a variety of consumer protection statutes, all of which permit class actions, nonetheless must be pursued through individual arbitration, per *Concepcion*); *D'Antuono v. Service Rd. Corp.*, 789 F. Supp. 2d 308, 322, 331 (D. Conn. 2011) (pre-*Italian Colors* case that relies on the fundamental principles set forth in (continued...)

ARGUMENT

I

THE PREEMPTED *DISCOVER BANK* RULE HAS NO LEGAL EFFECT ON JUDICIAL CONSTRUCTION OF ARBITRATION CONTRACTS

A. Preempted Common Law Rules Are as Moribund as Preempted Statutes; They May Not Be Resurrected

A state cannot accomplish by common law what it would be forbidden to accomplish by statute. In *Northwest v. Ginsberg*, 134 S. Ct. 1422 (2014), this Court held that a claim for breach of the implied covenant of good faith and fair dealing based on Minnesota state law is preempted by the Airline Deregulation Act because "it seeks to enlarge the contractual obligations that the parties voluntarily adopt." The Airline Deregulation Act's "aim can be undermined just as surely by a state common-law rule as it can by a state statute or regulation." *Id.* at 1430. Parallel to the Federal Arbitration Act's promotion of

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[2] (...continued)
Concepcion to question the continued validity of the Second Circuit case later overruled in *Italian Colors* and holds, "this Court reads the *AT & T Mobility* decision as casting sigificant doubt on virtually *any* 'device [or] formula' which might be a vehicle for 'judicial hostility toward arbitration'") (citing *Concepcion*, 131 S. Ct. at 1747); *Wallace v. Ganley Auto Grp.*, 2011-Ohio-2909 ¶ 19 (Ohio App. 2011) (*Concepcion* demands courts uphold arbitration agreements even when they include statutory consumer protection claims that the state believes should be litigated as class action). That said, California courts continue to go to great lengths to cabin *Concepcion*, as discussed in Section II, *infra.*

the freedom of parties to contract for dispute resolution in the ways that best suits them, the Court noted that the federal policy promoted by the Airline Deregulation Act with regard to frequent flyer programs is to allow the free market to operate. *Id.* at 1433.

Ginsberg followed a long line of cases consistently holding that federal law preempts state law when the state law "interferes with the methods by which the federal statute was designed to reach [its] goal," *International Paper Co. v. Ouellette*, 479 U.S. 481, 494 (1987), whether the state law is rooted in a statute, regulation, or common law rule. *Cipollone v. Liggett Group, Inc.*, 789 F.2d 181, 187 (3d Cir. 1986), *cert. denied*, 479 U.S. 1043 (1987) ("the duties imposed through state common law damage actions have the effect of requirements that are capable of creating 'an obstacle to the accomplishment and execution of the full purposes and objectives of Congress' ") (citation omitted). *See also Taylor v. General Motors Corp.*, 875 F.2d 816, 826 (11th Cir. 1989), *cert. denied*, 494 U.S. 1065 (1990) (The principle of preemption "applies whether the federal law is embodied in a statute or regulation, . . . and whether the state law is rooted in a statute, regulation, or common law rule."); *Abdullah v. American Airlines, Inc.*, 181 F.3d 363, 367 n.4 (3d Cir. 1999) ("State common law rules may be preempted in the same ways as state statutes or regulations.").

In short, the meaning of "state law" in preemption analysis includes not only the positive enactments of a state but also common law rules of liability as determined by state judicial decisions. *Cleveland By and Through Cleveland v. Piper Aircraft Corporation*, 985 F.2d 1438, 1441 (10th Cir. 1993). The reason statutes and common law rules are treated as

equivalent for purposes of preemption analysis is because both reflect public policy and both are intended to govern conduct. *San Diego Building Trades Council, Millmen's Union, Local 2020 v. Garmon*, 359 U.S. 236, 247 (1959) ("[R]egulation can be as effectively exerted through an award of damages as through some form of preventive relief. The obligation to pay compensation . . . is designed to be, a potent method of governing conduct and controlling policy."); *Attocknie v. Carpenter Mfg., Inc.*, 901 P.2d 221, 224 n.3 (Okla. App. 1995) ("[A] successful common-law tort action could have the effect of establishing a safety standard applicable to the same aspect of performance of a motor vehicle or item of motor vehicle equipment as that addressed by a federal standard.").

1. The Meaning and Effect of Preempted State Common Law Rules

The doctrine of federal preemption gives force to the Supremacy Clause of the Constitution by nullifying state laws that conflict with federal law. U.S. Const. art. VI, cl. 2. The very essence of supremacy removes all obstacles to its action within its own sphere, and thereby modifies every power vested in subordinate governments as to exempt federal operations from the states' influence. *Public Utilities Commission of State of Cal. v. U.S.*, 355 U.S. 534, 544 (1958) (citing *McCulloch v. Maryland*, 4 Wheat. 316, 427 (1819)). The meaning and effect of federal preemption has been phrased in a variety of ways, with the common theme that the preempted law or rule or statute is rendered ineffective.

In general, all state provisions that conflict with federal law are "without effect" or, in other words, a

"state statute is void to the extent it conflicts with a federal statute." *Maryland v. Louisiana*, 451 U.S. 725, 746-47 (1981) (citing *McCulloch*, 4 Wheat. at 427; *Hines v. Davidowitz*, 312 U.S. 52 (1941)). The Court applied this "without effect" definition in *Mutual Pharmaceutical Co., Inc. v. Bartlett*, 133 S. Ct. 2466, 2473 (2013). That case did not involve a statute; it involved New Hampshire's application of the common law tort duty to warn. The plaintiff sought to employ the state's "risk-utility approach" to determine whether a product is unreasonably dangerous as designed. *Id.* at 2473. Under the state's approach, a pharmaceutical manufacturer would be required to strengthen the warning on the generic drug at issue in the case. *Id.* at 2475. However, federal law prevents generic drug manufacturers from changing their labels. *Id.* at 2476. "Because it is impossible for Mutual and other similarly situated manufacturers to comply with both state and federal law, New Hampshire's warning-based design-defect cause of action is pre-empted with respect to FDA-approved drugs sold in interstate commerce." *Id.* at 2477 Importantly, the court found no relevance in the fact that the state law was of common law origin, instead of a statute: "In violating a common-law duty, as surely as by violating a statutory duty, a party contravenes the law." *Id.* at 2479. Because the state law duty to warn was preempted, the generic drug manufacturer had no need to alter its warnings to comply with it.

Similarly, some courts explain that a state rule that is preempted is no longer "good law." For example, the Second Circuit explained that federal copyright legislation preempted some state court decisions that relied upon state contract principles in conflict with the legislation, and, as such, those state

contract principles could no longer be considered "good law" on which parties could rely. *Nat'l Basketball Ass'n v. Motorola, Inc.*, 105 F.3d 841, 852 (2d Cir. 1997) ("[M]ost of the broadcast cases relied upon by the NBA are simply not good law. Those cases were decided at a time when simultaneously-recorded broadcasts were not protected under the Copyright Act and when the state law claims they fashioned were not subject to federal preemption.").

Preempted state rules may also be described as "abrogated." In *International Union, United Automobile, Aerospace and Agricultural Implement Workers of America, UAW v. Johnson Controls, Inc.*, 499 U.S. 187 (1991), this Court stated that "we have not hesitated to abrogate state law where satisfied that its enforcement would stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Id.* at 209-10 (internal quotation marks omitted). Abrogate means "To abolish (a law or custom) by formal or authoritative action; to annul or repeal." Black's Law Dictionary (10th ed. 2014); *Northeast Sav., F.A. v. Director, Office of Thrift Supervision*, 770 F. Supp. 19, 23 n.3 (D.C. D.C. 1991) (abrogate means "to repeal, abolish, annul, cancel"); *State v. Hobson*, 218 Wis. 2d 350, 353 n.1 (1998) (same). This Court also used the word "abrogation" in the preemption context in *Farmers Educational and Coop. Union of America, N.D. Div. v. WDAY, Inc.*, 360 U.S. 525, 535 (1959): "[C]auses of action for libel are widely recognized throughout the states. But we have not hesitated to abrogate state law where satisfied that its enforcement would stand 'as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.' " (Citations omitted.). The Ninth Circuit has done so as well, in the context of

federal bankruptcy law. For example, in *In re Schwartz-Tallard*, 765 F.3d 1096, 1102 n.5 (9th Cir. 2014), *reh'g en banc granted*, 774 F.3d 959 (2014), the Ninth Circuit heard an appeal from a Bankruptcy Appellate Panel, and noted that the BAP had relied on a case (*In re Walsh*, 219 B.R. 873 (9th Cir. B.A.P. 1998)) that was rejected in a later case (*Sternberg v. Johnson*, 595 F.3d 937 (9th Cir. 2010)), and that such reliance on the earlier case was "improper." The Circuit panel specifically disclaimed any reliance on the "partially abrogated *Walsh* decision." *See also In re Farmers Markets, Inc.*, 792 F.2d 1400, 1403 (9th Cir. 1986) ("Congress may, within its constitutional limitations, abrogate state law entitlements in bankruptcy pursuant to its Bankruptcy Clause power, U.S. Const. art. I, § 8, cl. 4.").

Most recently, this Court used the word "invalidate" to describe the effect of preemption on a state law. *Oneok, Inc. v. Learjet, Inc.*, 2015 WL 1780926, *4 (U.S. Supreme Ct. Apr. 21, 2015) ("Congress may consequently pre-empt, *i.e.*, invalidate, a state law through federal legislation. It may do so through express language in a statute. But even where, as here, a statute does not refer expressly to pre-emption, Congress may implicitly pre-empt a state law, rule, or other state action.") (citation omitted). A statute that is invalid, for whatever reason, could not be relied upon by either parties to litigation or by a court. *See Schaeffer v. San Diego Yellow Cabs, Inc.*, 462 F.2d 1002, 1006-07 (9th Cir. 1972) (reliance on an invalid state statute is not a defense to a Title VII suit); *King v. Hoke*, 825 F.2d 720, 724 (2d Cir. 1987) (sentencing judge's reliance on repealed sentencing statute is an error of law requiring reversal for resentencing); *Clay v. Permanente Medical Group, Inc.*,

540 F. Supp. 2d 1101, 1109-10 (N.D. Cal. 2007) (arguments fail that rely on older, non-current versions of a statute). This rule extends to the common law. *U.S. v. Sparks*, 711 F.3d 58, 64 n.3 (1st Cir.), *cert. denied*, 134 S. Ct. 204 (2013) (Reliance on a clear and well-defined judicial rule that is later abrogated is analogous to reliance on a subsequently invalidated statute.); *U.S. v. Tejada*, 631 F.3d 614, 619 (2d Cir. 2011) (Court rejected criminal defendant's challenge to his sentence in reliance on Circuit cases that were "abrogated by the Supreme Court's decision in *Abbott v. United States*, 562 U.S. 8 (2010)," because the abrogated cases were of no legal effect.).

2. Other Preempted Common Law Rules and Statutes Are Considered Nullified, Even by California Courts

In *Fidelity Federal Savings & Loan Association v. de la Cuesta*, 458 U.S. 141 (1982), this Court previously considered the relationship between federal preemption and California's common law. The case involved a federal regulation that granted federal savings and loan associations an option to include a due-on-sale clause in loan instruments. *Id.* at 144. When the defendant federal savings and loan association exercised its option to include the clause, three borrowers sued, claiming that the due-on-sale clause was unenforceable under a California common law rule announced in *Wellenkamp v. Bank of America*, 21 Cal. 3d 943 (1978), which held that a due-on-sale clause violates the state's prohibition of unreasonable restrains on alienation. The California Court of Appeal in *de la Cuesta* described this rule as "a substantive rule of California property and mortgage law," not

specifically intended to regulate federal savings and loan associations. *de la Cuesta*, 458 U.S. at 150 (citing *De La Cuesta v. Fidelity Sav. & Loan Ass'n*, 121 Cal. App. 3d 328, 339 (1981)). This Court analyzed the issue as a matter of "conflict" or "obstacle" preemption, as the statute lacked an express provision preempting state law. *Id.* at 153. The fact that a conflict existed was, as in this case, indisputable; the question was how that conflict affected continued application of the state rule.

> The conflict does not evaporate because the Board's regulation simply permits, but does not compel, federal savings and loans to include due-on-sale clauses in their contracts and to enforce those provisions when the security property is transferred. The Board consciously has chosen not to mandate use of due-on-sale clauses "because [it] desires to afford associations the flexibility to accommodate special situations and circumstances." Although compliance with both [the federal regulation] and the [state common law] rule may not be "a physical impossibility," the California courts have forbidden a federal savings and loan to enforce a due-on-sale clause solely "at its option" and have deprived the lender of the "flexibility" given it by the Board.

Id. at 155. (footnote and citations omitted). Therefore, because the state rule limited an "option the Board considers essential to the economic soundness of the thrift industry," the state rule acted as an "obstacle" to the federal regulation and was preempted. *Id.* at 156. As a result, the loan instruments *could* include a due-

on-sale clause, regardless of contrary California common law and policy. *See also Carter v. SSC Odin Operating Co., LLC*, 237 Ill. 2d 30, 39 (2010) ("[S]tate law is null and void if it conflicts with federal law.").

Outside the context of arbitration, California courts acknowledge the invalidating effect of a preemption holding. For example, in *Yarick v. PacifiCare of California*, 179 Cal. App. 4th 1158, 1162 (2009), the California Court of Appeal considered the preemptive effect of the Federal 2003 Medicare Prescription Drug, Improvement and Modernization Act, 42 U.S.C. § 1395w-26(b)(3) (also known as Medicare Advantage), on the plaintiff's state common law claims for negligence, elder abuse, and wrongful death. The plaintiff (decedent's administrator), argued that the financial incentive structure of the Medicare Advantage (MA) statute led the healthcare facilities that cared for the decedent to fail in their duties to exercise due diligence to ensure adequate care, and to establish an ongoing quality assurance program to ensure that healthcare benefits would not be delayed or denied to patients. *Id.* at 1164. The court considered PacifiCare's claims of both express and implied preemption. Some of Yarick's claims were premised on the state statutory standards for HMO organizations, *id.* at 1166, and these were held to be expressly preempted by the federal statute, that is, "superceded," with the result that those "sections cannot supply the standard of care for duties upon the respondent." *Id.* at 1167. "Obstacle" preemption eliminated the rest of Yarick's claims that were based on common law tort duties, rather than alleged violations of state statutes: "If state common law judgments were permitted to impose damages on the basis of these federally approved contracts and quality

assurance programs, the federal authorities would lose control of the regulatory authority that is at the very core of Medicare generally and the MA program specifically." *Id.* at 1167-68. Thus, the state laws were nullified and ineffective for establishing any standard of care with which the defendant had to comply.

In *Akopyan v. Wells Fargo Home Mortgage, Inc.*, 215 Cal. App. 4th 120, 129 (2013), *rev. denied* (Jun. 26, 2013), California residents sought to invoke state contract law and the state's Unfair Competition Law to bring a class action lawsuit against federally regulated loan servicing entities (a national bank and a "thrift institution") for their imposition of certain late fees. The court had to determine whether the plaintiffs' claims were preempted by the Federal National Bank Act (NBA) and Home Owners Loan Act (HOLA). First, the California court determined that federal law intended to occupy the field of lending regulation. *Id.* at 143. The plaintiffs argued, however, that their claims against the thrift were based on generally applicable contract law that should prevail because contract law is preempted from exemption where it only incidentally affects lending operations or is otherwise consistent with the Federal HOLA regulations. *Id.* at 143-44. The court rejected this argument:

> Appellants do not allege a routine breach of contract claim that purports to enforce their basic contract rights under the express terms of the loan agreements. Instead, the effect of implying a state substantive standard on late fees into the loans serviced by Aurora is to limit its ability to service the loans according to their express terms and to

> require that it service them in accordance with the specific state statute that applies to the loans. If this case is any indication, such a claim exposes the federal thrift to the additional expense of litigating which state statutes apply to particular loans, as well as to liability under a variety of state laws specifically regulating loan-related fees. Its effect is thus not to enforce a contractual obligation, but "to open the door to state regulation" of federal thrifts. In its final rule, the [Office of Thrift Supervision] expressly warned against the use of the savings clause to such an end.

Id. at 147. The plaintiffs' claims as to the bank were preempted by the NBA, even though national banks are "subject to state laws of general application" because that rule applies only to the extent that such laws "do not conflict with the letter or the general purposes of the NBA." *Id.* at 156 (citations omitted). The court explained that the breach of contract claim was not a run-of-the-mill application of contract principles because California had multiple late fee statutes, thus exposing Wells Fargo to the "expense and uncertainty of litigating, in the first instance, what statute applies to the loan it services." The California labyrinth of statutes also creates "diverse payment application schemes . . . despite the uniform payment application terms of the mortgages it services." *Id.* at 158. The court held this "inconsistent with the purpose of the NBA to prevent the states from imposing 'diverse and duplicative . . . limitations and restrictions' on its power to engage in the business of banking." *Id.* As such, the preempted California contract law principles were ineffective, that is, they

could not govern the actions of the bank and thrift. *See also Sanchez v. Lindsey Morden Claims Services, Inc.*, 72 Cal. App. 4th 249, 256 (1999), *rev. denied* (Jul. 28, 1999) (an abrogated common law duty is no duty at all).

B. California's *Discover Bank* Rule, Invalidating Class-Action Waivers as "Unconscionable," Can Have No Effect in the Construction of Any Arbitration Contract

The *Concepcion* opinion concludes: "Because it 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress,' California's *Discover Bank* rule is preempted by the FAA." 131 S. Ct. at 1753 (citation omitted). As shown above, common law rules and state statutes are treated identically for purposes of federal preemption analysis. The identical treatment is particularly appropriate for the *Discover Bank* rule, which was written so broadly "that it almost reads like a legislative decree." Alan Scott Rau, *Arbitral Power and the Limits of Contract: The New Trilogy*, 22 Am. Rev. Int'l Arb. 435, 544 (2011). As a tool for analyzing arbitration contracts, the *Discover Bank* rule is a nonentity that the court below never should have invoked.

The Ninth Circuit's reaction to *Concepcion* demonstrates how a court assesses the practical matter of dealing with preempted laws or abrogated cases. For example, in *Ferguson v. Corinthian Colleges, Inc.*, 733 F.3d 928, 937 (9th Cir. 2013), the court of appeals overruled circuit precedent applying the California Supreme Court's anti-arbitration *Broughton-Cruz*

doctrine[3] because the doctrine was preempted by the FAA. In so holding, the Ninth Circuit stated that it was overruling its prior precedent because it "is clearly irreconcilable with subsequent United States Supreme Court decisions concerning the FAA," such as *Concepcion*, *American Exp. Co. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (2013), and others. *Id.* at 934-37.[4] As such, the plaintiffs could not rely on the *Broughton-Cruz* doctrine as any type of authority supporting their claims.

The California courts appear to understand the nullifying effect of a preemption ruling in some circumstances. For example, in *California ARCO Distributors, Inc. v. Atlantic Richfield Co.*, 158 Cal. App. 3d 349, 363 (1984), the appellate court held that a state statute was preempted by a federal law. State courts were therefore forbidden to issue injunctions based on that preempted statute. *Id.* at 363-64. *See also Welton v. City of Los Angeles*, 18 Cal. 3d 497, 507 (1976) (First Amendment case noting that "[a]n

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[3] The doctrine holds arbitration provisions are unenforceable as against public policy if they require arbitration of injunctive relief claims brought for the public's benefit. *Broughton v. Cigna Healthplans of Calif.*, 21 Cal. 4th 1066, 1083-84 (1999); *Cruz v. PacifiCare Health Systems, Inc.*, 30 Cal. 4th 303, 318-19 (2003). The California Supreme Court granted review in *McGill v. CitiBank, N.A.*, 345 P.3d 61 (Cal. 2015), on April 1, 2015, to answer the question of whether the *Broughton-Cruz* doctrine survives *Concepcion*.

[4] Overruling a court's own prior cases is appropriate when a Supreme Court decision "must have undercut the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable." *U.S. v. Bryant*, 769 F.3d 671, 678 (9th Cir. 2014).

injunction based on an unconstitutional [law] exceeds the issuing court's jurisdiction.")).

The fact that the Federal Arbitration Act preempts the *Discover Bank* rule, limiting the scope of state contract law, is not unique. Many federal statutes affect state contract law, rendering their principles and remedies ineffective when they obstruct or otherwise conflict with federal law. For example, federal common and statutory law preempts state principles of contract law for purposes of the interpretation of policies issued pursuant to the National Flood Insurance Act of 1968. *Linder & Associates, Inc. v. Aetna Cas. & Sur. Co.*, 166 F.3d 547, 550 (3d Cir. 1999). Similarly, federal common law preempts state contract law for purposes of collective bargaining interpretation and enforcement. *Local 174, Teamsters, Chauffeurs, Warehousemen & Helpers of Am. v. Lucas Flour Co.*, 369 U.S. 95, 103-04 (1962).

California is not the only state to have common law rules affecting arbitration agreements preempted by the Federal Arbitration Act. For example, New York had required that parties would not be bound to an arbitration contract "in the absence of an express, unequivocal agreement to that effect." *Matter of Marlene Indus. Corp. (Carnac Textiles)*, 45 N.Y.2d 327, 333 (1978). The Second Circuit held that this rule, because it applied only to arbitration contracts, was preempted. *Progressive Casualty Ins. Co. v. C.A. Reaseguradora Nacional De Venezuela*, 991 F.2d 42, 46 (2d Cir. 1993). Subsequent courts interpreting arbitration agreements under New York law disregarded the *Marlene Industries* rule, as it was nullified and had no legal effect. *See, e.g.*, *Huntington Int'l Corp. v. Armstrong World Indus. Inc.*, 981 F.

Supp. 134, 138 (E.D. N.Y. 1997) (applying New York law other than the anti-arbitration *Marlene Industries* rule); *Aceros Prefabricados, S.A. v. TradeArbed, Inc.*, 282 F.3d 92, 100 (2d Cir. 2002) (disregarding effect of *Marlene Industries* when interpreting an arbitration contract).

Pennsylvania unconscionability law, like *Discover Bank*, also served to invalidate otherwise valid arbitration agreements. *Thibodeau v. Comcast Corp.*, 912 A.2d 874, 883-84 (Pa. Super. Ct. 2006) (class action waivers are substantively unconscionable where "class action litigation is the only effective remedy" such as when "the high cost of arbitration compared with the minimal potential value of individual damages denie[s] every plaintiff a meaningful remedy"). *Thibodeau* is now considered preempted by *Concepcion*. In *Quilloin v. Tenet HealthSystem Philadelphia, Inc.*, 673 F.3d 221 (3d Cir. 2012), the Third Circuit explained that it would apply the state law only "to the extent that such law is not displaced" by the Federal Arbitration Act, *id.* at 230, specifically, *Concepcion*. *Id.* at 233 ("The Pennsylvania law is not substantively different from the California law, which is unquestionably preempted by the FAA."). Therefore, although *Thibodeau* would have invalidated the arbitration agreement because it contained a class action waiver, the *Quilloin* court did not find it unconscionable and held that the motion to compel arbitration should have been granted. *Id.* at 235.

Although *Discover Bank* remains in the law books, and may be authority for propositions unrelated to the interpretation of contracts governed by the Federal Arbitration Act, the aspects of its holding preempted by federal law are impotent with regard to the

unconscionability rule invalidated in *Concepcion*. *See First Gibraltar Bank, FSB v. Morales*, 42 F.3d 895, 902 (5th Cir. 1995) ("Because the Texas homestead laws had not been repealed, they were in effect on the date of the Amendment, although they were arguably impotent in the context of federal bank regulation" which preempted the state laws prior to the federal statute's amendment.) (emphasis omitted).

II

CALIFORNIA COURTS MUST NOT ISOLATE THE STATE'S RESIDENTS FROM THE BENEFITS THEY SEEK TO OBTAIN FROM THE FEDERAL ARBITRATION ACT

The decision below continues a collision course upon which California courts have embarked with this Court's decisions regarding FAA preemption. Affirming the decision below would show state courts how to make "end runs" around the FAA and *Concepcion* via applicable state common law. Certainly, California courts have demonstrated marked persistence in light of this Court's decisions such that this Court may anticipate continued recalcitrance.

Since 1984, this Court has been reversing California court decisions that are based on distrust and disapproval of arbitration. *See Southland Corp. v. Keating*, 465 U.S. 1, 5, 7 (1984) (reversing the California Supreme Court's holding that the state Franchise Investment Law required judicial resolution rather than arbitral resolution because "[p]lainly the effect of the judgment of the California court is to nullify a valid contract made by private parties under

which they agreed to submit all contract disputes to final, binding arbitration"); *Perry v. Thomas*, 482 U.S. 483, 491 (1987) (reversing California Court of Appeal decision by holding that the FAA preempts a state labor law authorizing wage collection actions regardless of an agreement to arbitrate: "[U]nder the Supremacy Clause, the state statute must give way."); *Preston*, 552 U.S. at 359 (reversing California Court of Appeal and holding that the FAA's protection of an arbitration agreement vesting jurisdiction over all disputes in an arbitral tribunal supersedes state laws lodging dispute resolution jurisdiction in a different judicial or administrative forum); *Concepcion*, 131 S. Ct. at 1753 (reversing Ninth Circuit application of California's *Discover Bank* rule because "[s]tates cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons"); *see also Sonic-Calabasas A, Inc. v. Moreno*, 132 S. Ct. 496 (2011) (vacating and remanding California Supreme Court decision in *Sonic I*, which categorically forbade waiver of a Berman wage hearing prior to arbitration, for reconsideration in light of *Concepcion*); *CarMax Auto Superstores California, LLC v. Fowler*, 134 S. Ct. 1277 (2014) (vacating and remanding California Court of Appeal decision invalidating an arbitration contract on the "vindication of rights" theory, for reconsideration in light of *Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304 (2013)).

And as demonstrated by this case, each time this Court upholds an arbitration contract because the federal law requires it, California courts find new ways to express their unrelieved hostility to arbitration. *See, e.g.*, *Little v. Auto Stiegler, Inc.*, 29 Cal. 4th 1064, 1095 (2003) (Brown, J., concurring and dissenting) ("[T]his 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.") (citation omitted); *Gentry v. Superior Court*, 42 Cal. 4th 443, 473 (2007) (Baxter, J., dissenting) (noting the California Supreme Court's "continuing effort to limit and restrict the terms of private arbitration agreements, which enjoy special protection under both state and federal law"); *see also James v. Conceptus, Inc.*, 851 F. Supp. 2d 1020, 1036-37 (S.D. Tex. 2012) (applying California law; noting that some California courts, even post-*Concepcion*, continue to find arbitration forum-selection clauses unenforceable as unconscionable, while applying a far less stringent analysis to forum-selection clauses applicable to litigation).

With their continuing hostility to arbitration agreements, California state courts deprive the ability of millions of Californians to take advantage of the benefits of arbitration.

III

CALIFORNIA'S INTRANSIGENCE INFECTS OTHER STATES

Magnifying the problems posed by these challenges to the federal substantive law of arbitration, freedom of contract, and the FAA is the fact that California's hostility to arbitration has considerable potential to influence other states. As a center of economic trade, contracts across the country often provide that California law controls. *See, e.g.*, *Triad Sys. Fin. Corp. v. Stewart's Auto Supply, Inc.*, 47 F. Supp. 2d 1332, 1334 (N.D. Ala. 1999) (Alabama residents bound by contract that made California law

controlling); *Sec. Ins. Co. of Hartford v. TIG Ins. Co.*, 360 F.3d 322, 323 (2d Cir. 2004) (upholding reinsurance agreement that designated California law as controlling); *Naegele v. Albers*, 940 F. Supp. 2d 1, 8-9 (D.D.C. 2013) (relying on California arbitration law and staying federal proceedings); *Phillips Petroleum Co. v. Arco Alaska, Inc.*, No. 7177, 1986 WL 7612, at *6-7 (Del. Ch. July 9, 1986) (parties to oil and gas leases in Prudhoe Bay, Alaska, agreed that California law controlled their arbitration contract).

In addition to choice-of-law language in the contract itself, some courts find California decisions interpreting arbitration contracts persuasive authority when interpreting challenges to arbitration contracts under their own state laws. *See Monarch Consulting, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh*, 2014 WL 4459129, at *10 (N.Y. App. Div. Sept. 11, 2014) (finding persuasive an unpublished California Court of Appeal decision that invalidated an arbitration contract as incompatible with a state regulatory and statutory scheme related to workers' compensation); *Kristian v. Comcast Corp.*, 446 F.3d 25, 60 (1st Cir. 2006) (adopting California approach to unconscionability that prohibited a ban on classwide arbitration); *Brown ex rel. Brown v. Genesis Healthcare Corp.*, 228 W. Va. 646 (2011) (relying, in part, on California case law to invalidate arbitration clause in nursing home contract), *judgment vacated sub nom. Marmet Health Care Ctr., Inc. v. Brown*, 132 S. Ct. 1201 (2012); *see also Episcopal Church in Micronesia v. Chung Kuo Ins. Co., Ltd.*, No. 84-0001, 1985 WL 56588, at *2 (D. Guam June 28, 1985) (Guam's Arbitration Act is patterned after California's statutes and California law on the subject is persuasive, although not binding.); *Discover Bank v. Shea*, 827 A.2d 358, 362 (N.J. Super. Ct. Law

Div. 2001) (noting similarity of New Jersey and California law with respect to arbitration), *app. dismissed*, 827 A.2d 292 (N.J. Super. App. Div. 2003).

Indeed, California's repeated intransigence may serve as inspiration to other state courts that wish to "resurrect" state common law displaced by the FAA, especially other state courts that have made no secret of their disapproval of this Court's FAA jurisprudence. The Massachusetts Supreme Judicial Court's treatment of the consumer arbitration contract in the thrice-considered *Feeney v. Dell Inc.* case provides a salient example. In that case, consumers sued in a purported class action challenging Dell's allegedly improper collection of sales tax on optional computer service contracts for which (according to plaintiffs) no sales tax was actually due. The service contracts included an individual arbitration clause that waived the ability to pursue class relief. In *Feeney v. Dell Inc.*, 454 Mass. 192, 209-10 (2009), the court declined to enforce the class action waiver as a violation of Massachusetts' public policy in favor of class actions for "consumer protection" claims. After this Court decided *Concepcion*, Dell sought and received a rehearing, and the Massachusetts court issued a decision announcing a new reason for invalidating the arbitration contract, holding that *Concepcion* barred a court "from invalidating an arbitration agreement that includes a class action waiver where a plaintiff can demonstrate that he or she effectively cannot pursue a claim against [a] defendant in individual arbitration according to the terms of the agreement, thus rendering his or her claim nonremediable." *Feeney v. Dell Inc.*, 465 Mass. 470, 472 (2013).

Eight days later, this Court rejected that exact rationale in *Italian Colors*, 133 S. Ct. at 2312, n.5 ("[T]he FAA's command to enforce arbitration agreements trumps any interest in ensuring the prosecution of low-value claims."). Issuing its third decision in the case, the Massachusetts court grudgingly acknowledged the demise of *Feeney II*, holding that

> as long as an arbitration agreement does not expressly "forbid[ ] the assertion of certain [Federal] statutory rights" or "perhaps" require the payment of "filing and administrative fees attached to arbitration that are so high as to make access to the forum impracticable," a plaintiff was not deprived of his or her *right to pursue* statutory remedies.

Feeney v. Dell Inc., 466 Mass. 1001, 1002-03 (2013) (citation omitted). With a parting shot at this Court's holdings, the state court bitterly wrote: "Although we regard as untenable the Supreme Court's view . . . we are bound to accept that view as a controlling statement of Federal law." *Id.* at 1003. Even so, the court remanded the case to give the plaintiffs yet another chance to come up with "alternative grounds" to invalidate the contract. *Id.*

If this Court permits the California end-run to stand, Massachusetts and other arbitration-hostile jurisdictions will look to the decision below as a blueprint to avoid this reach of the Federal Arbitration Act and the federal substantive law of arbitration's commitment to freedom of contract.

CONCLUSION

The judgment of the California Court of Appeal should be reversed.

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Respectfully submitted,

DEBORAH J. LA FETRA
Counsel of Record
Pacific Legal Foundation
930 G Street
Sacramento, California 95814
Telephone: (916) 419-7111
Facsimile: (916) 419-7747
E-mail: dlafetra@pacificlegal.org

Counsel for Amicus Curiae Pacific Legal Foundation