

RECENT DEVELOPMENTS IN ARBITRATION & MEDIATION LAW

A Review of Recent Cases, Statutes and Rules Affecting the Practice of Mediation, Arbitration and Settlement Negotiation for Attorneys Practicing in Southern California

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I.

ARBITRATION – SIGNIFICANT CASES

A. ARBITRATOR DISQUALIFICATION – REQUIRED DISCLOSURES AND EVIDENT PARTIALITY

(1) Background Statement re Federal Disclosure Standard

The Federal Arbitration Act (“FAA”) does not specifically address the matter of pre-appointment disclosure by arbitrators or arbitrator disqualification. Instead, at the back end of the process, the FAA provides generally that an award may be vacated when an arbitrator has failed to disclose an interest or relationship that amounts to “evident partiality,”¹ meaning that such circumstance might affect impartiality or create an appearance of partiality. The details of what constitutes a required disclosure is a matter of case law, and starts with the United States Supreme Court’s 1968 decision in *Commonwealth Coatings Corp. v. Continental Casualty Co.*²

In *Commonwealth Coatings*, the arbitrator was a leading and respected consulting engineer who had performed services for most of the prime contractors in Puerto Rico, where the project and dispute were venued. The arbitrator was well known to the subcontractor’s counsel and they were personal friends.³ While the subcontractor’s counsel knew the arbitrator and knew of his reputation and business ties in the community, he was not aware of the fact that the arbitrator had performed services for the prime contractor whose bond was in issue, and that fact was not made known to claimant by the arbitrator or anyone else until after the award had been made. It is not clear from the facts whether the personal ties between the arbitrator and the subcontractor’s counsel were disclosed to the contractor or his counsel. However, when the award came out against the subcontractor and in favor of the contractor, the subcontractor complained that the arbitrator’s undisclosed, past business relationship with the prime contractor created an impression of bias. The district court refused to set aside the award because there was no charge that the arbitrator was guilty of fraud or actual bias in deciding the case. The court of appeal affirmed.

¹ 9 U.S.C. § 10(a)(2).

² 393 U.S. 145 (1968).

³ Id. at 152-153.

On further review by the United States Supreme Court, the confirmation of the award was reversed and the award vacated. In *Commonwealth Coatings*, the Supreme Court held that a party seeking to vacate an arbitration award for evident partiality need not show that the arbitrator “was actually guilty of fraud or bias in deciding th[e] case;”⁴ that “evident partiality” is distinct from actual bias. The Court held that the arbitrator’s failure to “disclose to the parties any dealings that might create an impression of possible bias” is sufficient to support vacatur.”⁵ The Court found this standard was satisfied where a neutral arbitrator in a dispute between a contractor and subcontractor failed to disclose that he had previously performed consulting work worth about \$12,000 for the contractor. Although “there had been no dealings between them for about a year immediately preceding the arbitration,” the arbitrator’s past relationship with the contractor had included irregular contacts “over a period of four of five years” and had gone “so far as to include the rendering of services on the very projects involved in th[e] lawsuit.”⁶ While the Court recognized “that arbitrators cannot sever all their ties with the business world,” it emphasized that because arbitrators “have completely free rein to decide the law as well as the facts and are not subject to appellate review,” courts must “be even more scrupulous to safeguard the[ir] impartiality.”⁷

What qualifies as a matter creating an impression of possible bias is a fact-driven inquiry. As a result the landscape is populated with cases where the courts have conducted their own case-by-case factual analysis to determine whether an undisclosed relationship rises to the level of a conflict sufficient to create an impression of possible bias and thus support vacatur. There is thus no “bright line” test. For example, in *Woods v. Saturn Distribution Corp.*,⁸ the Ninth Circuit refused to vacate the award rendered by an arbitration panel consisting of Saturn employees and dealers notwithstanding a charge of “evident bias” because the parties’ pre-dispute agreement provided for Saturn’s dispute resolution process to be the one utilized by the parties. That process was expressly described as one in which both mediation and binding arbitration would be conducted by a panel of two Saturn dealers and two Saturn employees, randomly selected from a pool of volunteers consisting of ten Saturn dealers and ten Saturn employees.

⁴ Id. at 147.

⁵ Id. at 149.

⁶ Id. at 146.

⁷ Id. at 148-149.

⁸ 78 F.3d 424 (9th Cir. 1996), cert. dismissed, 518 U.S. 1051 (1996).

In contrast, in *Schmitz v. Zilveti*,⁹ the Ninth Circuit vacated an award for evident partiality where the arbitrator's law firm had represented the parent company of a party "in at least nineteen cases during a period of 35 years" with the most recent representation ending less than two years before the arbitration was submitted.¹⁰ The Ninth Circuit disagreed with the district court's conclusion that evident partiality could not be shown because the arbitrator did not have actual knowledge of his law firm's conflict during the arbitration.¹¹ Based on *Commonwealth Coatings*, the court concluded that the standard for evident partiality is whether there are "facts showing a 'reasonable impression of partiality.'"¹² The court explained that this standard can be satisfied even where an arbitrator is unaware of the facts showing a reasonable impression of partiality because the arbitrator "may have a duty to investigate independent of [his] . . . duty to disclose."¹³

In further contrast, in the Ninth Circuit's recent decision in *Lagstein v. Certain Underwriters at Lloyds, London*,¹⁴ the court seems to have limited required arbitrator disclosures to relationships and dealings with the current arbitration participants. In *Lagstein*, a three-arbitrator panel concluded that Lloyds had breached an insurance contract and acted unreasonably with regard to the handling of the insured's claims, but the panel split on the amount of damages to be awarded. The majority concluded that Lagstein (the insured) should be awarded the full value of his policy (\$900,000), plus \$1.5 Million for emotional distress. The dissenting arbitrator would have awarded Lagstein only \$11,000 and would not have awarded emotional distress damages. Subsequent to the initial award, proceedings were held on request for punitive damages. Again, the majority awarded Lagstein punitive damages in the amount of \$4 Million, whereas the dissenting arbitrator argued that the panel lacked jurisdiction and, even if it had jurisdiction, the award should be limited to \$50,000. Following the panel's awards, Lloyds investigated the backgrounds of the arbitrators and discovered that the arbitrators forming the majority had been involved in an ethics controversy over a decade earlier. Lloyds then filed a motion to vacate the arbitration award on several grounds, including the arbitrators' failure to disclose their involvement in the prior ethics controversy. The district court granted vacatur, but not on the ground of "evident partiality" resulting from the majority arbitrators' failure to disclose the ethics controversy. On appeal, the district court's vacatur was reversed and remanded with instructions. However, with regard to the "evident partiality" challenge, the Ninth

⁹ 20 F.3d 1043 (9th Cir. 1994).

¹⁰ Id. at 1044.

¹¹ Id.

¹² Id. at 1048.

¹³ Id.

¹⁴ 607 F.3d 634 (9th Cir. 2010), cert. den., ___ U.S. ___, 131 S.Ct. 832 (2010).

Circuit agreed with the district court that Lloyds did not establish the existence of “an inappropriate relationship or contact” between the two arbitrators or a failure to disclose “information that would warrant vacating the award.”¹⁵ To show “evident partiality” in an arbitrator, the court held that the moving party “must establish specific facts indicating actual bias toward or against a party or show that [the arbitrator] failed to disclose to the parties information that creates ‘[a] reasonable impression of bias.’”¹⁶ Vacatur of an arbitration award is not required under Section 10(a)(2) of the FAA simply because an arbitrator fails to disclose a matter that might be of some interest to a party. Instead, an arbitrator is required to disclose “only facts indicating that he ‘might reasonably be thought biased against one litigant and favorable to another.’”¹⁷ Here, the Ninth Circuit found that Lloyds failed to show any connection between the parties to the present arbitration and any of the majority arbitrator’s past difficulties that would give rise to a reasonable impression of partiality toward Lagstein. Indeed, the court found that the majority arbitrator’s alleged misconduct occurred more than a decade before the subject arbitration and concerned neither of the parties to the current case.¹⁸

An example of what qualifies on a “nontrivial conflict of interest” justifying vacatur for “evident partiality” can be found in the Ninth Circuit’s decision in *New Regency Productions, Inc. v. Nippon Herald Films, Inc.*¹⁹ In this case, a film distribution company and film production company agreed to arbitrate a dispute concerning their respective rights and obligations under a film distribution agreement. After conducting six days of hearing, the arbitrator decided that Nippon was entitled to return of the \$440,000 fee it had paid New Regency for an undelivered film and New Regency was entitled to \$2,341,257 from Nippon as its interest in the proceeds of a recoupment pool. When New Regency moved to confirm the award, Nippon objected and sought vacatur on several grounds, including the arbitrator’s failure to disclose the fact that between the time of the last evidentiary hearing date and the issuance of his award, the arbitrator took a new job as a high-level executive with a film group that was in negotiations with one of the parties (New Regency) to finance and co-produce a major motion picture. The district court granted vacatur and the Ninth Circuit affirmed that decision. With regard to the challenge made under Section 10(a)(2) of the FAA, the Ninth Circuit concluded that the arbitrator had a duty to investigate potential conflicts

¹⁵ Id. at 645.

¹⁶ Id. at 645-646, citing *Woods v. Saturn Distribution Corp.*, supra, 78 F.3d 424, 427.

¹⁷ Id. at 646, citing *Commonwealth Coatings*, supra, 393 U.S. 145, 150.

¹⁸ Id., citing *Paine-Webber Group, Inc. v. Zinsmeyer Trusts P’ship*, 187 F.3d 988, 995 (9th Cir. 1999) (characterizing a claim of evident partiality as “border[ing] on frivolous” where there was no alleged relationship between the parties and the arbitrators, and “there [was] no evidence th arbitrators had any financial or personal interest in the outcome of the arbitration”).

¹⁹ 501 F.3d 1101 (9th Cir. 2007)

when he accepted the high-level executive position while the arbitration was ongoing; that the parties could reasonably have expected the arbitrator to investigate potential conflict when, during the pendency of the arbitration, he took a job in which his duties included overseeing the legal department of another film company. In this regard, the court stated that it believe that the arbitrator's decision to accept a new, high-level executive job at a company in the same industry as the parties was precisely the type of situation where an arbitrator should have reason to believe that a nontrivial conflict of interest might exist and should investigate to determine the existence of potential conflicts. As it turned out, the conflict alleged by Nippon was quite real because the connection between the arbitrator's new employer and New Regency was not attenuated, and because of the high-profile nature of the film project in question, the court could not conclude that the negotiation between the two companies was unimportant to the arbitrator's new employer. Moreover, the negotiation between New Regency and the arbitrator's new employer was not distant in time, but rather ongoing during the arbitration.²⁰

The federal cases discussed in Section 3, below, are some recent examples of the fact situations the federal courts have been presented with for purposes of defining (a) under what circumstances an arbitrator has an affirmative duty to undertake an investigation for possible conflicts, and (b) what types of relationships and/or interests must be disclosed on penalty of vacatur for "evident partiality" if the arbitrator fails to do so. What is clear in the Ninth Circuit, however, is that to establish "evident partiality," bald allegations of partiality are not enough; the moving party must present evidence to support this claim.²¹

(2) Background Statement re California Disclosure Standard

In 1961, California adopted the Uniform Arbitration Act. As originally enacted, there were no specific disclosure requirements imposed upon neutral arbitrators. In 1994, California enacted Code of Civil Procedure § 1281.9 to require specific arbitrator disclosures. As originally enacted, the disclosure requirements were relatively narrow, requiring only disclosure of information concerning prior arbitrations in which the arbitrator had served as a neutral or party arbitrator involving the parties or lawyers to the current arbitration. In 1997, Section 1281.9 was amended to expand those disclosure requirements to include any current or historical attorney-client relationship between the arbitrator and any party or lawyer to the current arbitration and any current or historical professional or significant personal relationships between the arbitrator, his or her spouse,

²⁰ Id. at 1110-1111.

²¹ See, *Ventress v. Japan Airlines*, 603 F.3d 676, 679-680 (9th Cir. 2010)

or minor child living in the household, on the one hand, and any party or lawyer to the current arbitration. In September 2001, Section 1281.9 was amended again and Sections 1281.85 and 1281.91 were added.

Under new Code of Civil Procedure § 1281.85, the Legislature delegated to the California Judicial Council authority and responsibility for adopting mandatory ethical standards for all individuals serving as neutral arbitrators in contractual arbitrations held in California. Pursuant to this mandate, the Judicial Council adopted the “Ethics Standards for Neutral Arbitrators in Contractual Arbitration” originally codified in Division VI of the Appendix to the California Rules of Court and now found in the end of the California Rules of Court following Title 10 (Judicial Administration Rules) and the Standards for Judicial Administration. The statutory disclosure requirements set forth in Section 1281.9 incorporate the Ethics Standards as being among a private arbitrator’s mandatory disclosure obligations. Under the Ethics Rules, arbitrators have a continuing duty to inform themselves about matters that need to be disclosed and to make all required disclosures from the time of appointment through the close of the arbitration. If something arises in the course of an arbitration that triggers a supplemental disclosure obligation, the arbitrator must make the required disclosures within 10 calendar days, and that disclosure will renew the parties’ disqualification rights discussed below.

Because private arbitration is a matter of agreement between the parties to the dispute, an arbitrator must withdraw if all parties request the arbitrator to do so. If only one party objects to the arbitrator in an administered arbitration, the general practice was to leave the determination of challenges to an arbitrator’s appointment to the provider institution (*e.g.*, AAA, JAMS, CPR) in accordance with their rules. In a non-administered (*ad hoc*) arbitration in which no specific institutional rules apply, the general practice recommended by the AAA / ABA Code was for the arbitrator to determine whether the reason for the challenge is “substantial” and, if so, to then determine whether he or she “can nevertheless act and decide the case impartially and fairly.” Under California law, disqualification based upon an arbitrator’s disclosures is an absolute right of the parties; it is not subject to review or determination by the provider institution or other higher outside authority.²² Under Code of Civil Procedure § 1281.91(b), disqualification is mandatory;

²² See, *Azteca Construction, Inc. v. ADR Consulting, Inc.*, 121 Cal. App. 4th 1156, 1163 (2004); *Ovitz v. Schulman*, 133 Cal. App. 4th 830, 840 (2005). The Court of Appeal in *Azteca* found that the provisions of the California Arbitration Act relating to arbitrator disqualification could not be waived because they were “enacted primarily for a public purpose.” In this regard, the Court of Appeal found that the procedural rules of the provider institution (AAA) “must yield to the disqualification scheme set forth in sections 1281.9 and 1281.91, for a number of reasons.” Among those reasons were the findings that (a) the neutrality of the arbitrator is of crucial

operates as a peremptory challenge; and takes effect when a party timely serves a notice of disqualification.

Under Section 1281.91(b), there is no limit on the number of times a party may challenge a proposed arbitrator. For the recalcitrant party trying to avoid binding arbitration, an obvious tactic would be to serve a notice of disqualification within 15 days of each proposed arbitrator's disclosures. The only way to limit the number of peremptory challenges a party may assert is by seeking court intervention via a motion that asks the court to appoint the arbitrator as provided by Code of Civil Procedure § 1281.91. Section 1281.91(a)(2) then provides that a party shall have the right to disqualify one court-appointed arbitrator without cause in any single arbitration and, beyond that, may petition the court to disqualify a subsequent appointee "only upon a showing of cause."

Code of Civil Procedure § 1286.2 provides the "strong-arm" mechanism for enforcing arbitrator disclosures – namely, vacatur. As amended, Section 1286.2 mandates that a court "shall" vacate an arbitration award if the arbitrator making the award (a) failed to disclose a ground for disqualification of which the arbitrator was aware, or (b) was subject to disqualification upon grounds specified in CCP Section 1281.9 but failed to disqualify himself or herself after receipt of a timely notice of disqualification. At least one court has commented that, on its face, "the statute leaves no room for discretion. If a statutory ground vacating an award exists, the trial court must vacate the award."²³

Despite the breadth and detail of the Ethics Rules, the California Supreme Court has previously made clear that the disclosure requirements are intended to ensure the impartiality of the arbitrator, not mandate disclosure of "all matters that a party might wish to consider in deciding whether to oppose or accept the selection of an arbitrator." *Haworth v. Superior Court* (2010) 50 Cal. 4th 372. And one court of appeal has construed the Ethics Rules such that "'ordinary and insubstantial business' arising from participation in the business or legal community do not necessarily require disclosure." *Luce, Forward, Hamilton & Scripps, LLP v. Koch* (2008) 162 Cal. App. 4th 720, 723, quoting *Guseinov v. Burns* (2006) 145 Cal. App. 4th 944, 959.

importance to the private arbitration process and (b) the California Supreme Court's recognition that arbitrator neutrality is "essential to ensuring the integrity of the arbitration process." 121 Cal. App. 4th at 1168, citing *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal. 4th 83, 103 (2000).

²³ See, *Ovitz v. Schulman*, supra, 133 Cal. App. 4th at 845; accord, *International Alliance of Theatrical Stage Employees, etc. v. Loughon*, 118 Cal. App. 4th 1380, 1386 (2004).

Whether operating under California or state law, it is a universal principal of arbitrator ethics that arbitrators have a duty to disclose meaningful relationships with the parties, counsel and/or subject matter of the cases to which they are assigned. There is considerable gray area and no clear definition of what is “ordinary and insubstantial” and what is a meaningful business or personal relationship or life experience that should be disclosed. Unfortunately, the consequence of an arbitrator’s failure to make a required disclosure is vacatur, which undermines the efficiency, economy and finality promised by arbitration. The state court cases discussed in Section 3, below, are recent decisions that continue the discussion/dissection of what is a required disclosure under California law and what circumstances give rise to arbitrator disqualification because they could cause a person aware of the facts to reasonably entertain a doubt that the proposed neutral arbitrator would be able to be impartial.

(3) Cases

(a) An Arbitrator’s Membership in Professional Groups and Participation on Bar Association Panels or Committees are not Required Disclosures or Disqualifying Relationships - *Nemecek & Cole v. Horn*, 208 Cal. App. 4th 641 (2nd Dist., Jul. 23, 2012)

After losing at arbitration in a an attorney malpractice case, the claimant hired a private investigator to determine whether there existed any undisclosed relationships between the arbitrator and the attorney/law firm respondents and their expert witness. The private investigator discovered the following: the arbitrator and one of the attorneys at the respondent law firm were both members of a 186-member committee of an L.A. County Bar Association section; the arbitrator had served on the executive board of the L.A. County Bar Association while respondents’ expert was its president; the arbitrator and respondents’ expert had appeared together as panelists for an ABTLA seminar; attorneys from the respondent law firm had appeared before the arbitrator when he was sitting as a district court judge; and the arbitrator was of counsel to a private law firm that had previously represented clients in the area of legal malpractice. When respondents petitioned to confirm the arbitration award, claimant opposed confirmation and moved to vacate the award on the ground that the arbitrator had failed to make required disclosures, specifically focusing on the required disclosure of (a) any “significant personal relationship,” Code of Civil Procedure § 1281.9(a)(6), and (b) other “interests, relationships, or affiliations” and “common matters that could cause a person aware of the facts to reasonably entertain a doubt that the arbitrator would be able to be impartial.” Ethics Rules, std. 7(d)(13). The trial court confirmed the award and claimant appealed. The Second District for the Court of Appeal affirmed, holding that the professional affiliations the arbitrator shared with respondents or their expert

was in the realm of “slight or attenuated” because there was no indication that the arbitrator had a personal relationship, or close friendship, with either the respondents or their expert. Further, there was no indication of any business relationship between or among them. The Court of Appeal further held that the arbitrator’s participation in panels or bar association committees was not a required disclosure item because it “does not provide a credible basis for inferring an impression of bias.” The court also held that no impression of bias could be inferred from the act that the arbitrator’s firm had represented attorneys in malpractice actions because the firm does not devote its practice to legal malpractice defense and had only represented a defendant (other than itself) in one matter and the arbitrator did not work on that matter. Finally, the court held that it bordered on frivolous for claimant to suggest that the arbitrator was biased because a member of respondent’s firm had appeared before him when he was on the bench.

**(b) Attorney’s Membership on the Same Provider Panel
as the Arbitrator was a Required Disclosure - *Gray*
v. Chiu, 2013 WL222279 (2nd Dist., Jan. 22, 2013).**

For many years, William Ginsburg represented Dr. Chiu. In 2009, Dr. Chiu and others were sued for medical malpractice. Ginsburg, in his of counsel capacity with Peterson Bradford Burkwitz, acted as the lead trial attorney for the defense team. The trial court granted defendant’s motion to compel arbitration before a three-member panel, consisting of two party arbitrators and a neutral arbitrator selected by the party arbitrators. After the matter was ordered to arbitration, Ginsburg retired from the Peterson Bradford firm and became an arbitrator/mediator associated with ADR Services. While he was no longer lead trial counsel for the defense, Ginsburg continued to represent Dr. Chiu as his personal attorney. After Ginsburg retired and became affiliated with ADR Services, the two party arbitrators selected the neutral arbitrator from the ADR Services panel (the Honorable Alan Haber (Ret.)). In his disclosures to the parties, Judge Haber stated that he had no significant personal relationship or other professional relationship with any party, or lawyer for a party. Judge Haber’s disclosures listed the names of the participants and attorneys for whom a conflict check was performed and did not include Ginsburg. The arbitration took place at the ADR Services office over nine working days and Ginsburg attended all of the sessions as personal counsel for Dr. Chiu. Judge Haber did not supplement his disclosures concerning Ginsburg and ultimately determined the matter in favor of the defendants. Plaintiff filed a petition to vacate the award on several grounds, including the failure of Judge Haber to disclose that Ginsburg was a member of the ADR Services panel. The trial court denied plaintiff’s vacatur request and entered judgment for defendants. Plaintiff appealed.

On appeal, the Second District Court of Appeal reversed the trial court, finding that the arbitrator failed to make disclosures required under Standard 8 of the Ethics Rules. Standard 8 imposes specific disclosure obligations upon arbitrators in “consumer arbitrations,” which is defined as an arbitration conducted under a predispute arbitration contract where the consumer party was required to accept the arbitration provision in the contract as a condition to receiving goods or services. Standard 8 (A) expressly requires the arbitrator to disclose if a party, a lawyer in the arbitration, or a law firm with which a lawyer in the arbitration is currently associated is a member of the provider organization. As such, the court of appeal concluded that “[t]he plain language of Ethics Standard 8 compels the arbitrator to disclose that a lawyer in the arbitration is a member of the administering DRPO.” The court of appeal rejected respondents’ estoppel/waiver argument to the effect that plaintiff knew or should have known of Ginsburg’s association with ADR Services because that argument assumed that someone other than the neutral arbitrator can effectively disclose the membership of a participating lawyer in the administering provider organization. The court held that Standard 8 requires that the neutral arbitrator make the disclosure, the only exception being if the provider organization makes the disclosure concerning the affiliation, which did not occur in this case.

(c) California’s General Arbitrator Disclosure Obligations are not Applicable to Arbitrators in International Commercial Arbitrations – *Comerica v. Howsam*, 208 Cal. App. 4th 790 (2nd Dist., Aug. 20, 2012)

In 2004, Comerica made loans totaling \$37 million to seven Canadian corporations and their principal, also a resident of Canada. The procedural history was quite complex and involved a criminal indictment, proceedings in an arbitral forum, proceedings in a trial court, and cert petitions to both the California and United States Supreme Courts (both denied). The Los Angeles Superior Court granted a motion to compel arbitration and later confirmed three arbitral awards against borrowers, as well as a sanctions award against borrowers’ counsel over the objections and request for vacatur made by borrowers and their counsel. On appeal, defendants argued that the awards must be vacated under CCP § 1286.2(a)(6)(A) and (B) due to the arbitrator’s failure to make a required disclosure under CCP § 1281.9 and his failure to disqualify himself upon receipt of a timely demand. The Second District Court of Appeal affirmed the trial court and held that the general disclosure obligations governing arbitrators in private commercial arbitrations do not apply to international commercial arbitration and thus a disclosure violation under those general rules is not a ground for vacatur of an international commercial arbitration award. In this regard, the court of appeal noted that an arbitrator’s disclosure duties under California’s

international commercial arbitration statutes materially differs from those applicable to domestic arbitration disputes. 208 Cal. App. 4th at 818, citing CCP § 1297.17 (“this title supersedes Sections 1280 to 1284.2 . . . with respect to international commercial arbitration and conciliation.”).

The disclosure requirements for arbitrators in international commercial disputes are set forth in CCP §§ 1297.121 through 1297.125. Significantly, unlike CCP § 1281.91 which provides that an arbitrator “shall be disqualified” upon the issuance of a party’s timely notice of disqualification, in international commercial arbitrations, the arbitral tribunal reviews the challenge and decides whether to disqualify the arbitrator. Cal. Code Civ. Proc. § 1297.133. If the challenge is not successful, the challenging party may request the superior court to disqualify the arbitrator. Cal. Code of Civ. Proc. § 1297.134. The decision of the superior court is final and not subject to appeal. Cal. Code of Civ. Proc. § 1297.135.

(d) The Fact that Arbitrator Sometimes Represented Investors Against Their Brokers was not Sufficient to Show “Evident Partiality” Under Section 10(a)(2) of the FAA – *Keegan & Co., Inc. v. Grant*, 2012 WL 5350949 (9th Cir., Oct. 25, 2012) (unreported decision)

Securities broker moved to vacate an arbitration award in favor of the investor on several grounds, including “evident partiality” under Section 10(a)(2) of the FAA. That motion was denied by the district court and affirmed by the Ninth Circuit. The broker complained that the arbitrator was biased in favor of investors because he sometimes represented investors against their brokers. The court held that that fact alone was not sufficient to show that the arbitrator had failed to disclose information that would create a reasonable impression of possible bias because as part of the pre-appointment process, the arbitrator had made disclosures about the investor representation aspect of his practice and there was no evidence that the disclosures he had made were inaccurate. In so ruling, the Ninth Circuit noted that while the district court’s decision to vacate or confirm an arbitration award is reviewed de novo, that review is nevertheless “limited and highly deferential.” *2, citing *Coutee v. Barington Capital Group*, 336 F.3d 1128, 1132 (9th Cir. 2003).

(e) **An Example of Strategic Gamesmanship in Arbitration Gone Awry – *Thomas Kinkade Company v. White*, ___ F.3d ___, 2013 WL 1296238 (6th Cir., Apr. 2, 2013)**

Against the backdrop of a tortured set of facts representing the penultimate in gamesmanship aimed currying the arbitrator's favor, the serious issue of "evident partiality" was missed by both the arbitrator and the provider organization, and thus had to be corrected by the courts.

The case involved a dispute between the Thomas Kinkade Company and one of its dealers. The company claimed that the dealers had not paid for artwork worth hundreds of thousands of dollars, and the dealers counterclaimed that they had been fraudulently induced to enter into the dealer agreements with the company. The entire case is worth a read because it presents "a model of how not to conduct [an arbitration]." 2013 WL 1296238, *1. However, looking only at the evident partiality aspect of the case, the facts were these: After nearly 5 years and 50 days of hearing (with the arbitration still not complete), the dealers and persons associated with the dealers began showering the arbitrator's law firm with new business directed to various of the arbitrator's partners on matters where the fees for the engagements were expected to be substantial. The arbitrator disclosed the fact of these engagements to the parties. The company objected to these concurrent engagements in a letter directed to the provider organization (the AAA). The arbitrator was re-confirmed after his partner declined one representation and the partner on the other representation left the firm. The AAA directed counsel not to copy the arbitrator on any of the objection paperwork, which instruction the dealer's attorney ignored by sending an email to the arbitrator in which he told the arbitrator that he had been "re-confirmed," thus opening the door for the arbitrator to surmise that the Company had objected to the arbitrator's firm's - engagements with the dealers and the related persons. Consequently, the Company filed a motion with the AAA seeking to disqualify the arbitrator outright, which the AAA denied. The Company then submitted a demand for disqualification directly to the arbitrator, which he in turn denied. The arbitrator then proceeded to continue with the arbitration in a manner that allowed the dealers several opportunities to correct errors and put documents into evidence they had failed to exchange as ordered. Ultimately, to no one's surprise, the arbitrator issued an award in favor of the dealers that exceeded \$1.4 Million. Also to no one's surprise, the company immediately filed a motion seeking to vacate said award under Section 10(a)(2) of the FAA. The district court granted that motion and the Sixth Circuit affirmed.

In vacating the award, the Sixth Circuit held that the company had established “a convergence of undisputed facts that, considered together, show a motive for [the arbitrator] to favor the [dealers] and multiple concrete actions in which he appeared actually to favor them. To begin with the motive: nearly five years into this arbitration, and in the space of eight weeks, the purportedly neutral arbitrator’s law firm – of all the law firms that practice commercial litigation in Michigan – was hired by one party’s arbitrator-advocate . . . and then again by that same party . . . for engagements that by all appearances would be substantial.” 2013 WL 1296238, *5. On the issue of the arbitrator’s disclosure of the engagements to the parties, the Sixth Circuit noted that the district court’s opinion “was particularly thoughtful.”

“One major benefit of arbitration is that it allows parties to exercise some control over who will resolve their disputes. . . . Disclosures at the outset of an arbitration allow a party to reject an arbitrator as ethically encumbered as [the arbitrator] was here; and [the company] obviously would have rejected [the arbitrator] out of hand if [the dealer] had hired [the arbitrator’s] firm just prior to this arbitration rather than five years in. thus, we entirely agree with the district court that, ‘[w]hen the neutral arbitrator engages in or attempts to engage in mid-arbitration business relationships with non-neutral participants, it jeopardizes what is supposed to be a party-structured dispute resolution process.”

Id.

What also appears to have swayed the Sixth Circuit was the “dilemma” the arbitrator’s mid-arbitration disclosures created for the company. Quoting from the company’s objection submitted to the AAA:

“[O]nce the disclosure was made the harm was done regardless of the outcome. The disclosure put our clients in the awkward position fo either objecting to or appearing to approve the representation by the neutral arbitrator’s firm of a party adverse to our client in another arbitration. If we object, we run the risk of offending the neutral; if we don’t object, we appear to condone a clear conflict. We should never have been put in this position.”

Id. The Sixth Circuit then concluded that a party who has paid a neutral arbitrator to prepare for and then sit through nearly 50 days of hearings over a five-year period, “deserves better treatment than this.” Id. at *6.

B. CLASS ACTION ARBITRATION – THE STATUS OF EXPRESS WAIVERS AND CONTRACT SILENCE

(1) Background Statement

The United States Supreme Court has said that consent to class arbitration may not be “read into” agreements covered by the Federal Arbitration Act because requiring class arbitration on a nonconsensual basis would interfere with the Congressional intent behind the Federal Arbitration Act (FAA). *Stolt-Nielsen v. AnimalFeeds Int’l Corp.* (2010) 130 S.Ct. 1262 (2010). If an arbitration agreement is silent on whether a class arbitration can be brought under its terms, and there is no evidence that the parties intended to include class actions in the agreement, then a party may not be compelled under the FAA to submit to class arbitration. In 2011, the Supreme Court expanded on the *Stolt-Nielsen* decision and held that the FAA’s overarching purpose is to “ensure the enforcement of arbitration agreements according to their terms.” *AT & T Mobility LLC v. Concepcion* (2011) 131 S.Ct. 1740. The arbitration agreement in that case included a class-action waiver in that it required the parties to arbitrate only in their “individual capacity, and not as a plaintiff or class member in any purported class or representative proceeding.” The arbitration agreement also prohibited the arbitrator from consolidating the claims of more than one person, or from presiding over any form of representative of class proceeding.

The majority of federal appeals court and district court decisions have followed *Concepcion*.²⁴ There is uncertainty, however, in California. In *Brown v. Ralph’s Grocery, Inc.* (2011) 197 Cal. App. 4th 489, the Second District Court of Appeal held that *Concepcion* did not apply to “representative actions” brought under the California Private Attorneys General Act and suggested that the four-factor test established by *Gentry v. Superior Court* (2007) 42 Cal. App. 4th 443.²⁵ That being said, the *Brown* majority

²⁴ See, e.g., *Cruz v. Cingular Wireless LLC*, 648 F.3d 1205 (11th Cir. 2011) (the FAA preempts a remedial consumer statute on the same grounds that it preempts *Discover Bank*); *Litman v. Celco Partnership*, 655 F.3d 225 (3rd Cir. 2011) (New Jersey law requiring the availability of class wide arbitration “creates a scheme inconsistent with the FAA” and therefore the district court properly enforced the class arbitration waiver by compelling individual arbitration); *Green v. Super Shuttle Int’l, Inc.*, 653 F.3d 766 (8th Cir. 2011) (in a class action alleging violations of Minnesota’s overtime law, the court held that the *Concepcion* decision foreclosed a state law challenged to the enforcement of class action waivers).

²⁵ *Gentry* held that if a trial court concluded – based on its four-factor test – that class arbitration is “likely to be a significantly more effective practical means of vindicating the rights of affected employees than individual litigation or arbitration,” and that there would be “less

did not reach the issue regarding the invalidity of the class action waiver because it found that the plaintiff had failed to satisfy *Gentry*'s four-factor test. While the California Supreme Court has not (yet) revisited *Gentry* in the wake of the *Concepcion* decision, California federal courts have held that *Concepcion* overruled *Gentry*.²⁶ And two other federal district courts have questioned the *Brown* court's holding that the right to bring a representative action under PAGA cannot be waived in an arbitration agreement.²⁷

The cases discussed in this section represent further California court of appeal decisions on the topic of class arbitration in the face of contract silence or an express waiver.

(2) Cases

(a) FAA Preempts California Law re the Enforceability of Class Action Waivers Even as to PAGA Claims - *Iskanian v. CLS Transp. Los Angeles, LLC*, 206 Cal. App. 4th 949 (2nd Dist., Jun 4, 2012), petition for review granted.²⁸

In 2006, plaintiff employee brought a putative class action against his employer for wage and hour violations. In connection with his employment, plaintiff signed a Proprietary Information and Arbitration Policy/Agreement providing that "any and all claims" arising out of his employment were to be submitted to binding arbitration before a neutral arbitrator. The arbitration agreement included a "class action waiver" provision. The employer moved to compel arbitration of the plaintiff's claims and to dismiss the class claims. That motion was granted based upon the trial court's finding that the arbitration agreement was neither procedurally nor substantively unconscionable. *Gentry* was decided after the trial court rendered its order, so the Second District Court of Appeal issued a writ of mandate directing the superior court to

comprehensive enforcement of overtime laws if the class action device is disallowed, the class action waiver must be invalidated."

²⁶ See, *Steele v. American Mortg. Management Servs.*, 2012 WL 5349511 (E.D.Cal. Oct. 26, 2012); *Sanders v. Swift Transp. Co. of Ariz., LLC*, 834 F.2d 1033 (N.D.Cal. 2012); *Lewis v. UBS Fin. Servs.*, 818 F.2d 1161 (N.D.Cal. 2011); *Valle v. Lowe's HIW, Inc.*, 2011 WL 3667441 (N.D.Cal. Aug. 22, 2011); *Murphy v. DIRETV, Inc.*, 2011 WL 3319574 (C.D.Cal. Aug. 2, 2011).

²⁷ *Quevedo v. Macy's, Inc.*, 798 F.Supp. 2d 1122 (C.D.Cal. 2011); *Grabowski v. C.H. Robinson Co.*, 817 F.Supp. 2d 1159 (S.D.Cal. 2011).

²⁸ On September 19, 2012, the California Supreme Court granted the Petition for Review filed by plaintiff/appellant, where it is pending as Case No. S204032.

reconsider its ruling “in light of the new authority.” Following remand, the employer voluntarily withdrew its motion to compel arbitration making it unnecessary for the trial court to reconsider its prior order. After conducting discovery, plaintiff moved to certify the class. On October 29, 2009, the trial court certified the class over the employer’s objection.

After the United States Supreme Court decided *Concepcion* in 2011, the employer renewed its motion to compel arbitration and dismiss the class claims, arguing that *Concepcion* was “new law that overruled *Gentry*.” The trial court granted the employer’s motion to compel arbitration and dismiss the class claims. Plaintiff appealed. On June 4, 2012, the Second District Court of Appeal affirmed the trial court and in so doing held that the FAA preempts California law as to the unenforceability of employees’ waiver of their right to representative action under PAGA and to the extent California law holds that the PAGA rights are unwaivable because such waiver is contrary to public policy. Plaintiff petitioned for review by the California Supreme Court. That petition was granted on September 19, 2012. This will be a case to watch during the later part of 2013.

(b) Certain Class Action Waivers are Still Invalid Post-*Concepcion* Per the *Gentry* Test - *Franco v. Arakelian Enterprises, Inc.*, 211 Cal. App. 4th 314 (2nd Dist., Dec. 4, 2012), petition for review granted.²⁹

In April 2007, employee filed a class action against employer for failure to pay overtime and provide meal and rest periods. The complaint alleged that the employer trucking company engaged in a systematic course of illegal of payroll practices that applied to all employees and that the potential class was so significant in size that individual joinder would be impractical. In June 2007, the employer filed a petition to compel arbitration of the employee’s claim and to dismiss or stay the civil action. That petition was granted and the employee appealed. In *Franco v. Athens Disposal Co., Inc.*, 171 Cal. App. 4th 1277, 1290-1294 (2009) (*Franco I*), the court of appeal found that the trial court had erred and held that *Gentry* invalidated a class action waiver of PAGA rights. In *Franco I*, the court of appeal also concluded that *Gentry* invalidated an arbitration clause that prohibited an employee from acting as a private attorney general under the Labor Code. The employer petitioned for review in both the California and United States Supreme Courts. Both petitions were denied and the case was returned to the trial court in January 2010.

²⁹ On February 13, 2013, the California Supreme Court granted the petition for review filed by the defendant/employer where it is pending as Case No. S207760. ___ Cal. App. 4th ___, 149 Cal. Rptr. 3d 530 (2013).

After the United States Supreme Court's decision in *Stolt-Nielsen*, the employer filed a second petition to compel arbitration of the individual employee's claim, arguing that a change in the law rendered the class action waiver enforceable. In September 2010, the trial court denied the petition and in April 2011 issued a comprehensive order. Employer again appealed, and six days after filing its appeal, the United States Supreme Court issued its decision in *Concepcion*. The court of appeal affirmed the trial court's denial of the second petition, holding that *Gentry* remains good law after *Stolt-Nielsen*. The court reasoned that under *Concepcion*, Federal Arbitration Act preemption occurs only if a state law automatically holds all class action waivers unconscionable. As *Concepcion* requires, *Gentry* does not establish a categorical rule against class action waivers. Instead, *Gentry* offers several factors to apply ad hoc to determine whether a class action waiver precludes employees from vindicating non-waivable statutory rights (i.e., overtime pay and rest and meal periods). As such, the court of appeal concluded that the class action waiver was unenforceable notwithstanding *Stolt-Nielsen* and *Concepcion*.

**(c) No Class Arbitration if the Agreement is Silent -
Kinecta Alternative Financial Solutions, Inc. v.
Superior Court, 205 Cal. App. 4th 506 (2nd Dist., May
1, 2012)**

In connection with her employment by Kinecta Federal Credit Union, plaintiff signed a comprehensive at-will employment agreement that included an arbitration provision. The arbitration agreement was silent on the issue of class arbitration and limited arbitration to disputes between the individual employee and the employer. After leaving the employ of the credit union, plaintiff filed a class action against her former employer alleging violation of wage and hour laws. In response, the employer filed a motion to compel arbitration of plaintiff's claims and to dismiss the class claims. The trial court granted the employer's motion to compel arbitration, but denied its motion to dismiss class claims. The trial court therefore imposed class arbitration even though the agreement was silent on the issue of class arbitration and expressly limited arbitration to disputes between the individual employee and the employer. On appeal, the court of appeal reversed and issued an order directing the trial court to vacate its earlier order and enter a new and different order dismissing the class action allegations from the complaint. In so ruling, the court of appeal relied on the United States Supreme Court decision in *Stolt-Nielsen* in holding that a party may not be compelled to class arbitration unless it expressly agreed to do so in the agreement. "[A] party may not be compelled under the FAA to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so." 205 Cal. App. 4th at 581, citing *Stolt-Nielsen*, *supra*, 130 S.Ct. at 1775 (emphasis in original).

The court of appeal avoided the issue of whether the *Gentry* four-factor test survived the overruling of *Discover Bank* in *Concepcion*. As noted above, this case did not concern a class action waiver in an arbitration agreement, it concerned silence on that issue. Plaintiff argued that an arbitration agreement that precludes effective vindication of statutory claims for overtime pay and other wage and hour statutory rights is unenforceable if the court determines that class wide arbitration would be a significantly more effective means of vindicating the affected employees' rights than individual arbitration. The court of appeal rejected this argument, finding that even if *Gentry* had not been overruled, in opposing the motion to compel arbitration and dismiss the class claims, plaintiff had failed to provide any evidence with respect to any of the four *Gentry* factors. As such, the court of appeal concluded that there was no evidence, and no substantial evidence, that plaintiff had established a factual basis that would require a declaration that the arbitration agreement was unenforceable.

**(d) Continuing Validity of the *Gentry* Standard
Questioned and *Horton* Rejected - *Nelsen v. Legacy
Partners Residential, Inc.*, 207 Cal. App. 4th 1115 (1st
Dist., Jul. 18, 2012).**

Employees brought a class action against their employer alleging violations of wage and hour laws. The employer moved to compel arbitration and also requested that arbitration be ordered on an individual as opposed to a collective basis based upon the United States Supreme Court's decisions in *Concepcion* and *Stolt-Nielsen*. The arbitration agreement in question was silent on class or consolidated proceedings. So the employer argued that it could not be compelled to submit to class wide arbitration because the arbitration agreements did not contain a contractual basis for authorizing class arbitration. The superior court granted the employer's motion to compel arbitration, but denied the request that it order individual, rather than class wide, arbitration. The employer filed a petition for writ of mandate with the court of appeal, challenging the lower court's refusal to order the arbitration to proceed on an individual (not class) basis.

The Fourth District Court of Appeal issued a writ of mandate commanding the superior court to vacate the portion of its order denying the employer's motion for an order requiring individual arbitration, but remanded for further proceedings to determine whether the *Gentry* standards were satisfied. The court noted that the California Supreme Court has not revisited *Gentry* since the United States Supreme Court's decisions in *Concepcion* and *Stolt-Nielsen* and stated in dicta that it agreed with the courts that have questioned the continuing validity of the *Gentry* standard to invalidate and express arbitration waiver contained in an employment arbitration

agreement governed by the FAA or to require class arbitration where the arbitration is silent and one party to the agreement objects. Nevertheless, the court of appeal held that it was “absolutely bound to follow the decisions of the California Supreme Court, unless the United States Supreme Court has decided the *same* question differently.” On this point, the court agreed with the employer that *Concepcion* implicitly disapproved of the reasoning of the California Supreme Court in *Gentry* and noted that the Second District Court of Appeal in its *Iskanian* decision had recently concluded that *Concepcion*’s broad language and reasoning undermine *Gentry*’s rationale. However, because the Court “did not directly address the precise issue presented in *Gentry*,” it declined to disregard the *Gentry* decision “without specific guidance from our high court.”

(e) Class-Action Waiver Clause is Unenforceable if Enforcement Would Preclude Their Ability to Bring Federal Antitrust Claims – *In re American Express Merchants’ Litigation*, 667 F.3d 204 (2nd Cir., Feb. 1, 2012), cert granted, 133 S.Ct. 594 (Nov. 9, 2012)

Merchants filed class action antitrust suit against AMEX. AMEX moved to compel arbitration pursuant to the terms of the Card Acceptance Agreement signed by the merchants. The district court granted AMEX’s motion and held that the arbitration clause was “paradigmatically broad” so that the parties’ disputes most certainly fell within its scope. The arbitration clause contained a class action waiver, as to which the district court held that that was a matter for the arbitrator to decide. The district court concluded that all of the plaintiffs’ substantive antitrust claims, as well as the question of whether or not the class action waivers were enforceable, were subject to arbitration. Accordingly, the district court dismissed plaintiffs’ cases against AMEX. *In re American Express Merchants’ Litigation*, 2006 WL 662341 (S.D.N.Y., Mar. 16, 2006). Plaintiffs appealed and the Second Circuit reversed, finding that the issue of the class action waiver’s enforceability was a matter for the court, not the arbitrator, to decide, and that class-action waiver provision contained in the Card Acceptance Agreement was unenforceable. *In re American Express Merchants’ Litigation*, 554 F.3d 300 (2nd Cir. 2010) (“*AMEX I*”). The Supreme Court granted AMEX’s petition for writ of certiorari, and vacated the *AMEX I* decision and remanded to the Second Circuit for reconsideration in light of its decision in *Stolt-Nielsen*. *American Express Co. v. Italian Colors Restaurant*, ___ U.S. ___, 130 S.Ct. 2401 (2010).

On remand from the Supreme Court, the Second Circuit found that *Stolt-Nielsen* did not require it to depart from its original analysis. The court of appeal concluded that the key issue was whether the mandatory class action waiver in the Card Acceptance Agreement was enforceable even if the plaintiffs are able to demonstrate that the practical effect of enforcement of the waiver would be to preclude them from

asserting federal antitrust claims against AMEX. *In re American Express Merchants' Litigation*, 634 F.3d 187, 196 (2nd Cir. 2011) ("AMEX II"). Accordingly, the Second Circuit reversed and remanded for further proceedings. *Id.* at 199-200. The court place a hold on the mandate in AMEX II in order to allow AMEX to file a petition seeking a writ of certiorari. While the mandate was on hold, the Supreme Court issued its decision in *Concepcion*, holding that the FAA preempted a California law barring the enforcement of class action waivers in consumer contracts. The Second Circuit then requested supplemental briefing on what impact, if any, *Concepcion* had on the court's earlier decision. This opinion ("AMEX III") followed.

In AMEX III, the Second Circuit held that because the arbitration clause in question included an express class-action waiver clause, that arbitration agreement was unenforceable because enforcement would effectively preclude plaintiffs from vindicating their federal antitrust claims. The court was particularly concerned that by utilizing an arbitration clause that was silent on the subject of class or that expressly waived the right to sue as a class, the defendant could immunize itself against antitrust liability. 667 F.3d at 219. Accordingly, the Second Circuit reversed the district court and remanded with instructions to deny AMEX's motion to compel arbitration. AMEX filed a petition with the Supreme Court seeking a writ of certiorari. That petition was granted on November 9, 2012. *American Express Co. v. Italian Colors Restaurant*, ___ U.S. ___, 133 S.Ct. 5941 (2012).

C. ARBITRABILITY – SUBJECT MATTER JURISDICTION

(1) Background Statement

In civil litigation, the power of the court over the parties and the subject matter of the dispute are both discussed under the general topic of "jurisdiction." In arbitration, "jurisdiction" is generally used to discuss the power of the arbitrator over the parties and "arbitrability" is used to discuss the power of the arbitrator to hear and decide particular issues or claims in a dispute. A challenge to arbitrability raises the question of whether the claim is within the scope of disputes the parties agreed to have determined through arbitration. Arbitration is a matter of contract and, as such, the parties may freely delineate the area of its application.³⁰ An arbitrator's authority over the parties and the subject matter of the dispute is consensual and must find its source

³⁰ *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 478 (1989).

in the parties' agreement.³¹ Accordingly, as a preliminary matter, before parties are ordered to arbitration, a valid agreement to arbitrate must exist and the particular dispute must fall within the scope of the agreement.³² In construing the parties' agreement to determine arbitrability, the law requires that questions of arbitrability "be addressed with a healthy regard for the federal policy favoring arbitration,"³³ and that "any doubts concerning . . . scope . . . be resolved in favor of arbitration."³⁴ Where arbitrable claims are combined with non-arbitrable claims, the court must separate the two and compel arbitration of the pendent arbitrable claims even though the result might lead to parallel proceedings between the disputants in different forums.³⁵

(2) Cases

(a) Statutory Claims are Arbitrable Unless the Statute Provides Otherwise - *CompuCredit Corp. v. Greenwood*, ___ U.S. ___, 132 S.Ct. 665 (Jan. 10, 2012).

Although plaintiffs' credit card agreement required their claims to be resolved by binding arbitration, they filed a lawsuit against CompuCredit and others alleging violations of the Credit Repair Organizations Act (CROA). The action was filed in federal court in the Northern District of California. The district court denied the defendants' motion to compel arbitration, concluding that Congress intended CROA claims to be nonarbitrable. The Ninth Circuit affirmed. On appeal to the United States Supreme Court, the Court reversed and held that because the CROA is silent on whether claims under the Act can proceed in an arbitrable forum, the Federal Arbitration Act requires the parties' arbitration agreement to be enforced according to its terms.

³¹ *Steelworkers v. Warrior & Gulf Nav. Co.*, 363 U.S. 574, 582 (1960).

³² *Volt*, supra, 489 U.S. at 479; *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995); see also *Trippe Mfg Co. v. Niles Audio Corp.*, 401 F.3d 529, 532 (3d Cir. 2005).

³³ *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 631 (1985); *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983).

³⁴ *Moses H. Cone*, supra, 460 U.S. at 24-25.

³⁵ *KPMG LLP v. Cocchi*, ___ U.S. ___, 132 S. Ct. 23 (2011) (per curiam). In this case, the Supreme Court reversed the Fourth Circuit Court of Appeals, which had refused to compel arbitration on a complaint as a whole because the arbitral agreement did not apply to direct claims, and two of the four claims were direct. *Id.* at 26. The Fourth Circuit said nothing about the other two claims. *Id.* at 25. The Supreme Court held that "[a] court may not issue a blanket refusal to compel arbitration merely on the grounds that some of the claims could be resolved by the court without arbitration." *Id.* at 24.

In its principal substantive provisions, the CROA prohibits certain practices, establishes certain requirements for contracts with consumers and gives consumers a right to cancel. Enforcement is achieved through the Act's provision of a private cause of action for violation, as well as through state and federal administrative enforcement. In seeking to avoid arbitration, plaintiffs (and the Ninth Circuit and district court) focused on two provisions in the CROA: one that requires the credit repair organization to provide notice to consumers before any contract is executed that advises them of their "right to sue a creditor repair organization that violates the [CROA]," and the other a nonwaiver provision providing that any waiver by a consumer of any protection afforded by the Act shall be void and unenforceable. The Ninth Circuit held that the required notice provision gave consumers the right to bring an action in a court of law and the waiver of the right to bring an action in a court of law contained in the arbitration agreement was thus unenforceable. The Supreme Court found the Ninth Circuit's reasoning to be flawed because it was premised on the required notice provision creating a private right of action in a court of law. The Court held that the only consumer right created was the right to receive the stated notice.

The Supreme Court rejected plaintiffs' argument that because the CROA contains a civil-liability provision, such causes of action must be prosecuted in a court of law. The Court noted that civil-liability provisions are "utterly commonplace," and if the mere formulation of the cause of action were sufficient to override the FAA, "valid arbitration agreements covering federal causes of action would be rare indeed. The Court also rejected plaintiffs' argument that because the CROA contains a nonwaiver provision, that provision should be construed as a mandate by Congress that the FAA shall not apply to CROA civil liability claims. Discussing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), and *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, supra, 473 U.S. 614, the Court noted that it had "repeatedly recognized that contractually required arbitration of claims satisfies the statutory prescription of civil liability in court."

(b) FAA Trumps Conflicting State Law that Prohibits Outright the Arbitration of a Particular Type of Claim - *Marmet Health Care Center, Inc. v. Brown*, ___ U.S. ___, 132 S.Ct. 1201 (Feb. 21, 2012) (per curiam)

Family members of patients who died while in a nursing home sued the nursing home for negligence that caused injuries or harm resulting in the death of their loved ones. In all cases, a family member of a patient requiring nursing care had signed an agreement with the nursing home on behalf of the patient that included a pre-dispute arbitration agreement. The state trial court dismissed the lawsuits based on the

agreements to arbitrate. On appeal to the West Virginia Supreme Court, the court reversed the trial court's dismissal and held that "as a matter of public policy under West Virginia law, an arbitration clause in a nursing home admission agreement adopted prior to an occurrence of negligence that results in a personal injury or wrongful death, shall not be enforced to compel arbitration of a dispute concerning the negligence." The state court considered whether West Virginia's public policy was preempted by the FAA and found the United States Supreme Court's interpretation of the FAA unpersuasive, "tendentious," and "created from whole cloth." The Supreme Court granted the petition for certiorari and, in a per curiam opinion, vacated the judgment of the West Virginia Supreme Court, holding that the state court's interpretation of the FAA was both incorrect and inconsistent with the precedents of the Court. "When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA."

(c) California Law Prohibiting Arbitration of Claims for Public Injunctive Relief – the *Broughton-Cruz* Rule – Held to be Preempted by the FAA After *Conception* Because the Rule Prohibits Outright the Arbitration of a Particular Type of Claim – *Kilgore v. KeyBank, N.A.*, 673 F.3d 947 (9th Cir., Mar. 7, 2012)

Plaintiffs are former students of a private helicopter vocational school operated by Silver State Helicopters LLC ("SSH"). According to plaintiffs, SSH engaged in an elaborate, aggressive and misleading marketing effort to attract students. Plaintiffs claim that SSH was a sham that targeted limited-income individuals who could not afford to pay for their pilot training without taking out student loans. SSH's "preferred lender" was KeyBank. To fund their helicopter training, plaintiffs and each member of the putative class borrowed between \$50,000 and \$60,000 from KeyBank. The documents executed in connection with the placement and funding of the loans included arbitration clauses. SSH failed and closed its doors, leaving students without a diploma, certificate or other accreditation for their training. Because SSH was in bankruptcy, protected by the automatic stay, plaintiffs – as the representatives of a putative class of similarly situated students – decided to sue KeyBank as having knowledge of SSH executives' looting of the company and the company's financial instability, all the while still funding student loans for tuition paid over to SSH. KeyBank filed a motion seeking to compel arbitration, which the district court denied because the *Broughton-Cruz* Rule established by two California Supreme Court decisions prohibits the arbitration of public injunctive relief claims. KeyBank appealed and the Ninth Circuit reversed, holding that the FAA preempted the state law rule relied upon by the district court judge.

In *Broughton v. Cigna Healthplans of California*, 21 Cal. 4th 1066 (1999), the California Supreme Court considered whether plaintiffs asserting claims under the state's Consumers Legal Remedies Act ("CLRA") could be compelled to arbitrate those statutory claims where the available remedies included an order enjoining defendant from engaging in deceptive advertising. The Supreme Court concluded in this case that an agreement to arbitrate could not be enforced in a case where the plaintiff is functioning as a private attorney general, enjoining future deceptive practices on behalf of the general public." This decision was based on the Court's determination that the California legislature did not intend this type of injunctive relief to be arbitrated. The *Broughton* court held also that prohibiting the arbitration of CLRA claims for injunctive relief did not contravene the FAA.

"[A]lthough the [U.S. Supreme Court] has stated generally that the capacity to withdraw statutory rights from the scope of arbitration agreements is the prerogative solely of Congress, not state courts or legislatures, it has never directly decided whether a [state] legislature may restrict a private arbitration agreement when it inherently conflicts with a public statutory purpose that transcends private interests."

21 Cal. 4th at 1083.

In *Cruz v. PacifiCare Health Systems, Inc.*, 30 Cal. 4th 303 (2003), the California Supreme court extended the *Broughton* rule to claims for public injunctive relief under the UCL. The court found that the request for injunctive relief is clearly for the benefit of health care consumers and the general public by seeking to enjoin [the insurer's] alleged deceptive advertising practices. Because public injunctive relief claims under the UCL are "designed to prevent further harm to the public at large rather than to redress or prevent injury to a plaintiff," the Court held that such claims could not be subject to arbitration, notwithstanding the parties' agreement to the contrary. *Id* at 316.

While the Ninth Circuit had previously agreed with the California Supreme Court the claims for public injunctive relief were not arbitrable, *Davis v. O'Melveny & Myers*, 485 F.3d 1066, 1082 (9th Cir. 2007), it felt compelled to examine whether *Davis* remained good law after the *Concepcion* decision. Upon review, the Ninth Circuit determined that the *Broughton-Cruz* Rule did not survive *Concepcion* because the rule "prohibits outright the arbitration of a particular type of claim – claims for broad public injunctive relief." 673 F.3d at 960. Accordingly, the Ninth Circuit reversed the district court, vacated the dismissal judgment and remanded the case with instructions to enter an order staying the case and compelling arbitration.

(d) **Bankruptcy Court has Discretion to Send “Core”
Bankruptcy Claims to Arbitration and “Non-Core”
Claims are Arbitrable - *Continental Ins. Co. v.
Thorpe Insulation Co. (In re Thorpe Insulation Co.)*,
671 F.3d 1011 (9th Cir., Jan. 30, 2012)**

This case involved an issue of *first impression* in the Ninth Circuit concerning the enforceability of an arbitration agreement when the claims to be arbitrated arise under the Bankruptcy Code or otherwise involve or affect the administration of a bankruptcy case pursuant to the Bankruptcy Code. To understand the Ninth Circuit’s holding, it is necessary to first review the background facts of the dispute that was presented to the bankruptcy court in the proceedings below.

Thorpe distributed and installed asbestos-containing products from 1948 to 1972. About 12,000 claims for asbestos-related injuries or deaths have been brought against Thorpe. Thorpe’s insurers, including Continental, have paid more than \$180 million defending and indemnifying Thorpe with respect to these claims. In 1985, Thorpe and its insurers entered into an omnibus insurance coverage and claims handling agreement. That agreement included an arbitration agreement for any coverage disputes. In 1998, Continental told Thorpe that it had exhausted its coverage under the Continental policies and ceased indemnifying Thorpe. Thorpe asserted a claim for “non-products” coverage, which Continental disputed and initiated arbitration under the omnibus agreement. The arbitrator rejected Thorpe’s claim and found that Thorpe had no remaining coverage rights under the Continental policies. Thorpe appealed and in 2003, the parties entered in a settlement agreement. The settlement agreement released only Thorpe’s claims against Continental. It did not refer to the direct action rights of individual asbestos claimants or to the contribution, indemnity or subrogation rights of other insurers. Those claims were not released. The settlement agreement included an arbitration agreement for any disputes regarding the settlement agreement and its terms.

In 2007, Thorpe filed a voluntary petition under Chapter 11 of the Bankruptcy Code. The primary purpose for the bankruptcy filing was to propose and confirm a plan of reorganization pursuant to Section 524(g) of the Bankruptcy Code, a unique provision in the Bankruptcy Code that provides a mechanism by which the asbestos-related assets and liabilities of a debtor are consolidated into a single trust for the benefit of present and future asbestos claimants. In this regard, Section 524(g) authorizes the bankruptcy court to enter a “channeling injunction” that channels all asbestos claims to a trust for administration and handling, and allows the debtor to continue operating without the continued disruption, expense and exposure of asbestos-claim litigation because, under the terms of such plans, asbestos claimants are

enjoined from suing the debtor. The injunction may also be extended to bar actions against third parties, such as the debtor's insurers, if those third parties contribute to the trust in amounts that are commensurate with their likely liability. In any event, in preparation for its bankruptcy, Thorpe negotiated with insurers other than Continental who agreed to fund the trust in consideration of Thorpe's filing for bankruptcy and seeking to confirm a "524 plan" that would result in a 524(g) injunction that would protect the insurers against asbestos-related claims arising out of policies issued to Thorpe. Additionally, these participating insurers agreed to assign their contribution, indemnification and subrogation rights against Thorpe's other insurers, including Continental, to the trust. As is not uncommon in a restructuring bankruptcy, before filing for bankruptcy, Thorpe collaborated with asbestos claimants to begin structuring a 524 plan. When Continental learned of Thorpe's pre-filing efforts to negotiate a 524 plan and prepare for bankruptcy, it claimed that such actions violated the 2003 settlement agreement. Continental also claimed that Thorpe had encouraged asbestos claimants to file direct actions against it and that that was also a violation of the 2003 settlement agreement. Pursuant to the arbitration clause contained in the 2003 settlement agreement, Continental made a demand for arbitration of this dispute. That arbitration was stayed when Thorpe filed bankruptcy in October 2007.

In the Thorpe bankruptcy case, Continental filed a claim for damages resulting from Thorpe's alleged violation of the 2003 settlement agreement (as discussed above). Thorpe objected to the claim, thereby commencing a "contested matter" proceeding in the bankruptcy court. Continental filed a motion in the bankruptcy court asking it to compel arbitration of the dispute. The bankruptcy court denied Continental's motion, and essentially held that the claims were not arbitral because (a) the resolution of Continental's claim had to be coordinated with the plan confirmation process because Continental's claim and its objection to plan confirmation overlapped factually, and (b) the remaining claims concerning Thorpe's alleged encouragement of direct actions against Continental involved Thorpe's exercise of its rights in bankruptcy and thus were within the "core" jurisdiction of the bankruptcy court and represented matters that should be decided only by a bankruptcy judge and not in a nonbankruptcy forum that might "end up adjudicating things that [it] has no business adjudicating" and result in violations of bankruptcy law and policy. 671 F.3d at 1019. Continental appealed to the district court, which affirmed, noting that Continental's claim regarding Thorpe's alleged encouragement of direct actions could have been separated out as a standalone claim for purposes of determining arbitrability, but Continental refused to separate that claim from the claims directed at Thorpe with respect to its invocation of its rights under the Bankruptcy Code to file and prepare for filing of a 524 plan. Continental appealed to the Ninth Circuit, which likewise affirmed.

In deciding the issue of whether the bankruptcy court erred in denying the motion to compel arbitration, the Ninth Circuit held that the threshold issue to determining arbitrability in the bankruptcy context is whether the dispute is a “core” or “non-core” proceeding.³⁶ *Id.* at 2010. In non-core proceedings, “the bankruptcy court generally does not have discretion to deny enforcement of a valid prepetition arbitration agreement,”³⁷ meaning that such claims are arbitral. *Id.* at 1021. However, in core proceedings, the Ninth Circuit held that the bankruptcy court “has discretion to deny enforcement of an arbitration agreement” if such enforcement would conflict with bankruptcy law.³⁸ The court explained that “[t]he rationale for the core/non-core distinction, . . . is that non-core proceedings ‘are unlikely to present a conflict sufficient to override by implication the presumption in favor of arbitration,’ whereas core proceedings ‘implicate more pressing bankruptcy concerns.’” *Id.* Importantly, in terms of leaving the door open for arbitration of “core” bankruptcy disputes, the Ninth Circuit held that “‘not all core bankruptcy proceedings are premised on provisions of the Code that inherently conflict with the Federal Arbitration Act;’ nor would arbitration of such proceedings necessarily jeopardize the objectives of the Bankruptcy Act.” *Id.*

In affirming the bankruptcy court’s decision to deny Continental’s motion to compel arbitration of the claim objection dispute, the Ninth Circuit held that Continental’s claim was a “core” matter in bankruptcy and that the bankruptcy court had discretion to deny Continental’s motion to compel arbitration if it found that arbitration of the claim would conflict with the purposes and policies of the Bankruptcy Code. Because Continental’s claim included a challenge to Thorpe’s right to seek relief under Section 524(g) of the Bankruptcy Code by taking issue with Thorpe’s activities in negotiating, proposing and confirming a plan under that section, the Ninth Circuit held that “[t]here was no error in the bankruptcy court concluding that such a claim must be resolved by a bankruptcy court and not an arbitrator.” *Id.* at 1023. In so ruling, the Ninth Circuit noted that Continental’s dispute in the case had heightened importance

³⁶ In so ruling, the Ninth Circuit referred to the earlier decisions on this issue made by several other circuits. See, *Whiting-Turner Contracting Co. v. Elec. Mach. Enters., Inc. (In re Elec. Mach. Enters., Inc.)*, 479 F.3d 791, 796 (11th Cir. 2007); *U.S. Lines, Inc. v. Am. S.S. Owners Mut. Prot. & Indem. Ass’n (In re U.S. Lines)*, 197 F.3d 631, 640 (2^d Cir. 1999); *Ins. Co. v. N. Am. V. NGC Settlement Trust & Asbestos Claims Mgmt. Corp. (In re Nat’l Gypsum Co.)*, 118 F.3d 1056, 1066-69 (5th Cir. 1997).

³⁷ Again, in so ruling, the Ninth Circuit referred to the earlier decisions on this issue made by several other circuits. See, *In re Elec. Mach. Enters., Inc.*, *supra*, 479 F.3d at 796; *Cyrsen/Montenay Energy Co. v. Shell Oil Co. (In re Crysen/Montenay Energy Co.)*, 226 F.3d 160, 166 (2^d Cir. 2000).

³⁸ See, *Phillips v. Congelton, LLC (In re White Mountain Mining Co.)*, 403 F.3d 164, 169 (4th Cir. 2005); *In re U.S. Lines*, *supra*, 197 F.3d at 640; *In re Nat’l Gypsum*, *supra*, 118 F.3d at 1067-68.

because the Continental's claim would need to be determined before payments could flow to Thorpe's creditors under the plan and as part of the plan confirmation process. *Id.* at 1023-24.

**(e) Nondischargeability Claims Are Not Arbitrable –
Ackerman v. Eber (In re Eber), 687 F.3d 1123 (9th Cir.,
July 9, 2012)**

This case also concerns the arbitrability of bankruptcy claims and was decided six months after the decision in *Thorpe* (discussed above). To appreciate the Ninth Circuit's holding, it is necessary to first review the background facts of the dispute that was presented to the bankruptcy court in the proceedings below.

Creditors commenced an arbitration proceeding against contract debtor seeking \$3.3 million in damages for breach of contract related to the construction and operation of a hair salon in Las Vegas. Later, the contract debtor filed a voluntary bankruptcy petition under Chapter 7 of the Bankruptcy Code, which resulted in the automatic stay of the arbitration proceeding. In the bankruptcy case, creditors filed a complaint under Section 523 of the Bankruptcy Code seeking a determination that the debtor's liability to them was nondischargeable. Creditors filed a motion for relief from the automatic stay to allow them to proceed to determine the debtor's liability and to liquidate the amount of their claim in the pre-petition arbitration proceeding. That motion was denied. Creditors then filed a motion to vacate the bankruptcy court's decision denying relief from stay and, concurrently, filed a motion to seeking to compel arbitration of the statutory claims they had asserted under Section 523 of the Bankruptcy Code. Both motions were denied and creditors appealed. The first level of appeal was to the district court, which affirmed the bankruptcy court. The district court agreed with the bankruptcy court that because creditors' claims "go to the issue of dischargeability," arbitration of such claims "inherently conflicts with the goals of centralized resolution of bankruptcy issues . . . and the power of the bankruptcy court to enforce its own orders." Creditors then appealed to the Ninth Circuit, where the bankruptcy court's decision was affirmed.

The Ninth Circuit recognized that the claims the creditors proposed be submitted to arbitration were claims that arose under the Bankruptcy Code – specifically, Section 523(a)(2) (the fraud exception), (a)(4) (the breach of fiduciary duty exception) and (a)(6) (the intentional tort exception) – and were thus "core matter[s] which bankruptcy courts have special expertise to decide." The Ninth Circuit viewed the issue on appeal as one of reconciling the Federal Arbitration Act with the Bankruptcy Code, "and, more specifically, the bankruptcy court's jurisdiction to determine dischargeability." *Id.* at 1128. In this decision, the Ninth Circuit looked to the Supreme Court's 1987 decision in

Shearson/Am. Express, Inc. v. McMahon, supra, 482 U.S. 220 for guidance. “While the FAA establishes a federal policy of favoring arbitration, [l]ike any other statutory directive, the Arbitration Act’s mandate may be overridden by a contrary congressional command” if the party opposing arbitration demonstrates that Congress intended to preclude a waiver of judicial remedies for the particular statutory claim at issue. *Id.* at 1129, citing *McMahon*, supra, 482 U.S. at 226-27.

In deciding the issue concerning the arbitrability of 523 claims, the Ninth Circuit applied the “*McMahon* factors”³⁹ and noted that both the Ninth Circuit and its sister circuits have previously found “no evidence in the text of the Bankruptcy Code or in the legislative history suggesting that Congress intended to create an exception to the FAA in the Bankruptcy Code.” *Id.* at 1129, citing *Thorpe*, supra, 671 F.3d at 1020. Applying the “*McMahon* facts” and Circuit precedent established by *Thorpe*, the Ninth Circuit held that the district court did not err when it affirmed the bankruptcy court’s denial of the creditors’ motion seeking to compel arbitration of their 523 claims. While the creditors attempted to characterize their claims as based on state law concerning breach of contract, fraud and breach of fiduciary duty, and thus non-core, arbitrable claims, the Ninth Circuit concluded that the object of the creditors’ motion was to arbitrate dischargeability, “a core bankruptcy issue,” meaning that the decision would be left to the discretion of the bankruptcy court. Here, the Ninth Circuit found that the bankruptcy court had not abused its discretion and agreed with the district court that allowing an arbitrator to decide dischargeability issues would conflict with the underlying purposes of the Bankruptcy Code. “When a bankruptcy court considers conflicting policies as the bankruptcy court did here, we acknowledge its exercise of discretion and defer to its determination that arbitration will jeopardize a core bankruptcy proceeding.” *Id.* at 1131.

³⁹ In *McMahon*, the Supreme Court constructed a framework under which courts can analyze how the FAA and a particular statute interact for purposes of determining whether Congress intended to override the FAA’s policy favoring arbitration with respect to claims brought under a particular statute. Under this framework, courts must examine: (1) the text of the statutes; (2) its legislative history; and (3) whether an inherent conflict between arbitration and the underlying purposes of the statute exist. 482 U.S. at 227.

(f) **Developer Can Enforce Arbitration Provision Contained in CC&R's Even Though They Were Recorded Before the HOA Was Formed – *Pinnacle Museum Tower Ass'n v. Pinnacle Market Development (US), LLC*, 55 Cal. 4th 223 (Aug. 16, 2012)**

The owners' association of a condominium project filed suit against the developer on its own behalf and as the representative of its members, complaining that construction defects had caused damage to the project. The developer petitioned to compel arbitration based on the arbitration clause contained in recorded covenants, conditions and restrictions for the project, and that petition was denied. One reason the trial court denied the petition and the court of appeal affirmed was the finding that the arbitration agreement was unconscionable and thus unenforceable. Another reason for denying arbitration was the lack of privity between the developer, on the one hand, and the owners association or its members, on the other. The California Supreme Court reversed the trial court and the affirming court of appeal on both grounds. The reasons for its reversal with respect to the unconscionability attack on the arbitration agreement are discussed in Section I(E)(2)(a), below.

With regard to the privity issue, the court of appeal affirmed the trial court's denial of arbitration because it held that the arbitration clause contained in the CC&R's was not binding on the owners' association because the association was not in existence at the time the CC&R's were recorded, so "for all intents and purposes, Pinnacle was the only party to the agreement." In reversing the court of appeal, the Supreme Court held that the court of appeal's reasoning was "not persuasive" in light of the settled principles of condominium law. Even when strict privity of contract is lacking between the developer and the persons who take title in a community interest development or act as representative for the owners, the Davis-Stirling Act ensures that CC&R's "will be honored and enforced unless proven unreasonable." The Court concluded that the expectations of all concerned were that construction disputes involving the developer would be resolved by binding arbitration.

(g) Collective Bargaining Agreement that Would Annul, Replace or Set Aside Education Code Provisions are not Arbitrable – *United Teachers of Los Angeles v. Los Angeles Unified School District*, 54 Cal. 4th 504 (Jun. 8, 2012)

After the Los Angeles Unified School District (“District”) approved the conversion of an existing public school into a charter school, the United Teachers of Los Angeles (“Union”) filed a number of grievances claiming that the District had failed to comply with provisions of the collective bargaining agreement (“CBA”). Unable to resolve the grievances informally, the Union sought to compel arbitration pursuant to the CBA. The District opposed arbitration and argued that the CBA provisions regulating charter school conversion were unlawful and thus unenforceable because they conflicted with the statutory scheme for creation and conversion of charter schools as provided in the California Education Code. The trial court agreed and denied the Union’s petition, but the Second District Court of Appeal reversed, concluding that it was not for the court to decide whether there was a conflict between the CBA and the statutes governing charter schools. Instead, the Court of Appeal held that the court’s function in adjudicating a petition to compel arbitration was limited to determining whether there was a valid arbitration agreement. The District then appealed to the California Supreme Court, which in turn reversed the Court of Appeal.

The Supreme Court held that a court faced with a petition to compel arbitration to enforce CBA provisions between a union and a school district should deny the petition if the CBA provisions at issue directly conflict with provisions of the Education Code – i.e., “if they would annul, replace, or set aside Education Code provisions.” The Court held that under the Education Code, an arbitrator has no authority to deny or revoke a school charter, which was the relief the Union was seeking. The Court remanded the matter to the trial court to give the Union an opportunity to identify the specific provisions of the CBA it claimed the District had violated and to allow the parties to address whether the provisions so identified conflict with the Education Code.

(h) When There are Conflicting Agreements, the Later Agreement Will Define the Scope of Arbitrability - *Grey v. American Management Services*, 204 Cal. App. 4th 803 (2nd Dist., Mar. 28, 2012)

In connection with his employment application, Grey was required to sign an Issue Resolution Agreement (IRA) in which he agreed to binding arbitration of any dispute arising out of his application or candidacy for employment, employment and/or cessation of employment with defendant employer. When Grey was later hired, he was

required to sign an employment contract which contained a narrower arbitration clause providing for binding arbitration of any disputes arising out of the breach of said contract. The contract also contained an integration clause. After his discharge in 2009, Grey filed suit against his former employer for discrimination, failure to pay wages in accordance with the Labor Code, and various other tort claims. Defendant petitioned the court to compel arbitration of all claims under the terms of the IRA. Grey opposed the petition, contending that the employment contract superseded the IRA and his claims were not within the scope of arbitration as provided by the arbitration clause contained in the employment contract. The trial court granted the employer's petition and ordered Grey to arbitration. Grey petitioned the court of appeal for writ of mandate, which was denied. The parties proceeded to binding arbitration and the arbitrator found in favor of the employer. The trial court then confirmed the award. Grey appealed, contending that he was not required to submit his claims to arbitration under the terms of his employment contract, which contained a narrower arbitration clause from that contained in the IRA. The court of appeal agreed with Grey and reversed. The court found that the defendant employer could not use the IRA as extrinsic evidence to show that the parties did not intend the employment contract to be their sole agreement because it contradicted the plain terms of the integration clause contained in the employment contract. The court of appeal held that the earlier agreement, having been superseded, was not a written agreement under which the employee could be compelled to arbitration. Because the employee's claims were based on statutory violations and not breach of contract, the employee's claims did not fall within the scope of the parties' agreement to arbitrate and thus employee was not required to arbitrate those claims. 204 Cal. App. 4th at 808, citing *Magness Petroleum co. v. Warren Resources of Cal., Inc.*, 103 Cal. App. 4th 901, 907 (2002) (a party is not obligated to arbitrate unless he or she has expressly agreed to do so by entering into a valid and enforceable written contract with the party who seeks arbitration); Cal. Code Civ. Proc. § 1281, et seq.

(i) Unilateral Modification Provision Made Arbitration Contract Illusory and Unenforceable and that Was for the Court to Decide - *Peleg v. Neiman Marcus Group, Inc.*, 204 Cal. App. 4th 1424 (2nd Dist., Apr. 17, 2012)

In connection with his employment, plaintiff signed a ten-page, standalone arbitration agreement. After plaintiff was terminated in 2008, he filed a lawsuit against his employer for wrongful termination, defamation and discrimination. The employer moved to compel arbitration and that request was granted over the employee's objections, including the argument that the arbitration agreement was illusory and thus

unenforceable because it contained a provision giving the employer the unilateral right to modify the agreement.

In 2009, the parties proceeded to arbitration as ordered. The matter was originally set for hearing in June 2010. There were two continuances of the arbitration hearing: the first at the request of the employer, and the second at the request of the employee. One week before the second rescheduled hearing date in October 2010, the employee requested another continuance, which was denied. On the day of the hearing, the employer appeared with its counsel and reported that it was ready to proceed. The employee appeared with an attorney, but the attorney stated that she could not go forward because she was not authorized to represent the employee at arbitration; that the employee's arbitration counsel was engaged in trial the Los Angeles Superior Court. The arbitrator dismissed the case with prejudice on the ground that the employee had failed to comply with an order: namely, to present his case at the October 2010 hearing. The arbitrator also awarded the employer with sanctions of \$40,350 in attorney's fees and costs. Back in the trial court, the parties filed cross-motions to vacate and confirm the arbitrator's award. The trial court confirmed the award and ruled that the arbitrator had not erred in denying the employee's continuance request.

On appeal, the employee renewed his argument that the arbitration agreement was illusory and thus unenforceable because it was illusory. On this issue, the court of appeal held that the question of whether the arbitration agreement was illusory was not arbitrable and was for the court to decide. It then determined that the arbitration agreement was illusory and unenforceable and thus reversed the trial court's orders compelling arbitration and confirming the arbitration award. The matter was remanded back to the trial court with instructions to place the case on the civil active list for determination in a court of law.

D. ARBITRABILITY – WHO DECIDES THE ISSUE?

(1) Background Statement

The Federal Arbitration Act declares "a national policy favoring arbitration." *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984). The FAA provides that covered arbitration agreements shall be enforced *except* "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. When parties commit to arbitrate contractual disputes, it is a mainstay of the FAA's substantive law that attacks on the validity of the contract, as distinct from attacks on the validity of the arbitration

provision itself, are to be resolved “by the arbitrator in the first instance, not by a federal or state court.” *Preston v. Ferrer*, 552 U.S. 346, 349 (2008); see also *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967). For these purposes, an arbitration provision is severable from the remainder of the contract. *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 445 (2006).

Under the FAA, the issue of “whether the parties have a valid arbitration agreement at all” is to be decided by the courts. *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444, 452 (2003). However, because arbitration is a matter of contract, questions relating to arbitrability may be delegated to an arbitrator, provided that the delegation is clear and unmistakable. *AT&T Technologies, Inc. v. Communications Workers*, 475 U.S. 643, 649 (1986); *First Options v. Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944-945 (1995). In this regard, a clause that delegates disputes relating to enforceability of the arbitration agreement will be respected and enforced. *Rent-A-Center West, Inc. v. Jackson*, ___ U.S. ___, 130 S. Ct. 2847 (2010) (held: a delegation provision requiring that the arbitrator decide issues of arbitrability was severable from a standalone arbitration agreement and enforceable unless the party specifically challenged the enforceability of the delegation provision).

(2) Cases

(a) FAA Supremacy and Contract Validity Issues are Decided by the Arbitrator - *Nitro-Lift Technologies, LLC v. Howard*, ___ U.S. ___, 133 S. Ct. 500 (Nov. 26, 2012)

In connection with their employment, plaintiffs signed confidentiality and non-compete agreements that contained an arbitration clause. Plaintiffs later quit and began working for a competitor. Claiming that plaintiffs had breached their noncompete agreements, the employer served the former employees with a demand for arbitration. Plaintiffs responded by filing suit in an Oklahoma state court in which they asked the court to declare the noncompete agreements null and void and to enjoin their enforcement. The trial court dismissed the complaint, finding that the contracts contained valid arbitration clauses under which the arbitrator, and not the court, must decide those issues. The Oklahoma Supreme Court accepted review and issued an order to show cause why the matter should not be resolved by application of an Oklahoma statute that limited the enforceability of noncompete agreements. The employer responded by arguing that any dispute as to the contracts’ enforceability was a question for the arbitrator and cited the numerous United States Supreme Court cases interpreting the FAA and making it applicable in both state and federal courts. The Oklahoma Supreme Court was not persuaded and held that despite the Supreme Court cases relied upon by the employer, the “existence of an arbitration agreement in an

employment contract does not prohibit judicial review of the underlying agreement and then declared the two noncompete agreements null and void rather than sending the issue to arbitration.

In a per curiam opinion, the United States Supreme Court vacated the Oklahoma Supreme Court's decision and ruled that the dispute over the noncompete clause must be heard by an arbitrator, as called for in the employment agreement. The Supreme Court took the Oklahoma Supreme Court to task for discounting federal precedent, noting that state courts rather than federal courts "are most frequently called upon to apply the Federal Arbitration Act, including the act's national policy favoring arbitration," it was thus "a matter of great importance . . . that state supreme courts adhere to a correct interpretation of the legislation," which the Oklahoma Supreme Court failed to do. 133 S. Ct. at 501.

The Oklahoma Supreme Court had said its decision rested on adequate and independent state law grounds, but the United States Supreme Court disagreed. "[T]he Oklahoma Supreme Court must abide by the FAA, which is 'the supreme Law of the Land,' [citations omitted] and by the opinions of this Court interpreting that law. 'It is this Court's responsibility to say what a statute means, and once the Court has spoken, it is the duty of other courts to respect that understanding of the governing rule of law.'" Id. at 503, citing *Rivers v. Roadway Express, Inc.*, 511 U.S. 298, 312 (1994).

(b) Court Decides Arbitration Clause Validity Unless Clear and Unmistakable Evidence Exists that the Parties Intended for the Arbitrator to Decide - *Ajamian v. CantorCO2E, LP*, 203 Cal. App. 4th 771 (1st Dist., Feb. 16, 2012)

Plaintiff was hired as an office manager in September 2006. At the time of her employment, plaintiff signed an annual acknowledgment and certification form that she had read the company's policies and procedures. Plaintiff alleged, however, that she signed this form with the understanding that it referred to an online compliance manual and that she had not seen the policies and procedures manual when she signed the form. The policies and procedures manual was a 65-page document that covered many topics, including the company's "Arbitration Agreement and Policy." Plaintiff did not sign the acknowledgment of her receipt of the handbook or the agreement to arbitrate. She also did not sign the arbitration agreement and policy.

In 2007, plaintiff was promoted from office manager to broker and, in connection with that promotion, signed an employment agreement that included an arbitration clause. Prior to signing the employment agreement, plaintiff had it reviewed by an

attorney of her choosing. Plaintiff's employment was terminated in March 2010, although she stayed on as an at-will employee until April 15, 2010. Five months later, plaintiff brought suit against her employer for sexual discrimination, sexual harassment, retaliation, failure to pay overtime, failure to provide rest breaks and meal breaks, etc. In response, defendant employer filed a motion to compel arbitration pursuant to the terms of the employment agreement or, alternatively, the handbook. The court denied the motion on several grounds, including the ruling that it is the court, not the arbitrator, who should decide whether an arbitration agreement is enforceable unless clear and unmistakable evidence exists showing that the parties intended to delegate the issue to the arbitrator. Defendant employer appealed.

On appeal, the Court of Appeal affirmed the trial court on all grounds. On what it termed an issue of first impression in terms of California state court decisional law, the court held that the arbitration provision at issue did not provide clear and unmistakable evidence that the parties intended an arbitrator to decide arbitrability. 203 Cal. App. 4th at 781-791.

“Language such as ‘any disputes, differences or controversies’ may well be adequate and necessary for the parties to express their intention to arbitrate all *substantive* claims, But the issue of who would decide the enforceability of the arbitration clause *itself* is a horse of a different color. It is a distinct issue and could and would be easily addressed – if the parties actually contemplated it at the time of contracting – by stating expressly that the arbitrator shall decide questions of the enforceability of the arbitration provision.”

Id. at 786 (emphasis in original). The Court of Appeal distinguished the present case from the facts presented in the *Rent-A-Center* case because the language of the arbitration clause in the *Rent-A-Center* case expressly stated that any dispute concerning the interpretation, applicability, enforceability or formation of the arbitration agreement would be submitted to binding arbitration. In this case, the clause only specified that “disputes, differences or controversies arising under [the] Agreement” were to be submitted to binding arbitration and said nothing about the enforceability of the arbitration agreement itself. As such, the Court of appeal reasoned that the clause at issue did not satisfy the *First Options*’ “clear and unmistakable evidence” test. Id. at 787-788.

**(c) Depending on the Circumstances, an Arbitrator can
Decide Alter Ego Issues and One Such
Circumstance is Where the Parties Submit Such
Issues to Arbitration – *Comerica Bank v. Howsam*,
208 Cal. App. 4th 790 (2nd Dist., Aug. 20, 2012)**

In 2004, Comerica made loans totaling \$37 million to seven Canadian corporations and their principal, also a resident of Canada. The procedural history was quite complex and involved a criminal indictment, proceedings in an arbitral forum, proceedings in a trial court, and cert petitions to both the California and United States Supreme Courts (both denied). The Los Angeles Superior Court granted a motion to compel arbitration and later confirmed three arbitral awards against borrowers, as well as a sanctions award against borrowers' counsel over the objections and request for vacatur made by borrowers and their counsel. On appeal, defendants argued that the awards should be vacated because the arbitrator exceeded his powers by deciding the alter ego issues. The Second District Court of Appeal affirmed the trial court and held that whether an arbitrator can decide alter ego issues depends on the circumstances. 208 Cal. App. 4th at 829, citing *Hotels Nevada, LLC v. L.A. Pacific Center, Inc.*, 203 Cal. App. 4th 336, 358 (2012); *Greenspan v. LADT, LLC*, 185 Cal. App. 4th 1413, 1447-1449 (2010); *Suh v. Superior Court*, 181 Cal. App. 4th 1504, 1513 (2010); *Rowe v. Exline*, 153 Cal. App. 4th 1276, 1285 (2007). The court rejected defendants' argument that the court's earlier decision in *Retail Clerks Union v. L. Bloom Sons Co.*, 173 Cal. App. 2d 701 (1959) stood for the proposition that an arbitrator can *never* decide alter ego issues. *Id.*

In this case, the court of appeal found two circumstances existed which gave the arbitrator the power to decide the alter ego issues. First, plaintiff's complaint contained extensive alter ego allegations, and when defendants' motion to compel arbitration was granted, they attached plaintiff's first amended complaint (with its alter ego allegations) to the demand for arbitration. The court thus concluded that defendants submitted the alter ego claims to arbitration. Second, defendants sought arbitration under California's international commercial arbitration statutes, which include a provision that the arbitrator may rule on his or her own jurisdiction. Cal. Code Civ. Proc. § 1297.161. They also included in their demand for arbitration a request that it be conducted under the auspices of the Independent Film & Television Alliance, which has its own Rules for International Arbitration. Under the Alliance's rules, the arbitrator is charged with determining his or her powers and is vested with authority to make a "final determination of all matters in dispute." The court thus concluded that those matters included the alter ego claims that were directly posited in the first amended complaint attached to the demand for arbitration. *Id.* at 828.

E. ARBITRATION AGREEMENTS – ENFORCEABILITY AND CHALLENGES TO ENFORCEMENT

(1) Background Statement

Under Section 2 of the Federal Arbitration Act (“FAA”), an arbitration agreement is “valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” 9 U.S.C. § 2. This statutory provision states a rule of federal substantive law which makes arbitration agreements enforceable both in state and in federal courts. *Southland Corp. v. Keating*, 465 U.S. 1 (1984). Any state law that attempts to render unenforceable an arbitration agreement which is enforceable under the FAA is preempted by the FAA. *Id.*; *Doctor’s Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996). This rule of federal substantive law applies if the transaction in question is a transaction “involving commerce” or a maritime transaction. The “involving commerce” requirement is to be construed broadly so as to reach the limits of the Commerce clause power of Congress. *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 513 U.S. 265 (1995).

The FAA mandates that trial courts “shall” compel arbitration and stay litigation involving disputes subject to an arbitration agreement. 9 U.S.C. §§ 3, 4. In this regard, the United States Supreme Court repeatedly has stated that the FAA manifests “a liberal federal policy favoring arbitration agreements.” *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985); *Moses H. Cone Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983). The liberal policy favoring arbitration requires courts to “rigorously enforce agreements to arbitrate.” *Mitsubishi*, *supra*, 473 U.S. at 625-626; *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985).

The court’s analysis in deciding whether to compel arbitration is generally devoted to a determination of three issues: (1) whether a valid arbitration agreement exists; (2) whether the issues sought to be arbitrated fall within the scope of the arbitration agreement; and (3) whether the party against whom enforcement is sought has failed or refused to arbitrate. If the court determines that these conditions have been met, it is required to direct the parties to arbitrate their dispute. The cases discussed in this section concern the first issue: namely, whether a valid/enforceable arbitration agreement exists. As such, they look primarily at defenses to the enforceability of an arbitration clause included in a business / consumer / finance / employment contract.

(2) Cases

(a) **Including an Arbitration Clause in CC&R's is Not
Procedurally or Substantively Unconscionable -
*Pinnacle Museum Tower Ass'n v. Pinnacle Market
Development (US), LLC*, 55 Cal. 4th 223 (Aug. 16,
2012)**

The owners' association of a condominium project filed suit against the developer on its own behalf and as the representative of its members, complaining that construction defects had caused damage to the project. The developer petitioned to compel arbitration based on the arbitration clause contained in recorded covenants, conditions and restrictions for the project, and that petition was denied. One reason the trial court denied the petition and the court of appeal affirmed was the finding that the arbitration agreement was unconscionable and thus unenforceable. Another reason for denying arbitration was the lack of contractual privity between the developer, on the one hand, and the association and its members, on the other. The California Supreme Court reversed the trial court and the affirming court of appeal on both grounds. The reasons for its reversal with respect to the privity issue are discussed in Section I(C)(2)(e), above.

Having found that the CC&R's were binding on the owners' association, the Court next looked at the arbitration provisions to see if they were unenforceable as unconscionable. The Supreme Court reversed this holding as well and found that the court of appeal's reasoning was "not persuasive" in light of the settled principles of condominium law. Even when strict privity of contract is lacking between the developer and the persons who take title in a community interest development or act as representatives.

(b) **Right to Pursue Provisional Remedies in Court Does
not Make Arbitration Agreement Substantively
Unconscionable - *Baltazar v. Forever 21, Inc.*, 2012
WL 6629610 (2nd Dist., Dec. 20, 2012).**

This case involved the assertion of unconscionability as a defense to formation and thus enforcement of a binding arbitration provision. A former employee brought suit against her former employer and other employees alleging that she was constructively discharged and subjected to discrimination and harassment based on race and sex. Defendants moved to compel arbitration pursuant to the arbitration clause contained in the employment agreement. Plaintiff opposed the motion on the grounds that the arbitration agreement was unconscionable. The trial court ruled in plaintiff's favor and denied the motion. On appeal, the Court of Appeal, Second

District, reversed, finding that while the arbitration agreement was a contract of adhesion, it was not substantively unconscionable. Relying on Code of Civil Procedure § 1281.8 (which allows a party to an arbitration agreement to seek provisional relief in a court of law), and noting that the entirety of the arbitration agreement was mutual and did not impose a unilateral restriction on employee remedies, the Court of Appeal held that the provision allowing either party to seek provisional remedies in court – such as a restraining order or injunction – did not render the agreement to arbitrate unconscionable.

(c) *Concepcion* Does not Prevent Courts from Rejecting Arbitration Agreements that are Unconscionable - *Samaniego v. Empire Today, LLC*, 205 Cal. App. 4th 1138 (1st Dist., Apr. 5, 2012)

Plaintiffs worked as carpet installers for defendant (a carpet and flooring company). When they were initially hired, they were given an 11-page, single-spaced “subcontractor agreement” that was written entirely in English (which plaintiffs could not read). The agreement was provided on a non-negotiable, take-it-or-leave-it basis with little or no time for review. The agreement contained a shortened six-month statute of limitations for subcontractors to sue under the agreement, as well as a unilateral fee shifting provision in favor of the employer. The agreement provided for binding arbitration pursuant to the Commercial Arbitration Rules of the American Arbitration Association, but did not attach a copy of said rules. When plaintiff workers brought a putative class action against their employer for alleged Labor Code violations relating to alleged misclassification as independent contractors, defendant employer moved to compel arbitration. The trial court refused to enforce the arbitration clause as procedurally and substantively unconscionable, and rejected the defendant’s argument that the United States Supreme Court’s decision in *Concepcion* precluded this result. The employer appealed.

On appeal, the First District Court of Appeal affirmed the trial court. With regard to procedural unconscionability, the court of appeal found that there was substantial evidence to support the trial court’s determination because the uncontroverted evidence showed that plaintiffs were hired to perform manual labor and were told they could not work without first signing the agreement; plaintiffs did not speak English as a first language and had limited or no literacy in English, but were not provided a copy or given an opportunity to take it home for review before signing. Additionally, the arbitration clause was one of 27 sections and was not flagged in any

way to alert/inform the workers that they were agreeing to binding arbitration.⁴⁰ Finally, the evidence showed that defendant failed to provide plaintiffs with a copy of the referenced arbitration rules, which the courts have previously found to be oppressive.⁴¹

With regard to substantive unconscionability, the court of appeal found that the agreement contained several one-sided provisions – shortened statute of limitations, unilateral attorney’s fees clause favoring only the defendant, and an exemption from arbitration of those claims typically brought by employers – and thus demonstrated “‘strong indicia of substantive unconscionability,’” as found by the trial court. *Id.* at 1147, citing *Lhotka v. Geographic Expeditions, Inc.*, 181 Cal. App. 4th 816, 821 (2010). The agreement also contained an Illinois choice-of-law provision, which the employer attempted to enforce and the court rejected, noting that “the same factors that render the arbitration provision unconscionable warrant the application of California law.” *Id.* at 1149. The court held that the rule in California is that the *weaker* party to an adhesion contract may avoid enforcement of a choice-of-law provision where enforcement would result in substantial injustice, as defined by California law. *Id.*, citing *Washington Mutual Bank v. Superior Court*, 24 Cal. 4th 906, 918 (2001); *Nedlloyd Lines B.V. v. Superior Court*, 3 Cal. 4th 459, 464 (1992).

With regard to defendant’s argument that *Concepcion* extends the Federal Arbitration Act so broadly that it preempts the recognition of any unconscionability defense to enforcement of an arbitration agreement, the court of appeal held that the Supreme Court in *Concepcion* decision expressly reaffirmed that the FAA permits the invalidation of arbitration agreements by generally applicable contract defenses and that arbitration agreements remain subject to unconscionability defenses and analysis post-*Concepcion*.

⁴⁰ In *Gutierrez v. Autowest, Inc.*, 114 Cal. App. 4th 77, 89 (2003), a similar type of “buried” arbitration clause was deemed procedurally unconscionable.

⁴¹ See, *Harper v. Ultimo*, 113 Cal. App. 4th 1402, 1406 (2003); *Trivedi v. Curexo Technology Corp.*, 189 Cal. App. 4th 387, 393-394 (2010).

(d) **Stronger Party Could not Attack its own Choice-of-Law Provision. Massachusetts Law Governed and Required a Clear and Specific Agreement to Arbitrate Statutory Discrimination Claims – *Harris v. Bingham McCutchen*, ___ Cal. App. 4th ___, 2013 WL 1278361 (2nd Dist., Mar. 29, 2013)**

Employee brought an action against her law firm employer for various statutory discrimination claims, as well as wrongful termination and defamation. In connection with her employment, plaintiff signed a letter agreement that contained an arbitration provision covering “any legal disputes” that might arise out of or relate to plaintiff’s employment with the firm or its termination. Defendants petitioned to compel plaintiff to arbitrate her claims. Plaintiff opposed the arbitration petition on the ground that it was unenforceable under the letter agreement’s choice-of-law provision applying Massachusetts law to the employment relationship. Plaintiff asserted that Massachusetts substantive law precluded arbitration of her statutory discrimination claims because agreements to arbitrate statutory discrimination claims must be stated in clear and unmistakable terms. The trial court agreed with plaintiff’s argument and denied defendants’ arbitration petition. Defendants appealed.

On appeal, defendants cited the court to *Samiengo* (discussed in Section (c), above) in support of their contention that California statutory claims, if they survive the choice-of-law provision, are “necessarily” governed by California law. The Second District Court of Appeal found that *Samiengo* was distinguishable; that it held that California law governed the enforceability of an arbitration clause in an otherwise unconscionable employment agreement which contained an Illinois choice-of-law provision; that the *employer/stronger party* could not enforce the choice-of-law provision for the same reasons that made the arbitration clause unconscionable and thus unenforceable. In the present case, the court of appeal found that the stronger party (the defendants) was attaching its own choice-of-law provision. The court of appeal agreed with the trial court’s reasoning and its conclusion that Massachusetts law governed the enforceability of the arbitration clause at issue in this case. *Id.* at *2.

The court then examined the general nature of plaintiff’s claim and found that it was for “discriminatory wrongful termination in retaliation for her request to accommodate her sleep disorder.” The court thus concluded that the applicable law was Massachusetts law as stated in the Massachusetts Supreme Judicial Court’s decision in *Warfield v. Beth Israel Deaconess Medical Center, Inc.*, 454 Mass. 390, 910 N.E.2d 317 (2009). In *Warfield*, the court found that the arbitration clause was unenforceable because the employment agreement did not explicitly state that discrimination claims would be decided by arbitration. The court in *Warfield* stated, “parties seeking to

provide for arbitration of statutory discrimination claims must, at minimum, state clearly and specifically that such claims are covered by the contract's arbitration clause." 454 Mass. at 400.

In this case, the court of appeal compared the arbitration clause in *Warfield* to the arbitration clause in the parties' employment agreement and found that they were "strikingly similar." *Id.* at *3. Defendants argued that *Warfield* should be narrowly construed to apply only to violations of Massachusetts anti-discrimination statute and not to any violations of California anti-discrimination statutes. The court found this argument unpersuasive because it would give defendants the benefit of applying its choice-of-law provisions to any employment relationship disputes while depriving plaintiff of Massachusetts law addressing statutory rights against discrimination in the workplace. "Defendants cannot have it both ways while claiming the employment agreement is not illusory." *Id.* at *3. Further, the court held that because the defendants were the drafters of the document which required a California employee to be bound by substantive Massachusetts law, any ambiguity was to be construed against defendants' interest." *Id.* at *4. In final analysis, the court concluded that the arbitration agreement was not enforceable under Massachusetts law as to the statutory discrimination claims brought by plaintiff in this case and that the trial court correctly denied defendants' arbitration petition.

**(e) FINRA Arbitration Rules are Substantively
Unconscionable Because of Excessive Fees -
Simmons v. Morgan Stanley Smith Barney, LLC, 872
F.Supp. 2d 1002 (S.D.Cal., May 24, 2012)**

This case concerned the attack on enforceability of an arbitration agreement on the grounds that it was unenforceable because it was both procedurally and substantively unconscionable.⁴² In connection with his employment as an executive

⁴² Under California law, in assessing whether an arbitration agreement or clause is enforceable, the court applies ordinary state-law principles that govern the formation of contracts in general. *Davis v. O'Melveny & Myers*, 485 F.3d 1066, 172 (9th Cir. 2007). A contractual clause is unenforceable if it is both procedurally and substantively unconscionable. See, *Armendariz v. Found. Health Psychcare Servs., Inc.*, 24 Cal. 4th 83, 114 (2000). That being said, a determination that the arbitration agreement contains a "flawed provision" does not necessarily mean that the entire arbitration agreement is substantively unconscionable. The court may consider and find that it is possible to sever the offending provision. *Davis v. O'Melveny & Myers*, *supra*, 485 F.3d at 1084. In determining whether a contract is unconscionable, the courts apply a sliding scale: "the more substantively oppressive a contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa." *Armendariz*, *supra*, 24 Cal. 4th at 224.

with Morgan Stanley, plaintiff signed an offer letter and sign-on agreement. The offer letter stated that plaintiff would be entitled to a forgivable loan of \$1 million, relocation benefits and an award of stocks. With regard to these matters, plaintiff signed promissory notes and bonus agreements that contained arbitration clauses. Three years later, plaintiff's employment was terminated. Morgan Stanley initiated an arbitration with FINRA seeking to arbitrate plaintiff's alleged violation of the promissory notes and bonus agreements. Shortly thereafter, plaintiff filed an action in the San Diego Superior Court in which he complained of employment discrimination in violation of state and federal law, wrongful termination in violation of public policy, fraud, and breach of contract. Morgan Stanley removed the action to federal district court and then filed a motion seeking to compel arbitration of plaintiff's claims. Plaintiff opposed the motion on several grounds, including an argument that the arbitration agreement contained in the promissory notes and bonus agreements were unenforceable because they were unconscionable.

With regard to the procedural unconscionability prong, the court held that procedural unconscionability analysis focuses on oppression or surprise. In that regard, it held that a contract of adhesion is one that is presented on a "take-it-or-leave-it" basis and is oppressive due to an inequality of bargaining power that results in no real negotiation and an absence of meaningful choice. *Id.* at 1016, citing *Flores v. Transamerica HomeFirst, Inc.*, 98 Cal. App. 4th 846, 853 (2001). In this case, the court determined that plaintiff's acceptance of the \$1 Million and \$400,000 in loans and the accompanying promissory notes and bonus agreements was not a condition of his employment. However, it found that Morgan Stanley had "superior bargaining strength" and failed to show that there was negotiation or a meaningful choice available to plaintiff. As such, the court found that the arbitration provisions contained a "minimal element of procedural unconscionability."

With regard to the substantive unconscionability prong, the court held that this analysis relates to the effect of the contract or provision and generally looks for a lack of mutuality evidenced by terms that are so one-sided as to "shock the conscience." *Id.* at 1016, citing *Davis v. O'Melveny & Myers*, *supra*, 485 F.3d 1075. While plaintiff took issue with several provisions in the promissory notes and/or bonus agreements, the court found that only one of those provisions qualified as substantively unconscionable, and that was the provision incorporating the FINRA rules, which might result in plaintiff being required to pay hearing fees in excess of what he would pay the court. *Id.* at 1019. That being said, the court then determined that the arbitration provisions at issue were not "permeated by unconscionability" because the single provision that was found to be substantively unconscionable had a low degree of unconscionability and could easily be severed.

**(f) Agents of Parties to Arbitration Agreement can
Enforce the Agreement - *Thomas v. Westlake*, 204
Cal. App. 4th 605 (4th Dist., Mar. 23, 2012)**

This case involved a defense to enforcement of an arbitration agreement on the ground that the party moving to enforce the arbitration agreement was not a signatory and thus could not force plaintiff to arbitrate the claims asserted against said party. Before her death, Katherine Thomas, an elderly widow, opened three investment accounts with Ameriprise Financial Services and a related subsidiary. Steven Westlake was the securities broker and investment advisor for these accounts. After Katherine died, her son John became her successor in interest on the three accounts and brought suit against Westlake, Ameriprise and others for financial elder abuse and other claims. The gist of the complaint was that defendants had conspired to “churn” Katherine’s accounts by inducing her to make unsuitable investments that increased defendants’ commissions and profits and substantially reduced the value of the accounts. In response to the complaint, defendants filed a motion to compel arbitration and to stay the court proceedings. That motion sought an order compelling John to arbitrate all claims against defendants, even though only some of the defendants were parties to the brokerage agreements signed by Katherine that contained the arbitration agreement. The trial court denied the motion to compel arbitration, noting that the contractual right to arbitration “may have to yield if there is an issue of law or fact common to the arbitration and a pending action or proceeding with a third party.” The trial court concluded that the difficulty of splitting up the claims asserted against the signatory and non-signatory defendants, coupled with the potential for inconsistent rulings, mandated denial of the motion. Defendants appealed and the court of appeal reversed.

Under the general rule of law, only a party to an arbitration agreement is bound by or may enforce the agreement. Cal. Code. Civ. Proc. § 1281.2; *Jones v. Jacobson*, 195 Cal. App. 4th 1, 17 (2011). In this case, Ameriprise was the only defendant that was a party to the agreements with Katherine containing the arbitration clauses, and under the general rule, it was the only party who could enforce the arbitration provisions against John. That being said, the court of appeal noted that there are exceptions to the general rule, including the exception when a plaintiff alleges that a defendant acted as an agent of a party to an arbitration agreement. Under such circumstances, the law in California is that such a non-signatory, alleged agent defendant may enforce the arbitration agreement. See, *Dryer v. Los Angeles Rams*, 40 Cal. 3d 406, 418 (1985); *RN Solution, Inc. v. Catholic Healthcare West*, 165 Cal. App. 4th 1511, 1520 (2008); *24 Hour Fitness, Inc. v. Superior Court*, 66 Cal. App. 4th 1199, 1210 (1998). The court of appeal recognized that under the “alleged agency exception,” when a plaintiff alleges a defendant was an agent of a party to an arbitration agreement, the defendant may

enforce that agreement even though it is not a party to the agreement. Accordingly, the court of appeal reversed the order denying defendants' motion to compel arbitration and remanded the matter to the trial court with instructions to enter a new and different order granting the motion and staying all proceedings until completion of the arbitration.

(g) Daughter of Resident of Skilled Nursing Home is not Subject to Arbitration Agreement that Applies to Resident - *Bush v. Horizon West*, 205 Cal. App. 4th 924 (3rd Dist., Jul. 18, 2012)

The resident of a skilled nursing facility, by and through her daughter and guardian ad litem, sued the facility for elder abuse (among other causes of action) based on their alleged neglect in providing her care and treatment at the facility. In the same complaint, the daughter joined in her own right and sued the facility for negligent infliction of emotional distress based on her observation of the harm they caused her mother through their neglect. When defendants moved to compel arbitration of the mother's claims pursuant to a written agreement containing an arbitration clause, the trial court exercised its discretion under CCP §1281.2(c) to deny the motion because of the possibility of conflicting rulings between the mother's claim for elder abuse, which was subject to arbitration, and the daughter's claim for negligent infliction of emotional distress, which was not. See, Cal. Code Civ. Proc. § 1281.2(c) (trial court may deny petition for arbitration to avoid conflicting rulings). Defendants appealed.

On appeal, the Court of Appeal affirmed, and in doing so distinguished this case from the California Supreme Court's recent decision in *Ruiz v. Podolsky*, 50 Cal. 4th 838 (2010), in which the Court held that under CCP § 1295, wrongful death claimants in medical malpractice cases are bound by arbitration agreements entered into by the decedent where the language of the agreement manifests an intent to bind such claimants (e.g., a clause providing for successors and heirs to be bound by the agreement). By contrast, the court of appeal found that no such statute applied in the context of claims for infliction of emotional distress for which the daughter was asserting her own personal claims and was not acting as a representative or heir of the party to the arbitration agreement. Accordingly, the court concluded that the daughter was not bound by the arbitration agreement signed by her mother and the trial court did not abuse its discretion in determining that there was a possibility of conflicting rulings if the two sets of claims proceeded in different forums.

(h) Nonsignatory May not be Compelled to Arbitrate Unless it is a Third-Party Beneficiary - *Epitech, Inc. v. Kann*, 204 Cal. App. 4th 1365 (2nd Dist., Apr. 16, 2012)

The secured creditors of a corporate entity brought suit against their borrower's financial adviser for fraud, negligent misrepresentation and concealment, alleging that the advisor had fraudulently induced them to forbear from foreclosing on their security to their financial detriment. Defendant petitioned to compel arbitration pursuant to the arbitration agreement contained within his contract with the corporate borrower. Defendant's theory was that plaintiffs were suing him because of the way her performed under his contract with the corporate borrower and therefore the plaintiffs should be treated as third-party beneficiaries of corporate borrower's contract with the financial advisor and should thus be bound by the arbitration clause contained within that contract. The trial court denied the petition, and defendant appealed.

On appeal, the court of appeal affirmed and held that the public policy favoring arbitration does not apply to disputes the parties have not agreed to arbitrate. In this case, there was no agreement to arbitrate between the plaintiff creditors and the defendant financial adviser. There are exceptions to the rule that a nonsignatory cannot be compelled to arbitrate, including the exception when a nonsignatory is a third-party beneficiary of a contract containing an arbitration clause. In this case, the court noted that while the plaintiff creditors might have benefited if the defendant had been able to secure financing for the corporate borrower, defendant had not contracted to pay the secured creditors any money from that prospective financing and the decision makers of the corporate borrower had not obligation to pay any of those financing monies over to the plaintiff creditors. 204 Cal. App. 4th at 1370. As such, the court of appeal reasoned that the plaintiff creditors were only incidental beneficiaries of their borrower's contract with the financial adviser and ruled that the "intended beneficiary" exception does not extend to incidental beneficiaries.

(i) No Implied-in-Fact Arbitration Agreement Where Employer Stated that Employee Signatures were Required - *Gorlach v. The Sports Club Co.*, 209 Cal. App. 4th 1497 (2nd Dist., Oct. 16, 2012)

The plaintiff was the former human resources director for the defendant employer. Prior to 2010, there were no arbitration agreements between the defendant and its employees. However, in mid-2010, the defendant employer revised its handbook to include an arbitration agreement. Plaintiff was then tasked with presenting the new handbook to all employees and collecting their signatures to the arbitration agreement. When plaintiff finished these meetings, she told the Chief

Operating Officer that all but four employees had signed the arbitration agreement. Plaintiff did not sign the agreement and did not identify herself as one of the non-signing employees, thereby leading the defendant employer to believe that she had signed. A few weeks later, plaintiff resigned her position with defendant employer and six months later filed a complaint seeking damages for wrongful termination, retaliation, paramour sexual harassment, intentional infliction of emotional distress, defamation, breach of contract and negligence. In its answer, the defendant employer asserted that the court lack jurisdiction to resolve the dispute due to the existence of a mandatory, binding arbitration agreement with plaintiff, and thereafter filed a motion to compel arbitration. It was undisputed that plaintiff never signed the arbitration agreement introduced in 2010. Nevertheless, the defendant employer argued that plaintiff had assented to the arbitration agreement by continuing her employment with defendant after learning that it was a condition of employment. The trial court denied the motion, finding that defendant had “failed to demonstrate that there exists a written arbitration agreement between the plaintiff and defendants.” Defendant appealed.

On appeal, the court of appeal affirmed, finding that the employer had not relied to its detriment on the plaintiff’s implied representation that she had signed the arbitration agreement, and that plaintiff’s failure to resign for two months after the arbitration agreement was introduced did not establish an implied-in-fact contract to arbitrate. As to this later point, the court of appeal distinguished an implied agreement case in which employees were deemed to have consented to arbitration by continuing their employment after the employer sent a memorandum that unilaterally stated that the employer’s arbitration policy “will govern all future legal disputes.” By contrast, the court of appeal noted that the defendant employer’s handbook stated that employees were required to sign the arbitration provisions in the handbook. Under such circumstances, an agreement to arbitrate could not be implied where the employee does not actually sign.

(j) After Nonbinding Arbitration, Law Firm Only had to Demand Arbitration and was not Required to File State Court Action - *Greenberg Glusker Fields Claman & Machtinger LLP v. Rosenson*, 203 Cal. App. 4th 688 (2nd Dist., Feb. 15, 2012)

When client engaged law firm, he signed a retainer agreement that provided for arbitration of any fee disputes. A dispute arose and client requested mandatory, nonbinding arbitration before the Beverly Hills Bar Association pursuant to the MFAA. The Bar Association arbitrators found that the client was overcharged by \$75,000 and awarded him that amount, plus \$5,000 in costs. Within 30 days of the nonbinding MFAA award, the law firm demanded binding arbitration under the arbitration

provisions contained in the retainer agreement. Rather than participating in the arbitration, the client filed a petition to confirm the MFAA award. The law firm opposed the petition, arguing that it had exercised its contractual right to binding arbitration by filing a demand within 30 days of the MFAA award. The client replied that the law firm had not effectively exercised its right to reject the MFAA award because it did not file an action in a court of law; that the commencement of the arbitration did not satisfy the filing of an action requirement under the MFAA. The trial court agreed and confirmed the MFAA award. The law firm appealed.

On appeal, the Second District Court of Appeal reversed the trial court and held that the trial court should have denied the client's motion to confirm the MFAA award because binding arbitration under the retainer agreement remained unresolved. The court of appeal held the MFAA does not foreclose the possibility binding arbitration after the MFAA process is completed if one or both parties are dissatisfied. In this regard, the court of appeal noted that the California Supreme Court's decision in *Schatz v. Allen Matkins Leck Gamble & Mallory LLP*, 45 Cal. 4th 557 (2009) affirmatively established that binding arbitration may follow nonbinding arbitration under the MFAA "if agreed to in writing by the parties, and invoked within the 30-day time period." *Id.* at 693-694. The court of appeal rejected the client's argument that the law firm should have first filed a superior court action and a motion to compel arbitration, rather than making a demand for arbitration because that set of procedures "would have run afoul of settled California law prohibiting an action to compel arbitration until the opposing side has refused to arbitrate. . . . Requiring [the law firm] to file a superior court action to compel arbitration before [the client] refused to participate is inconsistent with the goals of arbitration." *Id.* at 694.

**(k) California Choice of Law Provision Authorized
Trial Court to Refuse to Compel Arbitration Based
on Risk of Conflicting Rulings - *Mastick v. TD
Ameritrade, Inc.*, 209 Cal. App. 4th 1258 (2nd Dist., Oct.
9, 2012)**

An investor sued his accountant, investment management company and broker for professional negligence concerning the surrender and reinvestment of the cash value of her whole life insurance policies. The underlying "transaction" was a single meeting in November 2008 at which the accountant advised plaintiff to surrender her whole life insurance policies and invest the proceeds with Oakwood (an investment management company) who used an investment broker (TD Ameritrade) to make the investments in the stock market. In this lawsuit, plaintiff alleged that her accountant gave her bad advice about the ensuing tax consequences of the surrender/investment transaction and sued everyone for professional negligence.

Plaintiff's arrangement/agreement with her accountant did not include an arbitration clause. The investment management agreements between plaintiff and defendant Oakwood provided that the parties would be governed by California law and that disputes between them would be resolved through arbitration in accordance with the AAA rules. The client agreements between plaintiff and defendant TD Ameritrade provided that the parties would be governed by Nebraska law and that disputes between them would be resolved through arbitration in accordance with the FINRA rules.

Defendants Oakwood and TD Ameritrade petitioned the court to compel arbitration pursuant to their respective agreements with plaintiff. The trial court denied both petitions under CCP §1281.2(c), which gives the trial court discretion to refuse to enforce an arbitration agreement if a party to the agreement is also a party to related litigation with a third party that creates the risk of conflicting rulings on a common issue of law or fact. Oakwood and TD Ameritrade appealed.

On appeal, the Second District Court of Appeal affirmed the trial court with regard to the denial of defendant Oakwood's request for arbitration and reversed with regard to the denial of defendant TD Ameritrade's request for arbitration. The reason for this disparate result was based on the differences between the controlling law specified in the aforementioned agreements: one being California and one being Nebraska.

With regard to defendant Oakwood, the court of appeal held that the California choice of law provision in the agreements with plaintiff authorized the trial court to stay or refuse to enforce arbitration of plaintiff's claims against Oakwood to avoid duplicative proceedings and conflicting rulings pursuant to CCP §1281.2(c). The court of appeal held that the trial court did not abuse its discretion when it found that enforcement of plaintiff's agreement to arbitrate claims against Oakwood would create a risk of conflicting rulings with regard to plaintiff's claims against her accountant because those claims were "based on a single injury arising from advice given at a single meeting concerning a single transaction." The court of appeal reasoned that it made no sense to require plaintiff to pursue actions separately against her accountant and Oakwood on claims resulting from a single transaction because that would put in motion the risk of inconsistent rulings. 209 Cal. App. 4th at 1265. Accordingly, the court of appeal affirmed the trial court with regard to its decision to deny defendant Oakwood's petition to compel arbitration.

With regard to defendant TD Ameritrade, the court of appeal reversed the trial court based on its analysis of Nebraska law. Nebraska's law on arbitration does not include a provision which authorizes a court to stay arbitration or refuse to enforce an arbitration provision to avoid duplicative proceedings or conflicting rulings. *Id.* at 1266. When a choice-of-law provision exists in a private contract, California courts will honor it unless either (a) there is no reasonable basis for the parties' choice, or (b) application of the law of the chosen state would be contrary to the fundamental policy of a state that has a materially greater interest. *Id.* at 1267, citing *Nedlloyd Lines B.V. v. Superior Court*, 3 Cal. 4th 459 (1992). The court of appeal was "mindful of the desire to have a single forum," but found that TD Ameritrade's relationship with Nebraska supplied a reasonable basis for the parties' choice and that application of Nebraska law was not contrary to the fundamental policy of California favoring enforcement of valid arbitration agreements according to their terms. *Id.*, citing *St. Agnes Medical Center v. PacifiCare of California*, 31 Cal. 4th 1187 (2003)

**(I) Consumer Arbitration Provision Survives Attack on
Unconscionability Grounds – *Vasquez v. Greene
Motors, Inc.*, __ Cal. App. 4th __, 2013 WL 1232343
(1st Dist., Mar. 27, 2013)**

Plaintiff purchased a used car on credit from Greene Motors, who then assigned the financing to American Honda Finance Corporation ("Honda"). When plaintiff later sued Greene Motors and Honda in connection with the terms of the financing, defendants petitioned the superior court to compel arbitration under a clause contained in the sales contract. Plaintiff opposed the arbitration petition on the ground that the clause – contained on the back of a complex, one-page, preprinted documents – was procedurally and substantively unconscionable. The trial court agreed and denied defendants' arbitration petition.

On appeal, the First District Court of Appeal, agreed that the arbitration agreement was procedurally unconscionable because it was imposed on plaintiff without the opportunity for negotiation. However, the court found that the level of procedural unconscionability was minimal, and that there was an absence of significant substantive unconscionability. Accordingly, the court of appeal found that the arbitration agreement was enforceable and reversed and remanded with instructions to the trial court to enter an appropriate order directing the matter to arbitration under the terms of the sales contract. In so ruling, the court of appeal rejected plaintiff's various attacks on the clause which plaintiff had claimed were "unfair."

One such attack concerned the allocation of the costs of the arbitration. The contract required Greene Motors to advance the first \$2,500 of the buyer's arbitration costs, with the buyer being responsible for costs above this amount. While there are decisions that have held that it is unconscionable to require arbitration in consumer and finance contracts and to condition that process on the consumer posting fees he or she cannot pay, the court noted that there is no *per se* rule that requiring a plaintiff to pay arbitration costs is unconscionable; that such agreements must be evaluated on a case-by-case basis, with the outcome dependent on the ability of the claimant to pay, the anticipated costs of the arbitration, and the amount in issue in the arbitration. See, *Id.* at *10, citing, *Gutierrez v. Autowest, Inc.*, 114 Cal. App. 4th 77, 97-98 (2003); *Parada v. Superior Court*, 176 Cal. App. 4th 1554, 1580-1581 (2009). Accordingly, the court concluded that in order to demonstrate substantive unconscionability on the grounds of affordability of the required arbitration, plaintiff was required to submit evidence of his own financial resources, the reasonably anticipated cost of this particular arbitration, and the amount of the potential award. Because plaintiff provided no evidence of indigence or the likely cost and value of his arbitration, the court held that he had failed to carry his evidentiary burden. *Id.* at *11.

Another attack concerned the exemption of the remedy of repossession. Plaintiff argued that this provision was one-sided, but the court held that that was "by no means obvious." Repossession is governed by statute and is intended to provide an expeditious remedy for nonpayment without the time and expense of judicial proceedings. Arbitration is an alternative to the judicial process. As such, exempting repossession from the scope of the arbitration clause, preserves the intended efficiency of that self-help remedy. "In this way, the clause merely preserves the status quo; a buyer who has no right to litigate prior to repossession also has no right to arbitrate." *Id.* at *13.

Finally, plaintiff argued that the waiver of class action rights and the requirement to arbitrate "public," statutory claims was impermissible. The court held that both arguments have been foreclosed by the Supreme Court's decision in *Concepcion*. "Although *Concepcion* expressly considered only *Discover Bank's* judicially created ban on class action waivers as unconscionable, the same rationale would require a finding of preemption of the statutory ban on class action waivers in section 1751, which is similarly based on public policy." *Id.* at *13.

F. CHALLENGES TO THE ARBITRATION AWARD

(1) Background Statement

An arbitration proceeding is concluded by the issuance of an award. The only statutory requirements concerning the form of the award is that it must be in writing, signed by the arbitrator, and include a determination of all questions submitted to the arbitrator that must be decided in order to determine the controversy.⁴³ There are, however, rules governing the award process that have been adopted by various provider organizations.⁴⁴

As a matter of statutory law, the arbitrator is not required to issue formal findings of fact or conclusions of law.⁴⁵ Likewise, the arbitrator is not required to disclose his or her rationale or reasons for the award.⁴⁶ However, some provider organizations require that the arbitrator issue an award that includes a statement of the reasons for the award, unless the parties agree otherwise.⁴⁷ Other provider organizations give the parties the option of requesting a “reasoned award” as part of the process.⁴⁸

⁴³ Cal. Civ. Proc. Code § 1283.4.

⁴⁴ The American Arbitration Association (“AAA”) was founded in 1926 and is one of the oldest provider organizations in the world. AAA Manual, pp. 9-10; see also <http://www.adr.org/Welcome>. According to the AAA Commercial Rules, the award “shall be made promptly . . . no later than 30 days from the date of closing the hearing” unless otherwise agreed by the parties or specified by law. AAA Commercial Rules, *supra*, § R-41. JAMS is another large provider organization. According to the JAMS Rules, “the Arbitrator shall render the Award within thirty (30) calendar days after the date of the closing of the Hearing” JAMS Rules, *supra*, Rule 24.

⁴⁵ *Cothron v. Interinsurance Exchange*, 103 Cal. App. 3d 853, 861 (1980).

⁴⁶ *Arco Alaska v. Superior Court*, 168 Cal. App. 3d 139, 148 (1985); *Baldwin Co. v. Rainey Const. Co.*, 229 Cal. App. 3d 1053, 1058 n. 3 (1990). For cases governed by the FAA, see *Bosack v. Soward*, 586 F.3d 1096, 1102 (9th Cir. 2009) (“Arbitrators are not required to set forth their reasoning supporting an award. An arbitrator’s award may be made without explanation of their reasons and without a complete record of their proceedings. [But, if] they choose not to do so, it is all but impossible to determine whether they acted with manifest disregard for the law.”).

⁴⁷ See, e.g., JAMS Rules, *supra*, Rule 24.

⁴⁸ Rule R-42 of the AAA Commercial Rules provides that parties may request a reasoned award but, in order for that request to be binding on the arbitrator, all parties must request such an award in writing and the request must be made prior to the arbitrator’s appointment. Thereafter, a request for a reasoned award is subject to the discretion of the arbitrator. A

An arbitrator's award is not directly enforceable. Until it is confirmed, an award has no more force or effect than a written contract between the parties to the arbitration.⁴⁹ In order to enforce an arbitration award, the prevailing party must ask a judge to confirm the award.⁵⁰ That request is made by filing a petition with the court.⁵¹ For purposes of creating a record in these court proceedings, the petition must name as respondents all parties to the arbitration.⁵² The petition must also set forth the substance of the arbitration agreement or have a copy attached, it must identify the arbitrator; and it must set forth or have attached a copy of the award and the arbitrator's written opinion, if any.⁵³ The petition must be served on all respondents and a noticed hearing must be held similar to the type of proceeding had with respect to a petition to compel arbitration.⁵⁴ Once confirmed, the arbitration award becomes a judgment of the court, has the same force and effect as a judgment in a civil action, and may be enforced like any other judgment of the court in which it is entered.⁵⁵

"reasoned award" means an award that includes "either brief or detailed reasons or a written explanation of the arbitrator's decision." *Arbitration Awards / Safeguarding, Deciding & Writing Awards*, American Arbitration Association at 42 (2004) ("AAA Awards Manual"). The term "reasoned award" is not synonymous with formal findings of fact and conclusions of law. *Id.* Beyond what is stated in the arbitrator's award, parties may not depose the arbitrator to establish and then challenge his or her reasoning. *Hoeft v. MVL Group, Inc.*, 343 F.3d 57, 66-68 (2d Cir. 2003).

⁴⁹ Cal. Civ. Proc. Code § 1287.6; *Jones v. Kvistad*, 19 Cal. App. 3d 836, 840 (1971). However, unless vacated or corrected by the court, an arbitration award is entitled to res judicata and collateral estoppel effect in any subsequent proceedings. *State Farm Mut. Auto. Ins. Co. v. Superior Court*, 211 Cal. App. 3d 5, 14 (1989) (collateral estoppel effect as to issues "actually, necessarily, and finally" resolved in the arbitration proceeding); *Thibodeau v. Crum*, 4 Cal. App. 4th 749, 755 (1992) (res judicata doctrine applies to an arbitration award, even though unconfirmed, and bars subsequent assertion of claims falling within the scope of the arbitration).

⁵⁰ Cal. Civ. Proc. Code §§ 1285, 1287.4.

⁵¹ Cal. Civ. Proc. Code §§ 1288, 1288.4

⁵² Cal. Civ. Proc. Code § 1285; see *Walter v. National Indem. Co.*, 3 Cal. App. 3d 630, 634 (1970).

⁵³ Cal. Civ. Proc. Code § 1285.4.

⁵⁴ Cal. Civ. Proc. Code §§ 1290, et seq.

⁵⁵ Cal. Civ. Proc. Code § 1287.4; see *Britz, Inc. v. Alfa-Laval Food & Dairy Co.*, 34 Cal. App. 4th 1085, 1106 (1995).

An award reached by an arbitrator pursuant to a contractual agreement to arbitrate is not subject to judicial review, except on statutory grounds.⁵⁶ Such relief is sought by petitioning to vacate the award and may be filed by any party.⁵⁷ The scope of judicial review of arbitration awards is extremely narrow and is limited to the specific grounds defined by statute, which are directed at the process, not the substance of the award or the merits of the dispute.⁵⁸ Generally speaking, an arbitrator's decision is not reviewable for errors of fact or law.⁵⁹ Code of Civil Procedure section 1286.2 provides the limited exceptions to this general rule and sets forth the grounds for vacating an award, which include: the arbitrator exceeded his powers and the award cannot be corrected without affecting the merits of the decision;⁶⁰ the award was procured by corruption, fraud or other undue means or corruption in any of the arbitrators;⁶¹ the award was issued by an arbitrator required to disqualify himself or herself;⁶² the rights

⁵⁶ See, 9 U.S.C. § 10(a)(1)-(4); Cal. Civ. Proc. Code § 1286.2(a)(1)-(6); *Moncharsh*, supra, 3 Cal. 4th at 33. Courts may not act sua sponte. Cal. Civ. Proc. Code §§ 1286.4, 1286.8; *Valsan Partners Ltd. P'ship v. Calco Space Facility, Inc.*, 25 Cal. App. 4th 809, 818, 30 Cal. Rptr. 2d 785 (1994).

⁵⁷ *Baldwin v. Rainey Const. Co.*, supra, 229 Cal. App. 3d at 1058.

⁵⁸ In addition to the limited scope of review provided by statute, there is a strong public policy in favor of arbitration and according finality to arbitration awards. *Moncarsh*, supra, 3 Cal. 4th at 32.; *Cotchett, Pitre & McCarthy v. Universal Paragon Corp.*, 187 Cal. App. 4th 1405, 1416 (2010).

⁵⁹ *Moncarsh*, supra, 3 Cal. 4th at 6; *City of Palo Alto v. Service Employees Int'l Union*, 77 Cal. App. 4th 327, 333 (1999).

⁶⁰ 9 U.S.C. § 10(a)(4); Cal. Civ. Proc. Code § 1286.2(a)(4). An arbitrator derives his power solely from parties' arbitration agreement or the stipulation of submission and he has no legal right to decide issues not submitted by the parties. *Moncharsh*, supra, 3 Cal. 4th at 8; *O'Malley v. Petroleum Maintenance Co.*, 48 Cal. 2d 107, 110 (1957); *Luster v. Collins*, 15 Cal. App. 4th 1338, 1346 (1993). A party's failure to request the arbitrator to determine a particular issue within the scope of the arbitration is not a basis for vacating or correcting an award. *Corona v. Amherst Partners*, 107 Cal. App. 4th 701, 706 (2003). Arbitrators do not exceed their powers because they assign erroneous reasons for their decision. *Moncharsh*, supra, 3 Cal. 4th at 28. The focus of this inquiry is on whether arbitrators had the power, based on the parties' submissions, to reach a certain issue, not whether the arbitrator correctly decided the issue. *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 824 (2d Cir. 1997).

⁶¹ 9 U.S.C. § 10(a)(1); Cal. Civ. Proc. Code §§ 1286.2(a)(1), 1286.2(a)(2). This ground for vacatur applies to extrinsic fraud perpetrated by the arbitrator or a party (i.e., fraud which deprives the party of a fair hearing). *Pacific Crown Dist v. Brotherhood of Teamsters, Etc.*, 183 Cal. App. 3d 1138, 1147 (1986). It also applies to "undue" behavior which deprives a party of a "hearty 'first bite'." *Pour Le Bebe, Inc. v. Guess? Inc.*, 112 Cal. App. 4th 810, 831 (2003).

⁶² 9 U.S.C. § 10(a)(2); Cal. Civ. Proc. Code § 1286.2(a)(6). Arbitrators conducting arbitrations in California must comply with the Judicial Council ethics standards which require that an arbitrator make extensive conflict disclosures to the parties before accepting the appointment and hearing the dispute. Cal. Civ. Proc. Code §§ 1281.85, 1281.9 and 1281.91. An arbitrator's

of the party challenging the award were substantially prejudiced by the arbitrator's refusal to postpone the hearing despite sufficient cause shown for a postponement, his or her refusal to hear evidence material to the controversy or other misconduct.⁶³ Additionally, both state and federal common law recognize a "public policy" exception to confirmation of an award, which allows courts to refuse to enforce an arbitration award that violates well-defined public policy.⁶⁴

failure to comply with the disclosure requirements may be ground for disqualification of the arbitrator and for vacatur of any award issued. *Ovitz v. Schulman*, 133 Cal. 4th 830 (2005). Likewise, an arbitrator's failure to honor a demand for disqualification after making the required conflict disclosures mandates vacatur of any award issued. *Azteca Const., Inc. v. ADR Consulting, Inc.*, 121 Cal. App. 4th 1156, 1168-1169 (2004). An arbitrator's mere failure to disclose a conflict is not a basis for vacatur under the FAA. Proof of evident partiality is required under the FAA. 9 U.S.C. § 10(a)(2); *ANR Coal Co., Inc. v. Cogentrix of North Carolina, Inc.*, 173 F.3d 493, 499-500 (4th Cir. 1999).

⁶³ 9 U.S.C. § 10(a)(3); Cal. Civ. Proc. Code § 1286.2(a)(5). Arbitrators are required to decide all questions submitted that are necessary to determine the controversy. Cal. Civ. Proc. Code § 1283.4. Failure to do so may constitute "other conduct" for vacatur. *Muldrow v. Norris*, 12 Cal. 331 (1859). A party challenging an award on this ground bears the a "heavy burden" because it is presumed that all issues submitted have been decided. *Rodrigues v. Keller*, 113 Cal. App. 3d 838, 841 (1980). To overcome that presumption, the party challenging the award must show that its claims were expressly raised and not decided by the arbitrator. *Id.* This is difficult to do because findings are usually not required or part of the award. *Id.* In the case of a monetary award without findings, the decision that one of the parties should pay the other a sum of money "is sufficiently determinative of all items embraced in the submission." *Sapp v. Barenfeld*, 34 Cal. 2d 515, 522-523 (1949).

⁶⁴ In 1987, the United States Supreme Court held that courts can decline to enforce an arbitrator's award where enforcement "would violate 'some explicit public policy' that is 'well defined and dominant, and is to be ascertained by reference to the laws and legal precedents and not from general considerations of supposed public interests.'" *United Paperworkers' Int'l Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 43 (1987); see also *Exxon Shipping Co. v. Exxon Seamen's Union*, 11 F.3d 1189, 1191-1192 (3d Cir. 1994) (vacating labor arbitration award that required the reinstatement of a seaman who was found to be highly intoxicated while on duty), or a party's statutory rights. *Board of Education, Etc. v. Round Valley Teachers Ass'n*, 13 Cal. 4th 269, 277 (1996) (vacating arbitration award that required school district to comply with collective bargaining agreement procedure for termination a probationary teacher which was preempted by conflicting Education Code provisions). This exception arises out of the contract defense to enforcement where a contract is found to violate public policy. *Vimar Seguros y Reaseguros S.A. v. M/V Sky Reefer*, 515 U.S. 528, 540 (1995). This exception derives legitimacy from the public's interest in having its views represented in matters to which it is not a party but which could harm the public interest. *Seymour v. Blue Cross/Blue Shield*, 988 F.2d 1020, 1023 (10th Cir. 1993); see also *Di Russa v. Dean Witter Reynolds, Inc.*, *supra*, 121 F.3d at 824-825.

For arbitrations governed by the FAA, there are two additional, common law grounds for seeking vacatur of an award that come awfully close to looking like de novo review for errors of law..⁶⁵ The first is the “manifest disregard” of the law exception and allows the award to be vacated where the arbitrator knew applicable law but ignored or refused to apply it,⁶⁶ or where an obvious error of law exists.⁶⁷ The second is the “arbitrary and capricious” exception and allows the award to be vacated where no ground for the decision can be inferred from the facts, which is not yet uniformly accepted.⁶⁸

⁶⁵ AAA Awards Manual, *supra*, p. 10.

⁶⁶ Under Section 10 of the FAA, vacatur is appropriate where it is evident that “the arbitrators exceeded their powers or so imperfectly executed them that a mutual, final and definite award upon the subject matter submitted was not made. “[A]rbitrators exceed their powers in this regard not when they merely interpret or apply the governing law incorrectly, but when the award is completely irrational, or exhibits a manifest disregard of the law.” *Kyocera Corp. v. Prudential Bache Trade Serv. Inc.*, 341 F.3d 987, 997 (9th Cir. 2003) (en banc). “Manifest disregard of the law means something more than just an error in the law or a failure on the part of the arbitrators to understand or apply the law.” *Lagstein v. Certain Underwriters at Lloyd’s, London*, 607 F.3d 634, 641 (9th Cir. 2010), citing *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995). See, e.g., *Comedy Club, Inc. v. Improv West Assoc.*, 553 F.3d 1277, 1287 (9th Cir. 2009) (vacatur for manifest disregard of the law where injunction award included collateral relatives not in privity who, under California law, the arbitrator lacked authority to enjoin); see also *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056 (9th Cir. 1991) (vacatur allowed for arbitrator’s manifest disregard of the law).

⁶⁷ See, e.g., *International Telepassport Corp. v. USFI, Inc.*, 89 F.3d 82 (2d Cir. 1996) (vacatur allowed for error of law which is obvious and capable of being instantly perceived by the average arbitrator); *Roadway Package System, Inc. v. Kayser*, 257 F.3d 287 (3d Cir. 2000), cert denied, 534 U.S. 1020 (2001) (same); see also *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989); *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995); *Halligan v. Pipe Jaffray, Inc.*, 148 F.3d 197 (2d Cir. 1998); *Tanoma Mining Co. v. Local Union No. 1269*, 896 F.2d 745 (3d Cir. 1990); *Bowen v. Amoco Pipeline Co.*, 254 F.2d 925 (10th Cir. 2001).

⁶⁸ See, e.g., *Montes v. Shearson Lehman Bros., Inc.*, 128 F.3d 1456, 1458 (11th Cir. 1997). If no ground for the decision can be inferred from the facts, the award may be vacated as arbitrary and capricious. *Brown v. ITT Consumer Fin. Corp.*, 211 F.3d 1217, 1223 (11th Cir. 2000). Likewise, if an award is “so palpably faulty that no judge . . . could ever conceivably have made such a ruling,” the award may be vacated as arbitrary and capricious. *Safeway Stores v. Am. Bakery & Confectionary Workers, Local 111*, 390 F.2d 79, 82 (5th Cir. 1968). The award may also be vacated if it is found to be “completely irrational.” *French v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 784 F.2d 902, 906 (9th Cir. 1986); *G.C. & K.B. Investments, Inc. v. Wilson*, 326 F.3d 1096 (9th Cir. 2003) (same).

For arbitrations governed by the FAA, Section 10 provides the exclusive means by which a court reviewing an arbitration award may grant vacatur. While arbitration is a creature of contract, the United States Supreme Court ruled in 2008 that Section 10 provides the exclusive grounds for vacatur; that parties may not contract between themselves for an expanded scope of review.⁶⁹

The rule is different for arbitrations governed by the California Arbitration Act. In 2008, the California Supreme Court relied on the United States Supreme Court's statement in *Hall Street* that "[t]he FAA is not the only way into court for parties wanting review of arbitration awards: they may contemplate enforcement under state statutory or common law, for example, where judicial review of different scope is arguable,"⁷⁰ to conclude that *Hall Street* did not foreclose a more searching merits review of arbitral awards when done so under authority other than the FAA.⁷¹ The California Supreme Court went on to hold that "the CAA established the statutory grounds for judicial review with the expectation that arbitration awards are ordinarily final and subject to a restricted scope of review, but that parties may . . . provid[e] for review of the merits in the arbitration agreement."⁷²

In addition to judicial review at the trial court level through the petition to confirm or vacate process, any judgment entered on the award is appealable⁷³ and is subject to the rules and procedures applicable generally to appeals of civil judgments. Likewise, an order denying a petition to confirm the award is appealable.⁷⁴ The scope of this appellate review is limited, however, to whether the trial court erred in granting or denying a petition to confirm or vacate the arbitration award. It does not extend to a review of the merits of the arbitration award or to de novo review of the arbitration proceedings. The appellate court must accept the trial court's findings of fact if substantial evidence supports them and must draw every reasonable inference to

⁶⁹ See, *Hall St. Assoc., LLC v. Mattel, Inc.*, 552 U.S. 576, 584 (2008).

⁷⁰ 552 U.S. at 552..

⁷¹ See, *Cable Connection, Inc. v. DirecTV, Inc.*, 44 Cal. 4th 1334, 1354-1355 (2008).

⁷² 44 Cal. 4th at 1364.

⁷³ Cal. Civ. Proc. Code § 1294(d). An appeal from a judgment confirming an arbitration award is subject to a finality requirement. If other issues remain unresolved in the trial court, the judgment confirming the arbitration award is not final and cannot be appealed. *Rubin v. Western Mut. Ins. Co.*, 71 Cal. App. 4th 1539, 1547-1548 (1999) (award only appraised the amount of earthquake damage, liability phase still awaited trial on the merits).

⁷⁴ Cal. Civ. Proc. Code § 1294(c); *Ray Wilson Co. v. Anaheim Mem. Hosp. Ass'n*, 166 Cal. App. 3d 1081, 1085 n. 1 (1985).

support the award.⁷⁵ On issues concerning whether the arbitrator exceeded his or her powers, the appellate court reviews the trial court's decision de novo, but must give substantial deference to the arbitrator's assessment of his or her contractual authority.⁷⁶

(2) **Cases**

(a) **Arbitrator's Failure to Provide a Written Explanation of His Award was not Grounds for Vacatur Under the FAA – *Biller v. Toyota Motor Corp.*, 668 F.3d 655 (9th Cir., Feb. 3, 2012)**

Biller worked as an in-house attorney for Toyota for four years. In 2007, Biller presented Toyota with a claim for constructive wrongful discharge related to Toyota's alleged unethical discovery practices. Toyota and Biller settled that dispute and, as part of the settlement, the parties signed a Severance Agreement in which Biller agreed not to copy or disclose Toyota's confidential information and agreed to return all of Toyota's confidential information in his possession. The Severance Agreement included a binding arbitration agreement with respect to all claims relating to the interpretation, application or alleged breach of said agreement.

After settling with Toyota, Biller started Litigation, Discovery and Trial Consulting, a consulting business that provided seminars on various legal topics. On his website, Biller used information about his work at Toyota which Toyota believed to be confidential information covered by the Severance Agreement, as well as confidential information protected by the attorney-client privilege. The parties asserted various claims in their respective state and federal court actions. They later stipulated that their respective claims would be consolidated and submitted to binding arbitration before the Honorable Gary L. Taylor (ret.). After a two-week arbitration, the arbitrator awarded Toyota injunctive relief, \$2.5 million in liquidated damages and \$100,000 in punitive damages. The award was confirmed over Biller's objection and request for vacatur.

⁷⁵ *Alexander v. Blue Cross of Calif.*, 88 Cal. App. 4th 1082, 1087 (2001); *Pierotti v. Torian*, 81 Cal. App. 4th 17, 24 (2000).

⁷⁶ *Alexander v. Blue Cross of Calif.*, supra, 88 Cal. App. 4th 1082; *California Faculty Assn. v. Superior Court*, 63 Cal. App. 4th 935, 944-945 (1998); *Advanced Micro Devices, Inc. v. Intel Corp.*, 9 Cal. 4th 362, 373, 376 fn. 9 (1994).

On appeal, Biller argued that the district court erred by considering the award under the limited review authorized by the FAA rather than the more expansive review available under the CAA in cases where the parties contract for such expanded judicial review. The Ninth Circuit rejected that argument because, while the Severance Agreement stated that it would be governed by and construed in accordance with California law, the arbitration clause expressly stated that the arbitration agreement would be governed by the FAA.

Biller next argued that the arbitrator exceeded his powers under the Severance Agreement first by not providing a written explanation of his award sufficient to provide for judicial review and second by failing to address Biller's affirmative defenses under California law. With regard to the first argument, Biller pointed to the language in the Severance Agreement requiring the arbitration to "issue with his/her award a written decision sufficient to permit limited judicial review to enforce or vacate the arbitration award." The district court held that the arbitrator's written decision was sufficient to provide for the limited review authorized by the FAA: namely, whether the arbitrator manifestly disregarded the law or made an irrational decision. The Ninth Circuit agreed, noting that Biller's argument was focused on the writing's ability to facilitate a review on the merits, which was not available under the FAA.

With regard to Biller's argument that the arbitrator's decision demonstrated manifest disregard of the law because he did not apply California law regarding his affirmative defenses of unclean hands and equitable estoppel. The district court ruled that by virtue of the arbitrator's decision on the merits of the dispute, it was implicit that Biller's affirmative defenses had been rejected. The Ninth Circuit reviewed the prima facie elements of each defense and agreed with the district court.

**(b) Award Procured by Undue Means - *Maaso v. Signer*,
203 Cal. App. 4th 362 (2nd Dist., Mar. 1, 2012)**

Patient brought a medical malpractice action against his neurologist, which was submitted to arbitration before a three-arbitrator panel consisting of two party arbitrators and a neutral arbitrator selected by the party arbitrators. After the record was closed and the neutral arbitrator was deliberating on the issue of causation, the party arbitrator for the defendant faxed an ex parte, post-arbitration brief to the neutral arbitrator on the issue of causation. Four days later, the neutral arbitrator issued his arbitration award in which he concluded that while the defendant was negligent, the plaintiff had failed to meet his burden of proof on causation. Plaintiff petitioned to vacate the award. The trial court granted that petition, finding that defendant's post-arbitration letter brief to the neutral arbitrator had resulted in ex parte contact while the award was pending; that the ex parte contact "could have influenced" the award and

thus called into question “the irregularity and integrity of the decision-making process”; and that “undue means were employed that caused the Award to issue.” The trial court then ordered a new arbitration hearing before a different neutral arbitrator, which resulted in an award in favor of plaintiff for \$594,243, which was confirmed. Defendant appealed and claimed that the trial court had erred in vacating the first arbitration award. On appeal, the Court of Appeal held that the ex parte brief was an act that undermined the fairness and integrity of the arbitration process because a fair hearing process requires notice, the opportunity to be heard, the opportunity to present relevant and material evidence and argument to the decision makers, and for plaintiff to “have the last word.”

In connection with the vacatur challenge, the neutral arbitrator offered a declaration that he considered but did not rely on the ex parte brief in reaching his decision. Plaintiff objected to the arbitrator’s declaration on the grounds that his statement was inadmissible under Evidence Code §703.5, which limits the testimony of the arbitrator whose decision is being challenged on grounds to bias to that which addresses the charge of bias, partiality or improper conduct.” The merits of the controversy, the manner in which evidence was weighed or the mental processes of the arbitrators in reaching their decision are not subject to judicial review. The Court of Appeal concluded that because the portions of the arbitrator’s declaration did not fall within any of the statutory exceptions, the trial court did not err in excluding this evidence.

**(c) Legal Error by Arbitrator Deprived Party of
Unwaivable Statutory Right and Thus Warranted
Vacatur - *Richey v. Auto/Nation*, 210 Cal. App. 4th
1516 (2nd Dist., Dec. 12, 2012)**

In 2008, employer terminated a sales manager before the expiration of his approved medical leave because, after a superficial investigation, the employer believed he was misusing his leave by working in a restaurant he owned. The employee then sued the employer for violation of his CFRA rights. The employee’s claims were submitted to arbitration under the terms of a mandatory employment arbitration agreement, and an 11-day hearing was conducted. The arbitrator denied the employee’s claim based on the so-called “honest belief” defense. In 2010, the trial court denied the employee’s motion to vacate and granted the employer’s petition to confirm the award and enter judgment. The employee appealed. On appeal, the Second District Court of Appeal reversed the judgment under Code of Civil Procedure § 1286.2(a)(4) (arbitrator exceeded his powers) because it found that the arbitrator had committed “clear legal error” in basing his decision solely on the “honest belief” defense and not properly allocating the burden of proof on the employer to prove an employee’s misuse

of CFRA leave. “[N]o California case supports the arbitrator’s conclusion an employer may rely solely on its subjective, albeit honest, belief an employee has engaged in misconduct to justify its denial of an employee’s CFRA rights.” In opening the decision, the court of appeal acknowledged the long line of California Supreme Court cases limiting judicial review of arbitration awards to “circumstances involving serious problems with the award itself, or with the fairness of the arbitration process,” and noted that it is “within the power of the arbitrator to make a mistake either legally or factually.” However, relying on the Supreme Court’s 2010 decision in *Pearson Dental Supplies, Inc. v. Superior Court* (2010) 48 Cal. 4th 665, the court of appeal concluded in the context of nonwaivable statutory rights, the Supreme Court had left open the door for a broader level of judicial review so as to make sure that employees have had the opportunity to vindicate their statutory rights. The court of appeal also found grounds to vacate the arbitration award due to the arbitrator’s failure “to make relevant findings of fact and conclusions of law related to the employee’s CFRA claims. The matter was remanded with directions to conduct further proceedings not inconsistent with the opinion, including a further arbitration before a new or the original arbitrator.

(d) Award Vacated Because it Violated an Explicit Legislative Expression of Public Policy - *Ahdout v. Hekmatjah*, 213 Cal. App. 4th 21 (2nd Dist., Jan. 25, 2013)

In 2002, an individual (Ahdout) entered into a real property investment/development arrangement with a family limited partnership (Hekmatjah). The principal of the family limited partnership (Braum) served as the “manager” of the company. Braum was specifically authorized to enter into a contract with his investment and development company (BIDI) to construct the contemplated condominium development project. While any services Braum might render as “manager” of the company were to be uncompensated, BIDI was to be paid for its services related to the construction of the condominium project. The project was built and the certificate of occupancy was issued in January 2008 – at about the time that the financial crisis and resulting decline in real estate occurred. Not surprisingly, disputes arose between the two investors. Pursuant to their initial agreement, those disputes were submitted to arbitration. The arbitration was conducted over 27 days, at the end of which the arbitrators issued a decision that awarded construction costs to BIDI (Braum’s affiliate company) over Ahdout’s objection that BIDI was not a licensed contractor and, as such, was legally not entitled to be paid (or to enforce an agreement to be paid) for construction services under California’s Contractor’s State License Law. The arbitration award was confirmed over Ahdout’s objection because the trial court deferred to the arbitrator’s determination that the Hekmatjah parties had not performed unlicensed contracting work on the project so that the Contractors’ State License Law

was inapplicable. Ahdout appealed and the judgment was reversed. The court of appeal held that while the arbitration award was not within the exception to reviewability for awards enforcing illegal contracts, the arbitrators had nevertheless exceeded their powers by issuing an award that violated an explicit legislative expression of public policy – namely, Contractor’s State License Law. The court of appeal remanded the matter back to the trial court to conduct a de novo review of the evidence to determine whether Section 7031 of the Contractor’s State License Law is applicable and instructed the trial court that the arbitrators’ finding that BIDI did not function as a general contractor on the project was not binding on the trial court; that the trial court must independently consider this defense after taking into account all of the admissible evidence submitted to it regardless of whether that evidence was before the arbitrator.

(e) Arbitrators Did Not Exceed Their Power by Conducting the Evidentiary Hearing with Just Two of a Three-Member Panel – *Hotels Nevada v. L.A. Pacific Center, Inc.*, 203 Cal. App. 4th 336 (2nd Dist., Feb. 17, 2012)

This matter involves a complex set of legal proceedings between the seller and buyer of a hotel and apartment complex located in Las Vegas, Nevada. After several years of skirmishing in the trial and appellate courts, the matter was ordered to arbitration before a three-arbitrator panel. The parties selected an arbitration panel through JAMS. The panel presided over and ruled on several prehearing motions and in early 2009 conducted a 20-day arbitration. After the first week of arbitration hearings, one of the arbitrators had to undergo surgery and was unable to be physically present during the remainder of the arbitration. One party objected, but the panel determined that the Commercial Rules of the AAA (the rules governing the arbitration) permitted the arbitration to proceed as scheduled. The missing arbitrator was given a transcript and video disk each day, along with a copy of the exhibits identified by witnesses. After the presentation of the evidence and the submission of the post hearing briefs, the panel collectively deliberated, decided the matter and issued an award. The award was in favor of the buyer, and the selling party filed a motion to vacate the award on various grounds. Among the grounds was the contention that the arbitrators had exceeded their powers by proceeding with the arbitration once one arbitrator could not physically be present due to his need to undergo an unanticipated surgery because the arbitration agreement provided that all claims would be settled by a three-arbitrator panel. Over the seller’s objections and request for vacatur, the trial court confirmed the award, and seller appealed.

The Second District Court of Appeal affirmed the trial court, holding that the panel did not exceed its powers in proceeding during one arbitrator's medical absence because the AAA Rules governing the arbitration allow the remaining panel arbitrators to continue with the hearing and determination of the controversy in the event of a vacancy. Moreover, the procedure employed by the panel did not violate any provision of the parties' agreement. The agreement provided only that any arbitrable claims would be settled by three arbitrators, it did not mandate that the arbitration hearing be conducted in such a manner so as to imply that the physical presence of all three arbitrators was necessary.

F. MISCELLANEOUS

(1) Pre-Judgment Interest on Awards - *Tenzera, Inc. v. Osterman*, 205 Cal. App. 4th 16 (2nd Dist., Apr. 19, 2012)

After obtaining an arbitration award against a contracting company and its owners (the Tenzeras), the prevailing homeowners (the Ostermans) filed a petition to confirm the award and also requested prejudgment interest from the date of the arbitration award. The Tenzeras responded with a petition to vacate the award on the grounds that they had not voluntarily consented to the arbitration. The trial court vacated the award as to all parties even though the company did not seek to vacate the award. The Ostermans appealed, and in *Tenzera I*⁷⁷ the Second District Court of Appeal held that the trial court had erred in vacating the entire arbitration award, and should have modified the award to reflect that only the company was liable. The matter was remanded for a determination of the parties' respective motions for attorney's fees and the Osterman's motion for prejudgment interest. Both requests for attorney's fees were denied. The trial court granted the Osterman's request for prejudgment interest, but did not award the interest that would have accrued during the pendency of the first appeal in *Tenzera I*. The Ostermans took another appeal. As a matter of first impression, the court of appeal reversed the trial court and held that the Ostermans were entitled to prejudgment interest from the date of the award, including the period during which the appeal of the vacatur decision was pending. In reaching this decision, the court of appeal cited established case law holding that Civil Code § 3287 applies to judgments on arbitration awards, and that a prevailing party in arbitration is entitled to prejudgment interest from the date of the award through entry of judgment. Finding no applicable exception, the court held that where a trial court vacates an arbitration

⁷⁷ See, *Tenzera, Inc. v. Osterman*, 2010 WL 186253 (Jan. 21, 2010) (nonpub. opn.)

award that is later reinstated after appeal, prejudgment continues to accrue on the award during the pendency of the appeal of the vacatur decision.

(2) Implicit Waiver of Right to Arbitration by Not Funding the Required Advance Deposit

(a) *Cinel v. Christopher*, 203 Cal. App. 4th 759 (2nd Dist., Jan. 20, 2012)

In 2008, an investor in a limited liability company brought suit against the LLC's founding members for securities fraud and related claims. Based upon the arbitration clause contained in the private placement memorandum, one of the defendants (George Barna) petitioned to compel arbitration. That petition was granted in early 2009 and an arbitration was commenced with the AAA. By January 2010, the parties had selected a panel of three arbitrators for which they were billed for the arbitrators' advance fee deposit. The fee deposit was allocated pro rata between seven parties (one plaintiff and six defendants). When several of the defendant parties did not pay their share of the deposit, the AAA suspended the proceedings. Plaintiff suggested that if the petitioning defendant wished to continue in arbitration, he should pay the fee deposit of his non-paying co-defendants. Defendant's response was that plaintiff had greater means to do so because he was a billionaire. In any event, when the fee deposit was not fully funded, the panel terminated the arbitration for nonpayment of fees as allowed under the AAA Commercial Rules. One of the paying defendants (Richard Christopher) then petitioned the court to confirm the panel's termination ruling and dismiss plaintiff's complaint. The trial court denied that request, finding that termination of the arbitration did not constitute an award subject to confirmation. That ruling was affirmed on appeal.

(b) *Cinel v. Barna*, 206 Cal. App. 4th 1383 (2nd Dist., May 18, 2012)

As a follow along to the *Cinel v. Christopher* case (discussed above), when the matter was returned to the superior court in late 2010, the two defendants who had funded their portion of the arbitrators' fee deposit, filed petitions seeking compel arbitration for arbitration. Plaintiff opposed, contending that Barna and Christopher had waived their right to arbitration by failing to pay the fees for the arbitration they had compelled. The trial court's tentative was to deny the motion to compel unless the parties could work something out with regard to payment of the non-paying parties' share of the fees. Plaintiff refused to pay any portion of the non-paying parties' share of the fees and the petitioning defendant (Barna) advised the court that he could not afford to pay those fees. Accordingly, the trial court denied the motion. This appeal followed. On appeal, the trial court's denial was affirmed. The court of appeal held that by

refusing to agree among themselves to pay the fees of the nonpaying parties, both plaintiff and defendant Barna had waived the arbitration agreement “by their collective and simultaneous repudiation of it” through their inability to reach an agreement over the payment of fees. “By failing to come to an agreement that would permit them to proceed with the arbitration, the parties have collectively waived their right to arbitrate.” Because he waived his right to claim the benefits of the agreement, the court of appeal held that Barna could not unilaterally assert the right to arbitration. Referring to the Ninth Circuit’s decision in *Sink v. Aden Enterprises, Inc.* (9th Cir. 2003) 352 F.3d 1197, the court of appeal expressed concern that if the matter was returned to arbitration, Barna could refuse to pay his share of the fee deposit, which would result in another termination for nonpayment of fees and further postponement of the litigation (keeping in mind that it was now May 2012 and the litigation was commenced in 2008).

II.

MEDIATION – SIGNIFICANT CASES

A. MEDIATION CONFIDENTIALITY & MEDIATION PRIVILEGE

(1) Background Statement

In opening a mediation session, it is fairly routine for the mediator to promise comprehensive confidentiality to the participants. While there are a number of statutes, rules, and cases that support confidentiality in mediation, a certain amount of skepticism and concern exists regarding the scope of protection that actually exists. The uncertainty about the nature and extent of what confidentiality protections exist for things said in mediation is especially apparent in federal court litigation disputes.⁷⁸ Both state and federal courts recognize that a theoretical component of mediation is confidentiality, but while California has express statutory provisions that provide for confidentiality protections, and numerous California Supreme Court decisions endorsing those protections, no similar protections are available under federal law. The scope of protection available under federal law is unclear and minimal at best. A detailed discussion of the statutory and case law governing mediation confidentiality protection under California law as compared to federal law can be found in Rebecca Callahan’s recent article, *Mediation Confidentiality: For California Litigants, Why Should*

⁷⁸ See DWIGHT GOLANN, *MEDIATING LEGAL DISPUTES* 218-220 (2009); Dennis Sharp, *The Many Faces of Mediation Confidentiality*, in *HANDBOOK ON MEDIATION* 223-236 (2d ed. 2010).

Mediation Confidentiality be a Function of the Court in Which the Litigation is Pending? 12 Pepp. Disp. Resol. L.J. 63 (2012).

(2) Federal Perspective – Ninth Circuit

(a) Background Statement

The starting place for understanding the federal perspective on mediation confidentiality is the common law rule that (a) the public is entitled to every person's evidence, and (b) testimonial privileges are disfavored. Fed. R. Evid. 408(b)(1)-(2). There is no federal statute, rule of procedure, or rule of evidence that expressly recognizes or provides confidentiality protection for communications during or in connection with a mediation. The only express protection for settlement discussions is provided by Rule 408 of the Federal Rules of Evidence, which makes "conduct or statements made in compromise negotiations regarding the claim" inadmissible to prove liability. Thus, Rule 408 provides an admission standard for proof offered at trial to prove liability or invalidity of a claim and speaks in terms of *relevancy*. Its purpose is "to encourage the compromise and settlement of existing disputes"⁷⁹ so as to avoid "the chilling effect" that potential disclosure might have on a party's willingness to make a compromise offer for fear of jeopardizing its case or defense if the matter is not settled.⁸⁰

It is important to note that, by its terms, Rule 408(a) applies only to the *admissibility* of evidence at trial and does *not* apply to *discovery* of settlement negotiations or settlement terms. On this issue, the courts are split as to whether Rule 408 precludes discovery.⁸¹ Moreover, Rule 408(b) expressly provides that exclusion is not required if the "offer and compromise" evidence is offered for a purpose that is not expressly prohibited by Rule 408(a). Fed. R. Evid. 408(b). Among the "permitted uses" delineated in Rule 408(b) are evidence of settlement and compromise negotiations offered (1) to prove bias or prejudice on the part of a witness; (2) to prove that an alleged wrong was committed during the negotiations (e.g., libel, assault, unfair labor practice, etc.); (3) to negate a claim of undue delay; or (4) to prove obstruction of a

⁷⁹ *Josephs v. Pac. Bell*, 443 F.3d 1050, 1064 (9th Cir. 2006).

⁸⁰ *Molina v. Lexmark Int'l, Inc.*, No. CV 08-04796 MMM (FMx), 2008 WL 4447678, at *11-12 (C.D. Cal. Sept. 30, 2008).

⁸¹ Compare *Bottaro v. Hatton Assocs.*, 96 F.R.D. 158, 160 (E.D.N.Y. 1982) (barring discovery of settlement terms), with *Bennett v. La Pere*, 112 F.R.D. 136, 139-40 (D.R.I. 1986) (allowing discovery of settlement discussions), and *NAACP Legal Def. & Educ. Fund, Inc. v. U.S. Dep't of Justice*, 612 F. Supp. 1143, 1146 (D.D.C. 1985) (allowing discovery if information is relevant to other issues in the pending action).

criminal investigation or prosecution. Additionally, a number of courts, including the Ninth Circuit, have concluded that Rule 408 does not make settlement offers inadmissible in the removal context where such offers represent evidence of the amount in controversy for the purpose of establishing the date on which such information was first made available to the defendant and thus started the thirty-day time period for removing a state court action to federal court.⁸² Numerous district court decisions have used the settlement letter to establish the amount in controversy.⁸³

In sum, Rule 408 is keenly focused on offers of compromise and negotiations involved in making, accepting, or rejecting such offers. As such, Rule 408 appears *not* to provide protection of any sort for prenegotiation communications or exchanges of information that parties might have with or through a mediator, even though the goal of those discussions is to open settlement dialogue.

The only other source of confidentiality protection in federal cases is Rule 501 of the Federal Rules of Evidence. Rule 501 empowers the holder of a recognized privilege to use the legal process to prevent others from disclosing protected communications. It also vests the holder with the right to refuse to produce otherwise relevant evidence. What qualifies as a “recognized privilege” is *not* detailed in Rule 501. In federal question cases under 28 U.S.C. § 1331, the extent to which a privilege exists is governed by federal common law⁸⁴ and may not be augmented by local court rules.⁸⁵ In diversity

⁸² See, *Babasa v. LensCrafters, Inc.*, 498 F.3d 972 (9th Cir. 2007) (holding that a letter sent by plaintiffs estimating the amount alleged put defendant on notice of the amount in controversy); *Cohn v. Petsmart, Inc.*, 281 F.3d 837 (9th Cir. 2002) (“A settlement letter is relevant evidence of the amount in controversy if it appears to reflect a reasonable estimate of the plaintiff’s claim.”).

⁸³ See *Munoz v. J.C. Penny Corp.*, No. CV09-0833 ODW (JTLx), 2009 WL 975846 (C.D. Cal. Apr. 9, 2009) (settlement proposal letter was admissible to establish that the jurisdictional amount in controversy had been met for purposes of removing the case to federal court); see also *Ray v. Am. Airlines, Inc.*, No. 08-5025, 2008 WL 3992644, *4 (W.D. Ark. Aug. 22, 2008) (settlement letter used to establish the amount in controversy); *Haydel v. State Farm Mut. Auto. Ins. Co.*, No. CIVA 07-939-C, 2008 WL 2781472, *8, n.8 (M.D. La. July 10, 2008); *Finnegan v. Wendy’s Int’l, Inc.*, No. 2:08-cv-185, 2008 WL 2078068, *3 (S.D. Ohio May 13, 2008); *Sulit v. Slep-Tone Entm’t*, No. C06-00045 MJJ, 2007 WL 4169762, *3, n.1 (N.D. Cal. Nov. 20, 2007); *Turner v. Baker*, No. 05-3298-CV-S-SWH, 2005 WL 3132325, *3 (W.D. Mo. Nov. 22, 2005); *LaPree v. Prudential Fin.*, 385 F. Supp. 2d 839, 849, n.9 (S.D. Iowa Aug. 17, 2005).

⁸⁴ *Id.* See also *Religious Tech. Ctr. v. Wollersheim*, 971 F.2d 364, 367, n.10 (9th Cir. 1992). Rule 501 raises a difficult question regarding which law shall apply in federal question cases with pendent state law claims. In the Ninth Circuit, that question has been resolved so that the law of privilege is governed by federal common law. *Id.* at n.10 (court refused to apply California litigation privilege in copyright action with pendent state law claims); *Folb v. Motion Picture*

cases under 28 U.S.C. § 1332, where state law provides the rule of decision, the existence of a privilege is a matter of applicable state law.⁸⁶ To date, there are only two cases in the Central District of California that have recognized a federal mediation privilege to protect communications made in conjunction with a formal mediation proceeding: the 1998 reported decision of District Judge Paez in *Folb v. Motion Picture Industry Pension & Health Plans*⁸⁷ and the 2008 unreported decision of District Judge Morrow in *Molina v. Lexmark International, Inc.*,⁸⁸ both of which are discussed in the Callahan Article.

The federal cases discussed in this section of the materials are a continuation of the dialogue being had in the federal courts in an effort to understand mediation as a dispute resolution process distinguishable from a settlement negotiation between the

Indus. Pension & Health Plans, 16 F. Supp. 2d 1164, 1169-70 (C.D. Cal. 1998) (stating that the federal common law of privileges governs both federal and pendent state law claims in federal question cases); see also *Hancock v. Hobbs*, 967 F.2d 462, 467 (11th Cir. 1992) (per curiam) (the federal law of privilege is paramount in federal question cases even if the witness testimony is relevant to a pendent state law count which may be controlled by a contrary state law privilege); *Hancock v. Dodson*, 958 F.2d 1367, 1373 (6th Cir. 1992) (holding that the federal law of privilege is paramount to federal question cases).

⁸⁵ See *Facebook, Inc. v. Pac. Nw. Software, Inc.*, 640 F.3d 1034, 1040-41 (9th Cir. 2011) (“A local rule, like any court order, can impose a duty of confidentiality as to any aspect of litigation, including mediation. . . . But privileges are created by federal common law.”) In *Facebook*, the Winklevosses sought to avoid enforcement of the settlement agreement between ConnectU and Facebook which was negotiated and entered into during a private mediation. *Id.* at 1040. The Winklevosses proffered evidence of what was and was not said during the mediation. *Id.* The District Court for the Northern District of California excluded this evidence under its local rule that protected such communications as “confidential information,” which the court read as creating a “privilege” for “evidence regarding the details of the parties’ negotiations in their mediation.” *Id.* at 1040. While the Ninth Circuit found that the district court’s reason for excluding the evidence was wrong, it concluded that the court was nevertheless correct in excluding the proffered evidence because the parties had engaged with a private mediator and had signed an express written confidentiality agreement before the mediation commenced. *Id.* at 1041. Accordingly, the Ninth Circuit held that the confidentiality agreement signed by the Winklevosses precluded them from introducing “any evidence of what Facebook said, or did not say, during the mediation.” *Id.*

⁸⁶ FED. R. EVID. 501. See also *Olam v. Cong. Mortg. Co.*, 68 F. Supp. 2d 1110, 1124-25 (N.D. Cal. 1999). That being said, federal law governs whether a case exceeds the amount in controversy requirement. See *Molina v. Lexmark Int’l, Inc.*, No. CV 08-04796 MMM (FMx), 2008 WL 4447678, at *6 (C.D. Cal. Sept. 30, 2008) (citing *Horton v. Liberty Mut. Ins. Co.*, 367 U.S. 348, 352 (1961)).

⁸⁷ *Folb v. Motion Picture Indus. Pension & Health Plans*, 16 F. Supp. 2d 1164 (C.D. Cal. 1998).

⁸⁸ *Molina v. Lexmark Int’l, Inc.*, No. CV 08-04796 MMM (FMx), 2008 WL 4447678 (C.D. Cal. Sept. 30, 2008).

parties and a settlement conference presided over by the court. What we see is a growing appreciation of mediation, but resistance to the notion of blanket privilege.

(b) Cases

(i) **A Pre-Dispute Mediation Agreement Will
Not be Construed as a Waiver of Tribal
Immunity - *Miller v. Wright*, 699 F.3d 1120 (9th
Cir., Nov. 13, 2012)**

This case looks at “mediation privilege” from the perspective of participation not giving rise to a waiver of important rights, in this case tribal sovereign immunity. The Puyallup Tribe entered into a contract with the State of Washington whereby the Tribe agreed that tribal retailers would purchase only from Washington State Tobacco Wholesalers or state certified wholesalers, and would charge a cigarette tax equal to the amount of the tax that would otherwise be imposed by the state. The agreement provided that “[r]esponsibility for enforcement of the terms of this agreement shall be shared by the State and the Tribe. . . .” The agreement also provided for mediation in the event of a dispute. A retailer and his customers brought suit against the Tribe seeking to invalidate the cigarette tax. The action was filed in the District Court for the Western District of Washington. The District Court dismissed the action for lack of subject matter jurisdiction in light of the Tribe’s sovereign immunity. Plaintiffs appealed. One of the arguments raised on appeal was that the Tribe had implicitly waived its sovereign immunity by agreeing to dispute resolution procedures in its agreement with the State of Washington. While the U.S. Supreme Court has held that agreeing to an arbitration clause might establish a clear waiver of sovereign immunity,⁸⁹ the Ninth Circuit held that the inclusion of a mediation provision did not evidence a clear and explicit waiver of immunity.

“ . . . [M]ediation generally is not binding and does not reflect an intent to submit to adjudication by a non-tribal entity. Moreover, the CTC in this case did not contain any of the provisions, including subjecting itself to the jurisdiction of the state, that formed the basis for the waiver in *C & L*.”

699 F.3d at 1126-1127.

⁸⁹ In *C & L Enters., Inc. v. Citizen Band Potawatomi Indian Tribe of Okla.*, 532 U.S. 411 (2001), the Tribe entered into a roofing contract that contained an arbitration clause. That clause designated Oklahoma law as the law governing contract performance and provided for the Tribe to consent to application of Oklahoma’s Uniform Arbitration Act. The Arbitration Act, in turn, vested jurisdiction in the Oklahoma state courts over any arbitration award.

**(ii) District Court Respects and Enforces
Mediation Confidentiality Provided by Local
Rule - *Jones v. Metropolitan Life Ins. Co.*, 845
F.Supp. 2d 1016 (N.D.Cal., Feb. 24, 2012)**

This case provides a glimpse of how the federal courts enforce mediation confidentiality promised by the Local Rules governing their court-sponsored mediation program. After filing a complaint that initiated these federal court proceedings, the case was assigned to the “Alternative Dispute Resolution Multi-Option Program” sponsored by the District Court for the Northern District of California. The court’s Local Rules require confidentiality in mediation sessions and require counsel to sign a confidentiality agreement form. Such an agreement was signed by counsel in this case. In various court filings, plaintiff’s counsel revealed confidential statements made during the mediation, which prompted defendants to lodge an “ADR Complaint” against plaintiff’s counsel and to file various motions to strike. The Magistrate Judge assigned to the cases found that plaintiff’s counsel had violated the ADR Local Rules by disclosing confidential information from the court-sponsored mediation session and also found that plaintiff’s attorney had violated his professional duty to be aware of and refrain from violating the court’s Local Rules. The court later determined the merits of the case via summary judgment granted in favor of defendants. After appeal to the Ninth Circuit, the judgment was affirmed in part and vacated in part, including the district court’s denial of fees to plaintiff. This case concerned plaintiff’s motion for attorney’s fees, which included a request for fees for the 42.65 hours plaintiff’s counsel spent defending the ADR Complaint and motions to strike. The district court denied this request for fees, finding that the hours plaintiff’s counsel spent litigating a motion filed to redress his knowing and repeated violations of his professional duty “cannot be hours that were ‘reasonably expended.’”

**(iii) Evidence Admissible or Subject to Discovery
or Disclosure Shall not Become Inadmissible
or Protected from Disclosure Solely by
Reason of its Introduction or Use in
Mediation - *Yates v. Delano Retail Partners,
LLC*, 2012 WL 2563850 (N.D.Cal., Jun. 28,
2012)**

Plaintiff sued the property owner/landlord and tenant for damages arising from various alleged violations of the Americans with Disabilities Act concerning access to and enjoyment of a market in San Francisco. Plaintiff filed a motion seeking leave to amend his complaint to add Ralph’s Grocery Store as the alleged holder of the master lease for the grocery store. The landlord opposed the motion on the grounds that

plaintiff learned of the involvement of Ralph's Grocery Store with the property during a conversation had in a mediation convened pursuant to the court's ADR program. The trial court granted leave to amend over the defendant landlord's objection, finding that Ralph's Grocery Store was an interested party as the actual leaseholder of the subject property and that was a required disclosure under FRCP 26(a)(1)(A). That this fact was first disclosed at a mediation session instead of in the form that it should have been disclosed did not create a bar to plaintiff referring to or using the information. *3.

**(iv) Mediation Confidentiality Does not Operate
as a Shield to Discovery of the Underlying,
Pre-Dispute Facts and Pro Se Parties are not
Entitled to Special, Lesser Standards - *Hylton*
v. Anytime Towing, Slip Opinion 2012 WL
3562398 (S.D. Cal., Aug. 17, 2012)**

This case addressed a pro se litigant's refusal to answer fact-based questions on the grounds of relevance and "mediation privilege." The case actually involved an Early Neutral Evaluation proceeding conducted under the District Court's court-annexed ADR program. The pro se plaintiff refused to answer the majority of questions posed to him at deposition questions based on his understanding of the law and the Magistrate's prior orders. On motion by the defendant, the Magistrate found good cause to order a second deposition of the plaintiff and found that sanctions were warranted. The plaintiff objected to the Magistrate's sanction order. The issue for the trial court was whether the Magistrate's order was "clearly erroneous or contrary to law." The court concluded that the Magistrate's decision to impose sanctions was neither clearly erroneous nor contrary to law because neither Rule 30 nor Rule 37 require a finding of "bad faith." Rule 37 requires the imposition of sanctions unless the party whose conduct necessitated the motion to compel was "substantially justified." The court found that an individual's discovery conduct may be deemed "substantially justified" under Rule 37 if "reasonable people could differ as to whether the party requested must comply. In this case, the Magistrate deemed the plaintiff's refusal to answer fact-based questions unjustified and rejected the plaintiff's assertion that he misunderstood the ENE Order's confidentiality and privilege provisions. The court cut the plaintiff no slack, noting that although he was proceeding in pro se, "he is and should be subject to sanctions like any other litigant." There are thus no special rules or different standards for pro se litigants.

**(v) No Settlement Discussion Privilege or
Mediation Privilege is Recognized Under
Federal Law - *In re City of Stockton*, 475 B.R.
720 (Bankr. E.D.Cal., Jul 13, 2012)**

This case discusses the status of mediation privilege as a matter of federal law and the issue of when state privilege law applies in a federal court proceeding. This case involved the municipal bankruptcy filing by the City of Stockton. That filing occurred after the conclusion of the pre-filing neutral evaluation required by the newly enacted California statute as a precondition for permitting a California municipality to file a Chapter 9 petition.

Unlike other bankruptcy proceedings, the filing of a voluntary petition under Chapter 9 does not constitute an order for relief. Rather, when a municipality seeks relief in bankruptcy, it must be prepared to litigate its way to an order for relief by demonstrating its eligibility to be a Chapter 9 debtor and establishing that it filed the petition in good faith. 11 U.S.C. §§ 109(c) and 921(c). The burden of proof as to the eligibility elements is on the municipality. Among the eligibility elements is the “creditor negotiation” requirement, which may be satisfied in one of four ways: (A) the municipality negotiated with its creditors and obtained the agreement of a majority of creditors in each class to the terms of its proposed restructuring plan; (B) the municipality negotiated in good faith with creditors, but failed to reach agreement with a majority of creditors to the terms of a restructuring plan; (C) negotiations did not occur because they were impracticable; or (D) negotiations did not occur because a creditor may attempt to obtain a transfer that is avoidable as a preference. In this case, the City relied on the “good faith negotiation” prong [§109(c)(5)(B)] and requested that the bankruptcy court dispense with the confidentiality protections that attached to the pre-filing neutral evaluation.

The confidentiality provision in question is contained in California Government Code Section 53760.3(q) and requires the parties participating in the neutral evaluation to “maintain the confidentiality” of the process and “not disclose statements made, information disclosed, or documents prepared or produced, during the neutral evaluation process” during any bankruptcy proceeding except upon agreement of all parties or for the limited purpose of determining eligibility under Chapter 9. The question presented to the bankruptcy court was the extent to which the California confidentiality provision applies to the conduct of the City’s Chapter 9 case and, to the extent it does not apply, how to deal with matters warranting confidentiality. On this second issue, the bankruptcy court ruled that the confidentiality provision of Section 53760.3(q) applied to just one of the eligibility questions and that all others were

“creatures of federal law.” As such, Federal rule of Evidence 501 supplanted state privilege law on the issues where federal law provided the rule of decision.

On the issue of privilege, the bankruptcy court stated that “no settlement discussion privilege or mediation privilege is recognized” by federal statute or rule, so the question was “whether there is a common-law privilege that has been judicially recognized ‘in the light of reason and experience.’” 475 B.R. at 731. The court noted that the circuits that have addressed the issue are divided⁹⁰ and that the Ninth Circuit has yet to take a position even though the courts within the Ninth Circuit are divided on the question.⁹¹ In deciding the matter, the bankruptcy court ultimately concluded that “a settlement negotiation privilege is not necessary” because the parties can avail themselves of the court’s inherent authority to preserve confidentiality by seeking a protective order from the court. The bankruptcy court then exercised that authority and issued a protective order forbidding disclosure of statements made, information disclosed, or documents prepared or produced during the pre-filing neutral evaluation process.

**(vi) Post-Mediation Settlement Offers Carried
Between the Parties by a Mediator are not
Protected Under State Mediation
Confidentiality Statute - *Donahoe v. Arpaio*,
872 F.Supp.2d 900 (D.Az. June 1, 2012)**

Plaintiffs’ attorney made an offer of settlement to the defendant County Manager through a mediator who had previously conducted a mediation involving the parties. The mediator communicated that offer to defendant’s counsel via an email that asked said counsel to confirm his client’s agreement to the settlement terms “by replying to this email in the form of an ‘okay’ or something similar.” Defendant’s counsel sent a reply email stating, “We have an agreement.” Defendant later renounced the agreement, and plaintiffs filed a motion to enforce the settlement agreement. The county opposed the motion on the grounds that no one intended a binding agreement from the email exchange. The district court ordered the mediator and the County

⁹⁰ The Sixth Circuit recognizes such a privilege. *Goodyear Tire & Rubber Co. v. Chiles Power Supply, Inc.*, 332 F.3d 976, 979-83 (6th Cir. 2003). The Seventh and Eighth Circuits do not. *In re General Motors Corp. Engine Interchange Litigation*, 594 F.2d 1106, 1124 n.20 (7th Cir. 1979); *In re MSTG, Inc.*, 675 F.3d 1337, 1342 (Fed. Cir. 2012).

⁹¹ See, *Matsushita Elec. Indus. Co. v. Mediatek, Inc.*, 2007 WL 963975 (N.D.Cal. 2007) (no privilege); *Molina v. Lexmark Int’l, Inc.*, 2008 WL 4447678 *10-11 (C.D.Cal. 2008) (same); *California v. Kinder Morgan Energy Partners, L.P.*, 2010 WL 3988448 (privilege recognized); *Folb v. Motion Picture Industry Pension & Health Plans*, 16 F.Supp. 2d 1164, 1180 (C.D.Cal. 1998) (same)

Manager to appear and testify. Only the County Manager (now retired from that post) appeared. He testified that he believed he had authority to settle the plaintiffs' claims, that he authorized the mediator to communicate the settlement offer intending it to be binding and that he thought they had a binding settlement. The County objected to Smith's testimony on the grounds that it was barred by the Arizona mediation privilege statute. The district court rejected that argument, finding that the matters the County Manager had testified to were not communications during a mediation as that process is defined by statute. Because the mediation had been concluded, the district court reasoned that when the mediator stepped back in to carry the settlement offer exchanges, "the parties had passed into conscious and formal contract formation."

"Written offers and acceptances of settlement agreement, on their face expressing intent to be bound, fall outside the mediation privilege, even if the person who was the mediator is a witness to or conduit for them. . . . A mediator cannot by his presence purvey immunity from contract law when the prelude of negotiation has passed and the deal is made."

872 F.Supp. 2d at 911, citing *Folb v. Motion Picture Indus. Pension & Health Plans*, 16 F.Supp. 2d 1164 (C.D.Cal. 1998). See also *United States Fid. & Guar. Co. v. Dick Corp./Barton Malow, et al.*, 215 F.R.D. 503 (W.D.Pa. 2003) ("The mere fact that discussions subsequent to a mediation relate to the same subject as the mediation does not mean that all documents and communications related to that subject are 'to further the mediation process' or prepared for the purpose of, in the course of, or pursuant to a mediation.").

**(vii) FRE 408 and California Evidence Code
Section 1119 Read Together to Bar Settlement
Amount Information From a Mediation to be
Mentioned in Plaintiff's Complaint –
Blodgett v. Allstate Insurance Company, 2012
WL 2377031 (E.D.Cal., Jun. 22, 2012)**

Plaintiff was involved in an automobile accident in which the other driver was at fault and was under-insured. Plaintiff recovered \$15,000 from the other driver's insurance, but claimed that she had suffered damages in excess of \$100,000. Plaintiff maintained a policy that provided up to \$250,000 in benefits for accidents in which that other driver was uninsured or underinsured. Plaintiff made a claim against her policy, which the insurer denied. Plaintiff and her insurer then participated in a mediation. During the mediation, plaintiff offered to settle her claim for \$105,720, to which Allstate responded with an offer of \$7,500. The dispute was then submitted to binding arbitration, during which Allstate disputed plaintiff's entitlement to benefits under her

policy because she had already received the policy limits under the other driver's policy (\$15,000). At the conclusion of the arbitration, plaintiff was awarded the total amount of her claimed damages (\$119,110), less the \$15,000 she had received from the other driver's insurance. Plaintiff then filed this lawsuit seeking damages for insurance bad faith and breach of contract. Included in her complaint was the allegation that plaintiff had offered to settle her claims at mediation for \$105,720, which amount was within \$500 of what she was ultimately awarded at arbitration and significantly greater than the "nuisance value" offer Allstate had made. Allstate filed a motion to strike the allegations containing settlement amount information exchanged during the mediation. That motion was granted in part and denied in part.

The district court ruled that the settlement amount information raised during the parties' pre-lawsuit mediation was barred by Federal Rule of Evidence 408 and California Evidence Code Section 1119 because "it discloses confidential settlement negotiations." Accordingly, the reference in plaintiff's complaint to the specific dollar amounts she alleged offered the insurer to settle her claims were stricken.

The motion to strike was denied, however, with regard to the reference in the complaint to the fact that a mediation was held on a certain date. The district court reasoned that that fact "is not information protected by either Rule 408 or California Evidence Code § 1119."

**(viii) Remedying any Alleged Breach of a
Mediation Confidentiality Agreement
Occurring Outside the Confines of the Legal
Proceedings is Beyond the Reach of the
Court's Inherent Power – *Anselmo v. Mull*,
2012 WL 4863661 (E.D.Cal., Oct. 11, 2012)**

This case involved a land use/development dispute between plaintiffs, on the one hand, and Shasta County and certain officials, on the other. Plaintiffs' claims arise from defendants' alleged wrongful interference with plaintiffs' use of their land. Plaintiffs alleged that county officials engaged in a variety of wrongful conduct that interfered with plaintiffs' use of their property, such as issuing wrongful notices of grading violations, filing false reports with various officials and agencies, requiring an unnecessary environmental impact study, interfering with plaintiffs' development of their winery, and wrongfully denying plaintiffs' application for a Williamson Act contract. The facts are not very clear, but it appears that at some point in time that parties attempted to resolve their disputes through private mediation and that a Mediation Confidentiality Agreement was executed in connection with those proceedings. When the matter was not resolved, plaintiffs disclosed mediation briefs

and mediation statements to third parties, including the press. In response, the County filed a motion seeking an order prohibiting plaintiffs from making such further disclosures and awarding monetary sanctions against plaintiffs for their violation of the Mediation Confidentiality Agreement. That motion was denied.

While the district court agreed that the courts have inherent power to manage their own affairs so as to achieve the orderly and expeditious disposition of cases, to and remedy abuses of the judicial process, and to redress disobedience to the orders of the Judiciary, the plaintiffs' conduct complained of by the County was extra-judicial and had no legal effect on the proceedings before the court. Accordingly, the court concluded that remedying any alleged breach of the parties' mediation agreement occurring outside the confines of the legal proceedings was beyond the reach of the court's inherent power. Moreover, the court stated that even if it could be argued that the court's inherent power extended to the parties' mediation proceedings, "[it] would have no interest or desire to interject itself into those extra-judicial proceedings." In contrast, the court noted that courts have enforced mediation confidentiality agreements when the documents subject to the agreements are submitted to the court or offered at trial. *10, citing *Facebook, Inc. v. Pac. Nw. Software, Inc.*, 640 F.3d 1034, 1041 (9th Cir. 2011).

(3) California Perspective

(a) Background Statement

California has long favored private negotiation and settlement of civil disputes. The state legislature has expressly stated that "[t]he peaceful resolution of disputes in a fair, timely, appropriate, and cost-effective manner is an essential function of the judicial branch of state government."⁹² To effectuate this policy, the state legislature has expressly validated mediation as a process that "provides parties with a simplified and economical procedure for obtaining prompt and equitable resolution of their disputes and a great opportunity to participate directly in resolving those disputes."⁹³ Because mediation provides a simple, quick, and economical means of resolving disputes, and because it may also help reduce the court system's backlog of cases, California has recognized that the public has an interest in protecting not only the mediation participants, but the mediation process itself.⁹⁴

⁹² Cal. C. Civ. Proc. § 1775(a).

⁹³ Cal. C. Civ. Proc. § 1775(c).

⁹⁴ *Rojas v. Superior Court*, 33 Cal. 4th 407, 415 (2004).

The starting point for California's mediation confidentiality scheme is Evidence Code Section 1115 which defines the processes that qualify for confidentiality protection. That protection extends to "mediations" and "mediation consultations." A "mediation consultation" is defined a "a communication between a person and a mediator for the purpose of initiating, considering, or reconvening a mediation or retaining the mediator."⁹⁵ A "mediation" is defined as a process in which "a neutral person or persons facilitate communication between the disputants to assist them in reaching a mutually acceptable agreement."⁹⁶ The comments to Section 1115 make it clear that what qualifies as a mediation is to be determined by "the nature of a proceeding, not its label," and that a proceeding might qualify as a mediation for purposes of the confidentiality protections "even though it is denominated differently." The fact that a court may use the terms "mediation" and "settlement" interchangeably when referring to the process taking place or that a judicial officer might be assigned to preside over the talks will not transform the proceeding into a mandatory settlement conference without a clear record that such a conference was ordered.⁹⁷ This is an important distinction because Evidence Code Section 1117(b)(2) provides that the confidentiality protections afforded communications in mediation do not apply to communications had during a mandatory settlement conference convened pursuant to Rule 3.1380 of the California Rules of Court.

Under California law, confidentiality protection is provided in the form of an evidence exclusion provision. It does not provide for an evidentiary privilege. Evidence Code Section 1119 bars – as evidence in a court or other adjudicatory proceeding – disclosures of (a) anything said or any admission made for the purpose of, in the course of, or pursuant to, a mediation or mediation consultation;⁹⁸ (b) any writing prepared for the purpose of, in the course of, or pursuant to, a mediation or mediation consultation;⁹⁹ and (c) all "communications, negotiations, or settlement discussions" by and between participants in the course of a mediation or mediation consultation.¹⁰⁰ The California Supreme Court has confirmed on several occasions that the "any" and "all" provisions of Section 1119 are to be interpreted quite literally and made it clear that the scope of

⁹⁵ Cal. Evid. C. § 1115(c).

⁹⁶ Cal. Evid. C. § 1115(a).

⁹⁷ *Doe I v. Superior Court*, 132 Cal. App. 4th 1160, 1166-1167 (2005) (the "Archdiocese Case") ("Except where the parties have expressly agreed otherwise, appellate courts should not seize on an occasional reference to 'settlement' as a means to frustrate the mediation confidentiality statutes.")

⁹⁸ Cal. Evid. C. § 1119(a).

⁹⁹ Cal. Evid. C. § 1119(b).

¹⁰⁰ Cal. Evid. C. § 1119(c).

protection intended by the statute is unqualified, clear and absolute,¹⁰¹ and is not subject to judicially crafted exceptions or limitations.¹⁰² The facts of the cases in which the California Supreme Court has been called upon to rule about the scope of protection afforded by Section 1119 have been somewhat extreme and serve to illustrate the breadth of what will be held as confidential if the communications (and sometimes conduct) occurred during a mediation.¹⁰³

Special Rules Related to Mediators

Evidence Code Section 1121 provides that unless the parties agree otherwise, the court may not consider any “report, assessment, evaluation, recommendation or finding of any kind” by the mediator concerning a mediation he/she conducted; that the only report a mediator may make is one that simply states whether an agreement was or was not reached. The comments to Section 1121 explain that the rationale behind this statutory provision is aimed at making sure a mediator will “not be able to influence the result of a mediation or adjudication by reporting or threatening to report to the decision maker on the merits of the dispute or reasons why mediation failed to resolve it.” Companion to Section 1121 is Evidence Code Section 703.5 which declares that a mediator shall be incompetent to testify as to any statement, conduct, decision, or ruling occurring in or in conjunction with a mediation that he/she conducted.

The special rules related to mediators do not apply to other mediation participants. In this regard, the courts have held that the foregoing exclusionary provisions do not prohibit a party from advising the court about conduct during the mediation that might warrant sanctions. In *Foxgate*, plaintiff attached a report by the mediator and a declaration by plaintiff’s counsel reciting statements made during the mediation session, which the Supreme Court found was prohibited by Evidence Code Sections 1119 and 1121.¹⁰⁴ However, the Supreme Court noted that to the extent the declaration of plaintiff’s counsel stated that the mediator had ordered the parties to be present with their experts, there was no violation because “neither Section 1119 nor Section 1121 prohibits a party from revealing or reporting to the court about noncommunicative conduct, including violation of the orders of a mediator or the court

¹⁰¹ See, *Foxgate Homeowners Ass’n v. Bramalea Calif., Inc.*, 26 Cal. 4th 1, 14 (2001); *Rojas*, supra, 33 Cal. 4th at 424; *Fair v. Bakhtiari*, 40 Cal. 4th 189, 197 (2006).

¹⁰² See *Simmons v. Ghaderi*, 44 Cal. 4th 570, 588 (2008); *Cassel v. Superior Court*, 51 Cal. 4th 113, 124 (2011).

¹⁰³ An article discussing those cases will be provided as a handout at the program.

¹⁰⁴ 26 Cal. 4th at 18.

during the mediation.”¹⁰⁵ In 2008, the Court of Appeal for the Third District relied upon *Foxgate* to find that the failure to have all persons or representatives attend court-ordered mediation (as required by Local Rule) was “conduct that a party, but not a mediator, may report to the court as a basis for monetary sanctions.”¹⁰⁶ Similarly, in 2010, the Court of Appeal for the Second District upheld an order imposing sanctions for the unauthorized failure of a party to attend a court-ordered mediation.¹⁰⁷

Special Rules Related to Written Settlement Agreements Reached in Mediation

While the ultimate goal in mediation is for the parties to reach agreement on terms to resolve their dispute, a written settlement agreement or term sheet memorandum prepared with respect to the settlement are writings prepared during the course of mediation and, as such, are entitled to exclusionary protection under Evidence Code Section 1119. Pursuant to Evidence Code Section 1123, such writings shall not be inadmissible or protected from disclosure if any of the following conditions are satisfied:

- (a) the agreement provides that it is admissible or subject to disclosure or words to that effect;¹⁰⁸
- (b) the agreement provides that it is enforceable or binding or words to that effect;¹⁰⁹
- (c) all parties to the agreement expressly agree in writing to its disclosure;¹¹⁰ or
- (d) the agreement is used to show fraud, duress, or illegality that is relevant to an issue in dispute.¹¹¹

¹⁰⁵ *Id.*, n. 14.

¹⁰⁶ *Campagnone v. Enjoyable Pools & Spas Service & Repairs, Inc.*, 163 Cal. App. 4th 566, 572 (2008). The court of appeal went on to note, however, that reporting on anything more than a party’s non-attendance might violate the confidentiality rules. *Id.*

¹⁰⁷ *Ellerbee v. County of Los Angeles*, 187 Cal. App. 4th 1206, 1216-1217 (2010).

¹⁰⁸ Cal. Evid. C. § 1123(a).

¹⁰⁹ Cal. Evid. C. § 1123(b).

¹¹⁰ Cal. Evid. C. § 1123(c).

¹¹¹ Cal. Evid. C. § 1123(d).

In 2006, the California Supreme Court had occasion to construe the application of Evidence Code 1123 and found that the trial court had properly excluded a handwritten term sheet executed at the end of a successful mediation because the agreement did not contain words to the effect that it was intended to be binding and enforceable.¹¹² After the *Fair* decision, parties who draft settlement agreements or term sheets in mediation are encouraged to include an 1123 waiver and “BEEF” provision along the following lines if it is their intention that the document be admissible in any post-mediation proceedings to show the existence of the agreement for enforcement or other purposes:

This Memorandum of Understanding (and any attachments) may be disclosed and is admissible in any action or legal proceeding to show the existence of the agreement and / or to enforce the parties’ agreement as set forth herein in accordance with California Evidence Code Section 1123 and / or applicable Federal Statutes or Rules, and is intended as a binding agreement and shall be final, binding, effective and enforceable against the parties hereto pursuant to California Code of Civil Procedure Section 664.6 or comparable Federal Statutes as of the date set forth below.

Special Rules Related to Oral Settlement Agreements
Reached in Mediation

Evidence Code Section 1123(c) provides that an oral settlement agreement may be admissible if it satisfies the requirements of Evidence Code Section 1118. Pursuant to Evidence Code Section 1118, an oral agreement made “in accordance Section 1118” must satisfy *all* of the following conditions:

- (a) recorded by a court reporter or reliable means of audio recording;¹¹³
- (b) the terms must be recited on the record in the presence of the parties and the mediator, and the parties must express on the record that they agree to the terms so recited;¹¹⁴
- (c) the parties expressly state on the record that the agreement is enforceable or binding,¹¹⁵ and

¹¹² 40 Cal. 4th at 197.

¹¹³ Cal. Evid. C. § 1118(a).

¹¹⁴ Cal. Evid. C. § 1118(b).

¹¹⁵ Cal. Evid. C. § 1118(c).

- (d) the recording is reduced to writing and the writing is signed by the parties within 72 hours after it is recorded.¹¹⁶

The cases discussed in this section of the materials are a continuation of the dialogue being had in the California courts with regard to the contours and scope of the confidentiality protections afforded under California law for communications had and information exchanged during or in connection with a mediation.

(b) Cases

(i) Section 1123 Waiver not Satisfied Where Parties Forgot to Include the “BEEF” Provision - *Huh v. Jeong*, 2012 WL 1513689 (6th Dist., May 1, 2012 – unreported decision)

Plaintiff entered into a contract with the defendants for the construction of a new home. After construction was completed, plaintiff sued to collect the final payments due under the construction contract and defendants cross-complained for damages because the construction of their residence was defective and untimely. The parties went to mediation and, at the end of a full day mediation, agreed upon terms for settlement, which they memorialized in a writing prepared and signed at the mediation. Plaintiff subsequently repudiated the settlement agreement and the defendants brought a motion to enforce the settlement under Code of Civil Procedure Section 664.6. The trial court granted the motion and entered judgment in defendants’ favor, pursuant to the settlement, in the amount of \$166,262. Plaintiff appealed on the grounds that the settlement agreement was unenforceable because it was inadmissible under the Evidence Code provisions governing mediation confidentiality. The Court of Appeal agreed with plaintiff and reversed the judgment.

Citing the California Supreme Court decision in *Fair v. Bakhtiari*, supra, 40 Cal. 4th 189, 199, the Court of Appeal noted that a settlement agreement “drafted during mediation must be admissible before a court can reach the issue of enforceability.” The court then concluded that its resolution of the enforceability issue was governed by the Supreme Court’s decision in *Fair*, which interpreted the language of Evidence Code Section 1123(b), and held that “to satisfy section 1123(b), a settlement agreement must include a statement that is ‘enforceable’ or ‘binding,’ or a declaration in other terms with the same meaning.” Id. at p. 198. In this case, the language of the settlement agreement stated that it was a nonbinding “memorandum of terms for inclusion in a future agreement,” and provided for the parties to sign a more complete mutual release

¹¹⁶ Cal. Evid. C. § 1118(d).

and settlement agreement within 45 days. Additionally, the Court of Appeal noted that the settlement agreement did not include an express statement of the parties' intent that it was "enforceable" or "binding," or a declaration in other terms with the same meaning. Finally, the Court of Appeal rejected the defendants' argument that use of the phrase "full and final settlement of all claims" did not satisfy the section 1123(b) requirements.

**(ii) When a Mediation Ends is Defined by Statute
and Does not Occur When one Party Walks
Out – *Rodriguez v. United Nat'l Ins. Co.*, 2012
WL 541512 (2nd Dist., Feb. 16, 2012 –
unreported decision)**

This case concerned several underlying litigation matters. Plaintiffs filed a class action against their landlord and his related entities complaining about the habitability of a property located in Los Angeles. After the action was filed, the landlord asked his property insurer to add liability coverage for the subject property. At the time the insurer (UNIC) issued the policy endorsement, it was unaware that there was a pre-existing claim against the landlord concerning the property and agreed to defend the landlord subject to a reservation of rights. The landlord then sued UNIC for bad faith based upon its reservation of rights. In the bad faith action, UNIC filed a summary judgment motion seeking a declaration that it had no duty to defend or indemnify the landlord because the landlord's misrepresentation and concealment of the class action avoided the policy endorsement. Before the hearing on that motion, UNIC and its counsel participated in a mediation related to the plaintiffs' class action, as did the landlord, plaintiffs and plaintiffs' counsel. That mediation occurred on September 17, 2009. No settlement was reached at the mediation, but thereafter, over the course of two months, counsel participated in numerous e-mail exchanges concerning negotiated resolution of the class actions and the mediator was a party to or copied on all of those communications. A month later, UNIC's summary judgment motion was granted in the bad faith action and this action followed with a complaint filed by plaintiffs in the class action against UNIC and his counsel for breach of contract, fraud and negligent misrepresentation. Those claims were predicated upon statements UNIC's counsel allegedly made in the course of and subsequent to the mediation regarding UNIC's intention and desire to settle with plaintiffs.

In response to plaintiffs' complaint in this action, defendants filed an anti-SLAPP motion on the grounds that their representation of UNIC in settlement discussions was constitutionally protected activity. Defendants also argued that plaintiffs could not demonstrate a probability that they could prevail because the litigation and mediation privileges precluded liability based on any mediation-related communications or

litigation-related conduct, both of which formed the bases of the allegations in the complaint. In opposition, plaintiffs argued that the anti-SLAPP statute did not apply because a binding settlement agreement was reached post-mediation and their action sought enforcement of that agreement. The evidence of the alleged settlement agreement was contained in the post-mediation email communications. The trial court granted defendants' motion, finding that plaintiffs had failed to demonstrate a probability of prevailing because the communications at issue were protected by the litigation and mediation privileges. The court of appeal affirmed.

With regard to the mediation privilege, plaintiffs argued that the mediation privilege was inapplicable because UNIC's attorney "walked out" of the mediation and the mediation ended at that moment in time. As a result, plaintiffs argued that the e-mail and other communications later had between their attorney and UNIC's attorney may be viewed, collectively, as evidence demonstrating the existence of an enforceable settlement agreement. The court of appeal held that plaintiffs were "mistaken;" that [a]bsent an agreement to the contrary, a mediation does not end until and unless '[f]or 10 calendar days, there is no communication between the mediator and any parties to the mediation relating to the dispute.'" *10, quoting Cal. Evid. Code § 1125(a)(5). The trial court found that there was no 10-day lapse in communication, as such, there was no error in its ruling that the e-mail communications were protected. In this regard, the court of appeal noted that "[a]n e-mail is a writing for purposes of mediation confidentiality." *Id.*, citing *Wimsatt v. Superior Court*, 152 Cal. App. 4th 137, 159 (2007).

**(iii) Asserting the Mediation Privilege Did Not
Deny Defendant a Fair Trial – *Kurtin v. Elieff*,
207 Cal. App. 4th 305 (4th Dist., Jul. 9, 2012)**

Kurtin and Elieff had been equal partners in several ventures for over ten years when growing disagreements led Kurtin to sue Elieff in 2003 to separate their intertwined business interests. That litigation led to a mediation, which in turn led to a settlement agreement signed in 2005. Under the terms of the settlement agreement, Elieff and the "Joint Entities" agreed to buy out Kurtin for \$48.8 million to be paid in four installments of \$21 million, \$1.8 million, \$13.1 million and \$12.9 million. Elieff was personally responsible (with the Joint Entities) for the first installment of \$21 million, and that payment was made. Only the Joint Entities were responsible for the remaining three installments. The second installment was paid, but only \$3.5 of the \$13.1 million third installment as paid, and nothing was paid on the fourth installment. When Kurtin sought to enforce the settlement agreement against the Joint Entities under Code of Civil Procedure Section 664.6, the trial court denied his request based on the judge's determination that the Joint Entities were not parties to the 2003 litigation and thus could not have judgment entered against them. Kurtin then filed a new action in 2007

against Elieff and the Joint Entities asserting various claims, including breach of settlement agreement, fraud and negligent misrepresentation. The trial court made findings after a bench trial regarding distributions allegedly diverted from the Joint Entities to Elieff and then entered judgment against Elieff on a special jury verdict for misstating his authority to bind the Joint Entities in the course of agreeing to buy out his former partner.

A number of terms of the 2005 settlement agreement were relevant to the determination of the issues raised in the 2007 litigation. At trial, Elieff contended that those terms were ambiguous. Elieff sought to introduce evidence of what was said during the 2005 mediation as extrinsic evidence to explain the perceived ambiguities. Kurtin objected to such evidence by asserting the “mediation privilege,” and the court sustained that objection. On appeal, Elieff claimed that he had been deprived of a fair trial; that just as an attorney is allowed to use confidential information that is otherwise protected by the attorney-client privilege when sued by a former client, the mediation privilege must yield when there is an ambiguity in the mediated settlement agreement. The court of appeal rejected that argument – not because of the blanket protection provided by Evidence Code Section 1119 – but because of the terms of the settlement agreement itself. In this case, the settlement agreement provided a mechanism for resolving any conflict between the mediation privilege and any need to consider extrinsic evidence as it might bear on ambiguous terms in the contract: namely, the settlement agreement included an arbitration clause that gave each party the right to go to arbitration in front of the one person most familiar with what had happened at the mediation – the mediator. The court of appeal found that the mechanism set up by the settlement agreement for resolving any ambiguities was one where the parties first would resolve any ambiguities in the contract before the mediator acting as arbitrator before going to court. As such, the court of appeal held that in asserting the mediation privilege in the subsequent lawsuit, Kurtin “was only following the settlement agreement’s own logic, not sandbagging Elieff. Elieff cannot now complain of lack of due process when the settlement agreement itself provided him, at an arbitration, with the same opportunity as Kurtin to present any extrinsic evidence he wanted to introduced as bearing on the meaning of ambiguous contract terms.” 207 Cal. App. 4th at 334-335.

**(iv) No Exception to Mediation Confidentiality to
Test Reasonableness of Post-Trial Attorney
Fee Request – *Fogh v. Los Angeles Film
Schools*, 2012 WL 6604709 (2nd Dist., Dec. 18,
2012)**

Employee sued his former employer for wage and hour violations due to misclassification as an exempt employee. Employee prevailed after a bench trial and was awarded unpaid overtime of \$13,972, plus interest. He was also awarded statutory attorney fees of \$96,800. On appeal, defendant contended that the trial court abused its discretion in determining the fee award because it did not take into consideration the fact that it had made an oral settlement offer that exceeded the amount ultimately awarded by the court. The court of appeal rejected defendant's argument because the settlement offer was made during a mediation and was thus subject to the mediation privilege and inadmissible as evidence. The court noted that in anticipation of the mediation, the parties executed a confidentiality agreement which stated that all negotiations and discussions would be protected from later discovery and/or use in evidence and expressly incorporated Evidence Code Sections 1115 to 1128.

**(v) *Cassel is the Law and Even Fraudulent
Conduct by an Attorney is Protected if it
Occurs During a Mediation – *Hadley v. The
Cochran Firm*, 2012 WL 3140339 (2nd Dist.,
Aug. 3, 2012)***

The Cochran Firm represented plaintiffs in an action for racial discrimination filed against their employer. A mediation was held in July 2008. On the day of the mediation, the firm asked plaintiffs to sign a confidentiality agreement. Plaintiffs claim that they later learned that their signatures to the confidentiality agreement were later appended to a settlement agreement purporting to settle and dismiss their claims against their employer. Plaintiffs claim they did not authorize the settlement and sued the firm for fraud, breach of fiduciary duty and negligence. The trial court granted the firm's motion to dismiss the complaint, concluding that because the alleged deception occurred during a mediation, the mediation confidentiality provisions of the Evidence Code prevented plaintiffs from proving up their claims. On appeal, plaintiffs argued that because they did not intent to settle their claims at the mediation, their action was not "mediation related" and therefore not barred by Evidence Code Section 1119. Plaintiffs also argued that an attorney should not be permitted to commit fraud and avoid liability by hiding behind the mediation privilege. The court of appeal found no merit in plaintiffs' arguments and affirmed. Citing *Cassel v. Superior Court*, 51 Cal. 4th 113, 118 (2011), the court of appeal held that "[t]he mediation confidentiality provisions

are 'clear and absolute. Except in rare circumstances, they must be strictly applied and do not permit judicially crafted exceptions or limitations, even where competing public policies may be affected.'"

B. BINDING MEDIATION

(1) Background Statement

A disagreement becomes a dispute when two or more parties are no longer willing to accept the status quo or to accede to the demand or the denial of a demand by the other. When disputes arise, people have a number of procedural options to choose from to resolve their differences. These options range from informal, private procedures that involve only the disputants to coercion and often public action to force the opposing party into submission. This range of options is frequently referred to as the dispute resolution continuum.

At the collaborative end of the continuum is negotiation, which is a private and voluntary bargaining relationship designed to educate each other about their respective needs and interests, to exchange specific resources and to resolve less tangible issues. A step away from negotiation is mediation, which has been defined as "the intervention in a negotiation . . . of an acceptable third party who has limited or no authoritative decision-making power, who assists the involved parties to voluntarily reach a mutually acceptable settlement of the issues in dispute." Christopher W. Moore, The Mediation Process / Practical Strategies for Resolving Conflict (3d ed. 2003), p. 15.

At the collaborative end of the continuum is litigation, which involves the intervention of an institutionalized and socially recognized authority in a dispute. This approach shifts the resolution process from the private domain to the public and gives full decision-making authority to make a decision that will be binding and enforceable against the parties. A step away from litigation is arbitration, which is a private, adjudicative proceeding in which the parties give full decision-making authority to a third party via contract.

Against the backdrop of the dispute resolution continuum that ranges from processes that enable party self-determination to those that empower a third-party to decide the dispute, there is an incongruity in coupling "mediation" with "binding." Nevertheless, the term "binding mediation" entered our vocabulary in 2006 when the mediator in *Lindsay v. Lewandowski*, 139 Cal. App. 4th 1618 (2006) issued a "binding mediation ruling" that he said was a procedure he regularly used. Honorable Robert

Polist (ret.), the mediator in question, defined the process as one where the parties “agreed in advance that in the event [they failed] to agree, I then decide [the] terms and conditions, typically by asking the parties to each submit . . . their final offers, accompanied by their oral argument as to why I should select their version over all others.” Id. at 1621. The trial court’s confirmation of the binding mediation award as a judgment was reversed by the Fourth District Court of Appeal as unenforceable – not on any procedural grounds (like lack of due process because the mediator’s decision is made without benefit of evidence and is based on confidential information shared with only the mediator), but because the process as expressed by the parties in their agreement was ambiguous. Id. at 1624. In a concurring opinion, two Justices found the term “binding mediation” to be “deceptive and misleading” and the concept to be “oxymoronic” because mediations “are supposed to reflect a truly voluntary process” that, by definition, “reflect[s] the consent of the parties.” Id. at 1625-1628.

In the case discussed below, the Fourth District Court of Appeal affirmed the trial court’s entry of judgment on a “mediator award” and endorsed “binding mediation” as an alternative dispute resolution process. However, there is still much to talk about and explore with regard to this “hybrid” process.

(2) Cases

(a) Judgment on “Mediator Award” Affirmed Because “Binding Mediation” was the Alternative Dispute Resolution Process the Parties Agreed To - *Bowers v. Raymond J. Lucia Companies, Inc.*, 206 Cal. App. 4th 724 (4th Dist., Aug. 29, 2012)

Plaintiffs sued defendants for defamation and related torts. One of the defendants filed an arbitration proceeding against plaintiffs asserting similar claims. That defendant was dismissed from the lawsuit and both sets of proceedings continued on separate tracks. The arbitration hearing was commenced a few months before the scheduled trial date in the litigation matter. After several days of hearing, the parties agreed to settle the dispute by defendant dismissing all claims asserted against plaintiffs in the arbitration proceeding and by plaintiffs submitting their claims in the state court lawsuit to “mediation/binding baseball arbitration.” To wit, the parties agreed to participate in a full day mediation and, if they were unable to reach agreement at the end of the mediation, the mediator was empowered to set the amount of the judgment in favor of plaintiffs and against defendant “at some amount between \$100,000 and \$5,000,000” based on the parties’ respective last and final offer and demand, and that “mediator judgment” could then be entered as a judgment in the state court proceedings without objection of any party. As agreed, the parties

participated in a full-day mediation, but were unable to reach an agreement. Plaintiffs' last and final demand was \$5 million and defendant's last and final offer was \$100,000. Ultimately, the mediator selected the \$5 million number and plaintiffs petitioned to confirm the mediator's award as a judgment. The trial court declined to confirm the award as an arbitration award, but enforced the settlement agreement and mediator award under Code of Civil Procedure Section 664.6. The trial court explained:

"Despite their use of undefined legal terms such as 'mediation with a binding arbitration component' and 'mediation/binding baseball arbitration,' the parties clearly agreed in writing that the mediator would decide the amount of the judgment with the 'binding mediator judgment to then be entered as a legally enforceable judgment"

The Court of Appeal affirmed the judgment entered by the trial court on the "mediator award," and rejected each of the three attacks waged by defendant. With regard to mutual consent, the Court of Appeal found that there was substantial evidence in the transcript of the arbitration agreement and the parties' written settlement agreement showing that the parties agreed to a full-day mediation, at the end of which the mediator could make a binding award if the mediation was not successful. Moreover, the Court of Appeal found that "most supportive of the trial court's finding" was the absence of any indication by the defendant or its counsel that they ever requested the arbitrator to conduct an arbitration after the full-day mediation ended.

With regard to defendant's contention that the settlement agreement was unenforceable because "binding mediation" is an inherently uncertain term, the Court of Appeal disagreed and found that the term was sufficiently certain to be specifically enforceable. Of critical importance to the court was the fact that the parties – both in their agreement and in recorded statements made on the record in the arbitration proceeding – had elaborated on what they meant by the alternative dispute resolution method they had chosen, as well as the fact that defendant never objected or insisted on a post-mediation arbitration hearing until after the mediator made an award in plaintiffs' favor.

With regard to defendant's contention that the settlement agreement was unenforceable because "binding mediation" was not among the constitutionally and statutorily permissible means of waiving jury trial rights, the Court of Appeal disagreed. Although "binding mediation" is not among the methods listed in Code of Civil Procedure Section 631 for waiving a jury trial, the Court of Appeal found that that did not preclude enforcement of the settlement agreement because section 631 relates

only to the manner in which a party to a pending court action can waive his right to a jury trial instead of a court trial. It does not prevent parties from avoiding jury trial by not submitting their controversy to a court of law in the first instance. Therefore, while section 631 applies to the validity of a pre-dispute jury trial waiver in a judicial forum, it does not invalidate a post-dispute jury trial waiver in an agreement to settle in a non-judicial forum.

III. SETTLEMENT – SIGNIFICANT CASES

A. LEGAL STANDARD FOR EVALUATING APPROVAL OF CY PRES DISTRIBUTIONS IN CLASS ACTION SETTLEMENTS

(1) Background Statement

The settlement of a class action is subject to court approval and the standard for approval is “fair, adequate and reasonable.” Fed. R. Civ. Proc. 23(e)(2). The doctrine originated in the area of wills as a way to effectuate the testator’s intent in making charitable gifts, and federal courts now frequently apply it in the settlement of class actions “where the proof of individual claims would be burdensome or distribution of damages costly.” *Six Mexican Workers v. Ariz. Citrus Growers*, 904 F.2d 1301, 1305 (9th Cir. 1990). Used in lieu of direct distribution of damages to silent class members, this alternative allows for “aggregate calculation of damages, the use of summary claim procedures, and distribution of unclaimed funds to indirectly benefit the entire class.” *Id.* at 1305. To ensure that the settlement retains some connection to the plaintiff class and the underlying claims, however, a *cy pres* award must qualify as “the next best distribution” to giving the funds directly to class members. *Id.* at 1308.

In *Six Mexican Workers*, a class of undocumented Mexican farm workers sued various companies for violations of the Farm Labor Contractor Registration Act. After a bench trial, the district court found the defendants liable for over \$1.8 million, which was later reduced to \$850,000 in statutory damages. The district court identified the Inter-American Fund, which provided humanitarian aid in Mexico, as the *cy pres* recipient of any unclaimed funds. The Ninth Circuit reversed, finding that the district court had abused its discretion because there was “no reasonable certainty” that any class member would benefit from it, even though the money would go “to areas where the class members may live.”

The cases discussed in this section of the materials are a continuation of the Ninth Circuit's statement/development of the legal standard to be used in evaluating approval of distributions of *cy pres* awards.

(2) Cases

(a) **Not Just Any Worthy Recipient Can Qualify as an Appropriate *Cy Pres* Beneficiary - *Nascshin v. AOL, LLC*, 663 F.3d 1034, 1038 (9th Cir., Nov. 21, 2011)**

In this case, AOL was accused of violating a number of statutes, including the UCL and the CLRA by wrongfully inserting commercial footers into the plaintiffs' outgoing emails. Because would be small and distribution to the class prohibitively expensive, AOL agreed, as part of a class action settlement, to make substantial donations to three charities: the Legal Aid Foundation of Los Angeles, the Federal Judicial Center Foundation, and the Los Angeles and Santa Monica Chapters of the Boys and Girls Club of America. The Ninth Circuit reversed the district court's approval of the *cy pres* award in the class action settlement, and explained that not just any worthy recipient can qualify as an appropriate *cy pres* beneficiary; that to avoid the "many nascent dangers to the fairness of the distribution process," there must be "a driving nexus between the plaintiff class and the *cy pres* beneficiaries." *Id.* at 1038. The court held that a *cy pres* award must be "guided by (1) the objectives of the underlying statute(s) and (2) the interests of the silent class members." *Id.* The court held that the *cy pres* distribution provided for in the AOL class settlement failed "to target the plaintiff class, because it [did] not account for the broad geographic distribution of the class." *Id.* at 1040. The class included over 66 million AOL users across the country, but two-thirds of the distributions were slated for Los Angeles charities. Further, although the Federal Judicial Center Foundation "at least conceivably benefit[ed] a national organization" it had "no apparently relation to the objectives of the underlying statutes, and it [was] not clear how this organization would benefit the plaintiff class." *Id.* In dicta, the court noted that it should not be difficult for the parties to find an appropriate charity because the class members all had two things in common: (1) they used the internet, and (2) their claims against AOL arose from alleged exploitation from a purportedly unlawful advertising campaign. The court suggested that there were "any number of non-profit organizations that work to protect internet users from fraud, predation, and other forms of online malfeasance."

(b) Proposed *Cy Pres* Beneficiary Description was so Broad that it Might not Serve a Single Person Within the Plaintiff Class - *Dennis v. Kellogg Company*, 697 F.3d 858 (9th Cir., Sept. 4, 2012)

Consumers filed a class action against a breakfast-cereal producer alleging that the producer's marketing claims regarding the effect of cereal on children's attentiveness constituted false advertising in violation of California's Unfair Competition Law ("UCL") and California's Consumer Legal Remedies Act ("CLRA"), and similar laws of other states. The district court approved a settlement that included a provision for *cy pres* distributions to a charity that feeds the indigent. The Ninth Court reversed, finding that while the *cy pres* distribution provision served a "noble goal," it had little or nothing to do with the purposes of the underlying lawsuit or the class of plaintiffs involved. *Id.* at 866. The Ninth Circuit found that the gravamen of the lawsuit was that Kellogg advertised that its cereal improved attentiveness in children and it was those alleged misrepresentations that provided the plaintiffs with a cause of action under the UCL and CLRA and "not the nutritional value of Frosted Mini-Wheats." *Id.* at 867. Accordingly, the court held that appropriate *cy pres* recipients are not charities that feed the needy, by organizations dedicated to protecting consumers from, or redressing injuries caused by, false advertising. "On the face of the settlement's language, 'charities that provide food for the indigent' may not serve a single person within the plaintiff class of purchasers of Frosted Mini-Wheats." *Id.*

The Ninth Circuit also rejected the argument that the settlement provided for the specific charity recipients to be later identified and approved by the court. The court held that "[o]ur standards of review governing pre-certification settlement agreements require that we carefully review the entire settlement, paying special attention to 'terms of the agreement contain[ing] convincing indications that the incentives favoring pursuit of self-interest rather than the class's interests in fact influenced the outcome of the negotiations.'" *Id.*, quoting *Staton v. Boeing Co.*, 327 F.3d 938, 960 (9th Cir. 2003). The court went on to explain that *cy pres* distributions "present a particular danger" if the selection of the *cy pres* beneficiaries is not tethered to the nature of the lawsuit and the interests of the silent class members because the selection process might "answer to the whims and self interests of the parties, their counsel, or the court." *Id.*, quoting *Nachshin*, *supra*, 663 F.3d at 1039.

The Ninth Circuit remanded the case, stating that the parties were “free to negotiate a new settlement or proceed with the litigation. However, if they again decided to settle, “they must correct the additional serious deficiencies we find in this settlement agreement” because it not only failed to identify the *cy pres* recipients of the unclaimed money and food, it was otherwise “unacceptably vague and possibly misleading” as well. *Id.*

**(c) *Cy Pres* Distribution Approved Because the
Proposed Charity was Dedicated to Protecting
Against and Redressing Injuries Caused by the
Same Conduct at Issue in the Class Action Litigation
- *Eddings v. Healthnet, Inc.*, 2013 WL 169895
(C.D.Cal., Jan. 16, 2013)**

Plaintiff filed a complaint against various Health Net entities alleging that defendants had violated the Fair Labor Standards Act (“FLSA”) and various California state labor laws by failing to pay plaintiff and other similarly situated employees for all time worked. The district court conditionally certified a nationwide class under the FLSA based solely on defendants’ timekeeping and rounding policies. The district court also certified a class under plaintiff’s state labor law violation claims. After defendants’ summary judgment motion was granted in part and denied in part, defendants agreed to settle for \$600,000. The proposed settlement provided that any funds remaining after distribution to class members would be distributed in *cy pres* to the Legal Aid Society-Employment Law Center. Citing and relying on both *Dennis v. Kellogg* and *Nachsin v. AOL, LLC* (discussed above), the district court approved the settlement and, specifically, the *cy pres* distribution provisions. As to the latter, the district court found that the proposed charity was “an appropriate charity” because it is dedicated to protecting workers from, or redressing injuries caused by violations of labor laws.

B. 998 OFFERS

(1) Background Statement

The right to recover costs is derived solely from statutes. In the absence of statutory authority, each party must pay his or her own costs. *Davis v. KGO-TV, Inc.*, 17 Cal. 4th 436, 439 (1998). The general statutory rule allowing recovery of costs is found in Code of Civil Procedure Section 1032. *Scott Co. v. Blount, Inc.*, 20 Cal. 4th 1103, 1108 (1999); *Guerrero v. Rodan Termite Control, Inc.*, 163 Cal. App. 4th 1435, 1439 (2008). Section 1032 requires the trial court to award costs to the prevailing party, except as otherwise provided by statute, and Section 1033.5 identifies the costs that are recoverable under Section 1032.

Code of Civil Procedure Section 998 modifies the general rule set forth in Section 1032. *Scott Co., v. Blount, Inc.*, supra, 20 Cal. 4th at 1112. Subdivision (a) of Section 998 states that “costs allowed under Sections 1031 and 1032 shall be withheld or augmented as provided in this section.” Costs are augmented pursuant to Section 998 when an offer to compromise is rejected and the rejecting party fails to achieve a better outcome at trial. In this situation, Section 998 establishes a procedure for shifting the costs upon a party’s refusal to settle and by expanding the type of recoverable costs and fees over and above those permitted by Section 1032. See, *Murillo v. Fleetwood Enterprises, Inc.*, 17 Cal. 4th 985, 1000 (1998); *Westamerica Bank v. MBG Industries, Inc.*, 158 Cal. App. 4th 109, 128 (2007).

In personal injury actions, Section 3291 of the Code of Civil Procedure allows the plaintiff to receive an award of interest at the legal rate of 10 percent per annum if the plaintiff makes CCP § 998 offer that is not accepted by the defendant prior to trial or within 30 days of making, whichever occurs first, and the plaintiff obtains a more favorable judgment.

In order to qualify for cost enhancements under CCP § 998, a “good faith” requirement is read into the statute to effectuate the purpose of the statute, meaning that the settlement offer must be “realistically reasonable under the circumstances of the particular case.” *Adams v. Ford Motor Co.*, 199 Cal. App. 4th 1475, 1483 (2011), citing *Wear v. Calderon*, 121 Cal. App. 3d 818, 821 (1981). “The offer must . . . ‘carry with it some reasonable prospect of acceptance.’” *Id.*, quoting *Elrod v. Oregon Cummins Diesel, Inc.*, 195 Cal. App. 3d 692, 698 (1987). “[A] party having no expectation that his offer will be accepted ‘will not be allowed to benefit from a no-risk offer made for the sole purpose of later recovery large expert witness fees.’” *Id.*, quoting *Jones v. Dumrichob*, 63 Cal.

App. 4th 1258, 1263 (1998). That being said, “[e]ven a modest of ‘token’ offer may be reasonable if an action is completely lacking in merit.” *Nelson v. Anderson*, 72 Cal. App. 4th 111, 134 (1999); see also, *Culbertson v. R. D. Werner Co., Inc.*, 190 Cal. App. 3d 704, 710-711 (1987). Whether a CCP § 998 offer was reasonable and made in good faith is left to the sound discretion of the trial court. *Adams v. Ford Motor Co.*, supra, 199 Cal. App. 4th at 1484. Where the defendant obtains a judgment more favorable than its offer, “the judgment constitutes prima facie evidence showing the offer was reasonable. . . .” *Santantonio v. Westinghouse Broadcasting Co.*, 25 Cal. App. 4th 102, 117 (1994).

(2) Cases

(a) Trial Court Denial of Cost Enhancements After Arbitration - *Maaso v. Signer*, 203 Cal. App. 4th 362 (2nd Dist., Mar. 1, 2012)

As discussed in Section I(F)(2)(a), above, this matter involved a medical malpractice action against a doctor and a medical center that was submitted to arbitration. For reasons not relevant to this discussion, there were two arbitrations. Shortly before the start of the first arbitration, plaintiff gave the defendant doctor a CCP § 998 offer in the amount of \$500,000, which defendant did not accept. Shortly before the second arbitration, the defendant doctor gave plaintiff a CCP § 98 offer that proposed mutual releases, dismissal of the action and a waiver of costs, which plaintiff did not accept. At the conclusion of the second arbitration, plaintiff received an award greater than the CCP § 998 offer he had made to the defendant doctor. While plaintiff put the arbitrators on notice that a CCP § 998 offer had been made, he did not seek to present evidence on the issue, nor did he seek a ruling on costs under that section. When plaintiff petitioned to confirmed the arbitration award, he asked the trial court to award him costs under the offer of judgment rule, which the trial court denied. The trial court reasoned that the language in CCP § 998 allowing either the court or an arbitrator to award cost enhancements simply meant that “what the trial court can do, the arbitrator can also do,” and that the most logical way to read this parallel language was that “in cases tried to the court, the court makes the decisions about awarding CCP § 998 cost connected with the case, while in cases that are arbitrated, those decisions belong to the arbitrator.”

The court of appeal agreed, holding that it only made sense that “the arbitrator decides section 998 costs incurred in arbitration because an award of expert witness costs, and the amount, is discretionary under section 998,” and “it is the arbitrator, not the trial court, which is best situated to determine the amount of reasonable attorney fees and costs to be awarded for the conduct of the arbitration proceeding.” *Id* at 379, citing *DeMarco v. Chaney*, 31 Cal. App. 4th 1809, 1816-1817 (1995). In this regard, the

court of appeal noted that the parties had stipulated that all claims and controversies alleged in the action were being submitted to binding arbitration, including “damages according to proof, costs and all proper relief.” Accordingly, the submission was not limited and included the issue of costs and interest and, where available, attorney fees. *Id.* at 377, citing *Corona v. Amherst Partners*, 107 Cal. App. 4th 701, 706 (2003).

(b) Recovery of Pre-Offer Costs - *Bates v. Presbyterian Intercommunity Hosp., Inc.*, 204 Cal. App. 4th 210 (2nd Dist., Mar. 12, 2012)

Administrator of patient’s estate brought an action against the hospital and others for negligence, wrongful death and elder abuse. Prior to trial, the defendant hospital served plaintiff with a CCP § 998 offer in which it offered to waive costs and to refrain from pursuing a claim for malicious prosecution if plaintiff agreed to dismiss her claims against defendant with prejudice. Plaintiff did not accept the offer and it expired. However, plaintiff later voluntarily dismissed her claims against the hospital with prejudice without having settled with defendant. One month later, the defendant hospital submitted a memorandum of costs seeking \$83,713, including \$64,826 in pre-offer expert witness fees. Plaintiff objected on several grounds. With some slight adjustments, the trial court awarded defendant its costs, including the \$64,826 requested for pre-offer expert witness fees. Plaintiff appealed. The court of appeal affirmed. Citing *Regency Outdoor Advertising, Inc. v. City of Los Angeles*, 39 Cal. 4th 507 (2006), the court held that while the first sentence of Section 998 limits recoverable costs to those incurred after the offer is served, the second sentence relating to expert witness fees contains no such limitation. Therefore, expert witness fees recoverable under Section 998 are not tied to the date the compromise offer is served and, in the discretion of the court or arbitrator may include pre-offer expert witness fees.

(c) Recoverable Costs Explained – Expert Witness Fees and More - *Chaaban v. Wet Seal, Inc.*, 203 Cal. App. 4th 49 (4th Dist., May 9, 2012)

Plaintiff sued his former employer for wrongful termination. Defendant made a CCP § 998 offer to plaintiff (not described in the opinion), which was not accepted. Defendant then obtained a defense verdict after trial and judgment for defendant was entered accordingly. Defendant then filed a memorandum of costs claiming \$29,770, to which plaintiff objected. The trial court allowed all of defendant’s costs, including the deposition costs and fee paid to plaintiff’s expert, even though he was not allowed to testify at trial; the costs incurred to expedite preparation of the deposition transcript for plaintiff’s expert, which was then used to support a motion in limine filed the next day; the costs related to defendant’s expert’s preparation time, travel time and testimony at trial; the costs related to taking the depositions of plaintiff’s co-workers; the costs

incurred depositing plaintiff's treating physician; and the cost of photocopying trial exhibits. The court of appeal affirmed and, in so doing, explained that the foregoing costs are within the purview of CCP § 998 so long as they are reasonably necessary to prepare for trial. An issue of first impression concerned the award of fees defendant paid to plaintiff's expert in connection with his deposition. The court of appeal held that under CCP § 998, the expert witness fees are recoverable without qualification as to the sponsoring side. 203 Cal. App. At 54-55.

**(d) Strict Compliance Required under CCP § 998 -
Perez v. Torres, 206 Cal. App. 4th 418 (5th Dist., May
24, 2012)**

An injured passenger brought suit for personal injury against the driver of the vehicle that hit the vehicle in which passenger was traveling. Prior to trial, defendant made a CCP § 998 offer to plaintiff in the amount of \$100,000, which plaintiff did not accept. The matter proceeded to trial and, while plaintiff prevailed, she recovered less than what defendant had offered. Thereafter, defendant filed his memorandum of costs of almost \$45,000, and plaintiff filed a competing motion to tax costs. The trial court granted plaintiff's motion, concluding that defendant's CCP § 998 was invalid because it did not include "a provision that allows the party to indicate acceptance of the offer by signing a statement that the offer is accepted," as required by subdivision (b) of Section 998. The court of appeal affirm the trial court and held that parties must comply strictly with the requirements of Section 998 in order to enjoy its benefits. 206 Cal. App. 4th at 425-426.

**(e) Unallocated Offer to Married Plaintiffs is Valid -
Farag v. ArvinMeritor, Inc., 205 Cal. App. 4th 372 (2nd
Dist., Apr. 24, 2012)**

Husband and wife sued numerous defendants for personal injury and loss of consortium resulting from exposure to asbestos-containing vehicles and vehicle parts. Prior to trial, one of the defendants (ArvinMeritor) served a CCP § 998 offer on plaintiffs offering to compromise for one cent in exchange for a dismissal with prejudice and a mutual waiver of costs. The offer was made jointly and did not specify that it was capable of acceptance by either plaintiff without the consent of the other. The offer was predicated on defendant's assertion that there was no evidence that the plaintiff husband had been exposed to any ArvinMeritor product. Plaintiffs did not accept the offer and proceeded to trial against ArvinMeritor and the other defendants. The jury returned a verdict in favor of ArvinMeritor, and ArvinMeritor then submitted a memorandum of costs. The trial court entered judgment on the jury verdict and awarded expert witness fees and travel costs under the cost-shifting provisions of Section 998. Plaintiffs appealed. The court of appeal affirmed after a lengthy discussion

of what it term “pertinent case law” with respect to the validity of joint offers made to co-plaintiffs where the co-plaintiffs are husband and wife.

The court of appeal noted that the general rule is that joint CCP § 998 offers to co-plaintiffs are invalid; that only an offer made to a single plaintiff, without requiring co-plaintiffs to agree on allocation or acceptance, qualifies as a valid offer under Section 998. 205 Cal. App. 4th at 376-377, citing *Meissner v. Paulson*, 212 Cal. App. 3d 785, 791 (1989). As noted by the court in *Meissner*, a joint offer places a plaintiff who wishes to settle at the mercy of one who does not and frustrates the goal of encouraging settlement. Moreover, if two or more plaintiffs obtain a money judgment, it may be impossible for the trial court to determine whether any particular plaintiff received a judgment less favorable than the defendant’s joint settlement offer if not allocated between/among plaintiffs.

In the case of a husband and wife, however, none of these concerns apply when the claims of either spouse that arise during the marriage constitute community property and either spouse has the authority to compromise such claims under California Family Code Section 1100. In a typical multi-plaintiff case, an unallocated joint offer may make it impossible for the trial court to determine whether the defendant obtained a more favorable result against any particular plaintiff, and puts the plaintiff who wishes to settle at the mercy of the other plaintiffs. In the case of spouses, neither of these concerns arise because the entire judgment is community property, and either spouse can settle the claim without the other spouse’s consent. As such, the court of appeal in this case held that the defendant’s non-apportioned CCP § 998 offer was valid and affirmed the trial court’s award of expert witness costs to defendant under Section 998.

(f) **Recovery of Attorney’s Fees and Costs After
Settlement – *Wohlgemuth v. Caterpillar, Inc.*, 207
Cal. App. 4th 1252 (5th Dist., Jul. 23, 2012)**

In 2002, plaintiffs purchased a new 2003 motor home. Six years later, plaintiffs filed suit against the engine manufacturer under the Song-Beverly Consumer Warranty Act alleging that the engine was defective. Plaintiffs sought a refund of the purchase price or a replacement motor home. Shortly before trial was set to start in 2010, defendant served plaintiffs with a “998 Offer” in which defendant offered to pay plaintiffs the sum of \$50,000 in exchange for the dismissal with prejudice of the entire action and a general release of all claims. Plaintiffs accepted the offer and filed a notice informing the court that a settlement had been reached whereby a dismissal of the case was imminent. Two weeks after filing the request for dismissal (and presumably receipt of the \$50,000 settlement amount), plaintiffs filed a motion for attorney’s fees and costs under the provisions of the Song-Beverly Act. Plaintiffs argued that in light of

the practical result achieved by the settlement, they were the “prevailing” parties in the action. Plaintiffs stressed that where an accepted offer of compromise under Code of Civil Procedure section 998 is silent on the issue of attorney’s fees and costs (as was the case here), the prevailing party is entitled to recover same if authorized by contract or statute. The trial court found plaintiffs to be the prevailing parties and awarded them \$117,625 in attorney’s fees and \$7,737 in costs. Defendant appealed.

On appeal, the court was asked to determine whether the plaintiffs qualified as prevailing parties for purposes of recovering statutory attorney’s fees. The court of appeal held that under the circumstances, both parties met the definition of a prevailing party under Code of Civil Procedure section 1032 – the defendant because a dismissal was entered in its favor, and the plaintiffs because they were the parties with a net monetary recovery. As such, the court of appeal held that the trial court had discretion to determine that plaintiffs were the prevailing parties and upheld the award of attorney’s fees and costs to plaintiffs.

**(g) Offers not Made Pursuant to CCP § 998
Cannot be Considered in Reducing a Fee
Award – *Fogh v. Los Angeles Film Schools*,
2012 WL 6604709 (2nd Dist., Dec. 18, 2012)**

Employee sued his former employer for wage and hour violations due to misclassification as an exempt employee. Employee prevailed after a bench trial and was awarded unpaid overtime of \$13,972, plus interest. He was also awarded statutory attorney fees of \$96,800. On appeal, defendant contended that the trial court abused its discretion in determining the fee award because it did not take into consideration the fact that it had made an oral settlement offer that exceeded the amount ultimately awarded by the court. The court of appeal rejected defendant’s argument because the settlement offer was made during a mediation and was thus subject to the mediation privilege and inadmissible as evidence. It further held that even if the offer were admissible, the trial court reasonably ignored it in determining the reasonableness of the fee award in light of the circumstances surrounding the offer: the offer was made on a “take-it-or-leave-it” basis with a short deadline for acceptance; it was never reduced to writing; and defendant refused to provide any documentation supporting the amount of the offer in response to plaintiff’s requests. Under these circumstances, the court of appeal held that the offer was not made in good faith because plaintiff lacked sufficient information and time to consider the offer’s merit.

C. MISCELLANEOUS

(1) Supreme Court Repudiates Common Law Release Rule – *Leung v. Verdugo Hills Hospital*, 55 Cal. 4th 291 (Aug. 23, 2012)

This case concerned a medical malpractice case in which the plaintiff suffered irreversible brain damage six days after his birth. Through his mother as guardian ad litem, plaintiff sued his pediatrician and the hospital in which he was born. Before trial, plaintiff and the pediatrician agreed to a settlement of \$1 million – the limit of the doctor’s malpractice insurance policy. The case proceeded to jury trial against the hospital, after which the plaintiff was awarded both economic and noneconomic damages of almost \$100 million (present value approximately \$17 million) and apportioned negligence between the doctor and hospital at 55 percent and 40 percent, respectively (and 2.5 percent to the parents). The trial court found the settlement not to be in good faith and entered a judgment on the jury verdict against the hospital holding it jointly and severally liable for 95% of all economic damages, less the setoff of \$1 million representing the amount of settlement with the doctor. Defendant hospital appealed.

On appeal, the court of appeal agreed with the hospital that under the common law release rule, plaintiff’s settlement with (and release of liability claims against the doctor) also released the nonsettling hospital from liability for plaintiff’s economic damages. Under the common law release rule, a plaintiff’s settlement with, and release of liability of, one joint tortfeasor also releases from liability all other joint tortfeasors.¹¹⁷ On further appeal to the California Supreme Court, the Court reversed and held that the common law release rule is no longer to be followed in California. 55 Cal. 4th at 302. The Court explained that the rationale behind the common law release rule assumes that the amount paid in settlement to a plaintiff in return for releasing one joint tortfeasor from liability always provides full compensation for all of the plaintiff’s injuries, and that therefore anything recovered by the plaintiff beyond that amount necessarily constitutes a double or excess recovery. The Court found that that assumption is unjustified for a variety of reasons, including a settling defendant’s limited resources or relatively minor role in causing the plaintiff’s injury. reversed

¹¹⁷ Under the common law rule’s rational, there can be only one compensation for a single injury and because each joint tortfeasor is liable for all of the damage, any joint tortfeasor’s payment of compensation in any amount satisfies the plaintiffs entire claim. See, 5 Witkin, Summary of California Law (10th ed. 2005) *Torts*, § 70, pp. 142-143; see also *Tech-Built, Inc. v. Woodward-Clyde & Associates*, 38 Cal. 3d 488, 499 (1985).

(2) Settle with Your Adversary and Sue Your Attorney for Settlement Malpractice – *Filbin v. Fitzgerald*, 211 Cal. App. 4th 154 (1st Dist., Nov. 12, 2012)

Settle and sue cases are generally disfavored, because the “problem with allowing the proposed post-settlement litigation is that it would deprive the settling parties of a major advantage of settlement. Establishing the insured's actual liability after settlement would involve litigation of the very issue that the insured and the insurer attempted to avoid litigating. Whether the claimant wins or loses on the liability issue, he has succeeded in forcing the insurer and insured to litigate the claim they had previously concluded by settling. Allowing such a post-settlement trial on the insured's liability would diminish any advantage to be gained by either the insured or the insurer in settling the underlying claim. Indeed, it would *penalize* the insurer for choosing to settle a claim rather than pursuing it to a final judgment, by subjecting the insurer to subsequent litigation on the liability issue it has already settled.” *Moradi-Shalal v. Fireman’s Fund Ins. Companies*, 46 Cal.3d 287, 312 (1988); but see *Earth Elements, Inc. v. National American Ins. Co.*, 41 Cal. App. 4th 110 (1995) [remedy against insurer available where damages directly result from breach of duty to indemnify]. Thus, courts have not granted post-settlement remedies, for example, in attorney malpractice actions where there is no causal connection between the attorney's negligent acts and omissions and the amount the clients received when they settled. *Barnard v. Langer*, 109 Cal. App. 4th 1453 (2003).

In this case, husband and wife plaintiffs sued their former attorney for legal malpractice, contending that the attorneys’ alleged negligence caused them to receive a settlement in an underlying eminent domain case that was less favorable than it would have been absent the attorneys’ negligence. Specifically, plaintiffs claimed that their attorney made various errors in representing them and, after replacing the attorney with new counsel, were forced to accept an unfavorable settlement. Following a bench trial, the trial court entered judgment in plaintiffs’ favor on the malpractice claim. The First District Court of Appeal reversed. The court explained that in a “settle and sue” malpractice action, the plaintiff must prove that *but for* the malpractice she would *certainly* have received more money. Simply showing that the attorney erred is not enough. The court of appeal noted that the requirement that a malpractice plaintiff prove damages to a “legal certainty” is difficult to meet in “settle and sue” cases because claims of inadequate settlement are often inherently speculative since settlement involves a wide spectrum of considerations and broad discretion. Importantly, the court of appeal did not flatly prohibit liability against former counsel for less favorable settlement, and simply concluded that based upon the facts before it, plaintiffs had failed to prove causation or damages as a matter of law.

IV. SIGNIFICANT STATUTES & RULE CHANGES

A. CALIFORNIA

(1) **Exception to Mediation Confidentiality for Attorney Misconduct/Malpractice During Mediation – AB 2025 (Gorell) (2011-12 Reg Session)**

AB 2025 (Gorell) proposed to require the California Law Revision Commission to study and report to the Legislature regarding mediation confidentiality. Specifically, this bill provided that the California Law Revision Commission (Commission) shall study and report to the Legislature regarding the relationship under current law between mediation confidentiality and attorney malpractice and other misconduct, and the purposes for and impact of those laws on public protection, professional ethics, attorney discipline, client rights, the willingness of parties to participate in voluntary and mandatory mediation and the effectiveness of mediation, as well as other issues the Commission deems relevant. The measure passed the Assembly Judiciary Committee 10-7, the Assembly Appropriations Committee 17-0, and the Assembly 76-1. The bill moved to the Senate Rules Committee for assignment, where no further action was taken. See final amendment at http://www.leginfo.ca.gov/pub/11-12/bill/asm/ab_2001-2050/ab_2025_bill_20120510_amended_asm_v98.pdf.

(2) **Mandatory Mediation Before the Filing of any FEHA Claim – SB 1038 (Committee on Budget and Fiscal Review), Statutes of 2012, Chapter 46, §§ 18, 27-66, 68, 70, 101 &115) State Government**

This budget trailer bill provides the necessary statutory references to enact the 2012-13 Budget related to the consolidation, reorganization and restructuring of state entities. The portion of the bill that reorganized civil rights enforcement under the Fair Employment and Housing Act (FEHA) (Cal. Gov't Code § 12900 *et seq.*):

- Eliminated the Fair Employment and Housing Commission effective January 1, 2013. (Legis. Counsel's Dig., Sen. Bill 1038 (46 Stat. 2012) (Reg. Sess.) Summary Dig. p. 3.)

- Transferred the Commission's regulatory function to the Department of Fair Employment and Housing (DFEH) within a new Fair Employment and Housing Council.
- Ended administrative adjudication of FEHA claims.
- Authorized the Department of Fair Employment and Housing to file cases directly in court.
- Required all parties to participate in mandatory dispute resolution in the DFEH's internal Dispute Resolution Division, free of charge, before the DFEH files a civil action.
- Authorized the DFEH to collect attorney fees and costs when it is the prevailing party in FEHA litigation.

The bill was signed into law by the Governor and made effective on June 27, 2012, and became operative on January 1, 2013.

(3) Elimination of Court-Annexed ADR Programs and What that Means to Civil Litigants

As anyone who works in the state court system knows, the state courts have been severely impacted by the state budget crisis. The Los Angeles Superior Court has been especially hard hit. On November 27, 2012, the Los Angeles Superior Court posted a tersely worded announcement describing the drastic and immediate cutbacks being forced upon the largest court system in the world. According to the post, the court's administrators have been told to permanently cut the court's budget by \$55 million to \$86 million by June 2013. These cuts are in addition to the \$100 million in budgetary cuts made over the past two years. Included within the cuts are the Temporary Judge and court-run ADR programs. These programs will be discontinued, and the only settlement assistance that will be available through the court will be settlement conferences presided over by judges who have been reassigned from the civil panel to act as settlement (versus trial) judges. The November 27th announcement encouraged counsel to significantly reduce their law and motion activity and "to pursue ADR outside the Courts." Some have predicted that we will soon return to a five-year wait for trial in civil matters. However, others, are of the view that the elimination of the court ADR programs will not produce catastrophic backlogs because Southern California has a mature mediation market that is both familiar with ADR and the providers of ADR services.

(4) Legal Representation in Arbitration - Code of Civil Procedure
§ 1282.4

Under existing law, until January 1, 2013, out of state attorneys were permitted to represent a party in an arbitration proceeding in the State of California and to render legal services within the state in connection with an arbitration proceeding pending in another state, provided that such attorneys served upon the arbitrator, the parties, the parties' counsel and the State Bar of California a certificate containing specified information. As amended on July 9, 2012, the January 1, 2013 repeal date was deleted, thereby making the provisions for out-of-state attorney representation in arbitration operate indefinitely.

(5) Settlement Agreements – Department of Consumer Affairs
Licensees – Business & Professions Code § 143.5

This statute was added in 2012 and prohibits licensees regulated by the Department of Consumer Affairs from including in a civil dispute settlement agreement any type of provision that prohibits the other part in the dispute from contacting, filing a complaint, or cooperating with the DCA. It also prohibits the inclusion of any type of provision in a settlement agreement requiring the other party to withdraw a complaint made to the DCA or its various boards, bureaus or programs. A licensee who acts in violation of these provisions is subject to disciplinary action.

(6) Municipal Bankruptcy Filings – Pre-Filing Requirements that the
Government Entity Participate in an Early Neutral Evaluation –
Government Code §§ 53760, et seq.

Under Bankruptcy Code § 109(c), a state municipality is eligible to be a debtor in bankruptcy, but only if it is specifically authorized by State law to file for bankruptcy relief. Under existing law, Government Code § 53760 allowed any taxing agency of instrumentality of the state to file a petition in bankruptcy. Because of the reduction in services and fiscal impact on the state and surrounding municipalities when a municipality files for bankruptcy, Section 53760 was amended in October 2011 (effective January 1, 2012) to require that a municipality participate in a neutral evaluation process before filing. Section 53760.3 was then added to the Government Code to define the neutral evaluation process, the object of which is to achieve a negotiated resolution that avoids a bankruptcy filing altogether or results in agreement on a preagreed plan of adjustment in connection with a Chapter 9 filing. Subsection (q) provides for confidentiality and states that the parties who participate in the process

must maintain the confidentiality of the neutral evaluation process and must not disclose statements made, information disclosed, or documents prepared or produced unless everyone expressly agrees in writing to disclosure or the information is deemed necessary by the bankruptcy judge presiding over the bankruptcy proceeding.

(7) **Conditional Settlements – Effect on Pending Hearings – California Rule of Court, Rule 3.1385**

By amendment in 2012, which becomes effective July 1, 2013, subdivision (c) was rewritten and now requires that upon the filing of a notice of conditional settlement, the court must vacate all hearings and other proceedings requiring the appearance of a party, with the express exception of those proceedings relating to sanctions or the determination of a good faith settlement under Code of Civil Procedure § 877.6. The revised statute further provides that no other hearings may be set earlier than 45 days after the dismissal date specified in the notice of conditional settlement, and that the filing of a notice of conditional settlement stops the computation of time used to determine case disposition time.

B. FEDERAL

(1) **General Order No. 11-10 of the United States District Court for the Central District of California – Incorporating “Mediation” Into Accepted ADR Procedures and Renaming “Attorney Settlement Officers” as “Mediators”**

On August 15, 2011, the U.S. District Court for the Central District of California completed an overhaul of its court-annexed ADR program with the entry of General Order No. 11-10. Before this new order, the court-annexed ADR Program referred to ADR as “settlement proceedings” and to its panel members as “attorney settlement officers” similar to the programs in state court where attorneys appointed as “temporary judges” preside over mandatory settlement conferences. Now the process involving attorney volunteers is called “mediation” and panel members are called “mediators.”

The new general order also made progress in providing for a defining confidentiality protection available to participants in mediations conducted under the auspices of the court’s ADR Program, which in turn prompted the 2012 revisions to Local Rule 16-15 and the forms used in court-annexed mediations.

(2) **Local Rule 16-15.4 of the United States District Court for the Central District of California – Mediation as a Recognized/Accepted ADR Procedure**

In 2012, the U.S. District Court for the Central District of California revised Local Rule 16-15.4 to set forth three suggested “ADR Procedures,” as compared to prior “Settlement Proceeding” options for civil litigants to choose from. Under the revised rule, parties may elect to appear before a neutral selected from the court’s “Mediation Panel,” as compared to the prior option of appearing before an “Attorney Settlement Officer.”

(3) **Local Rule 16-15.8 of the United States District Court for the Central District of California – Mediation Confidentiality Protection**

In 2012, the U.S. District Court for the Central District of California revised Local Rule 16-15.8 to provide for “confidential treatment” by the court, the mediator, counsel, parties, and any other persons attending the mediation for “confidential information.” Under the revised rule, “confidential information” is defined as including the mediation briefs, any documents prepared “for the purpose of, in the course of, or pursuant to” the mediation, anything said or done in the mediation relating to the subject matter of the case, any position taken and any view of the merits of the case expressed by any participant in connection with the mediation. According to the new rule, anything qualifying as “confidential information” shall not be disclosed by the participants to anyone not involved in the litigation or the assigned judges, and shall not be used for any purpose in any pending or future proceeding in the court or any other forum.

Given the Ninth Circuit decision in *Facebook*, which refused to respect the confidentiality protections created by a similarly worded Local Rule adopted by the U.S. District Court for the Northern District of California, the enforceability of the protection provided by the new rule is uncertain.

C. OTHER

(1) Status of Adoption of the Uniform Mediation Act or Similar Statutory Schemes re Mediation Confidentiality Protections

The Uniform Mediation Act (“UMA”), constructed by drafting committees from the National Conference of Commissioners on Uniform State Laws and the American Bar Association’s Section of Dispute Resolution, as well as legal academics, is an attempt to bring uniformity to mediation across the country. See, www.nccusl.org. A primary purpose of the UMA is to provide “a privilege that assures confidentiality in legal proceedings.”

Currently, eight states have enacted the UMA: Nebraska, Illinois, New Jersey, Ohio, Iowa, Washington, Indiana, and the District of Columbia – all within the last 10 years.

Although they did not adopt the UMA, several other states have adopted statutes very similar to the UMA: Delaware, Florida, Montana, Nevada, Oregon, and Wyoming. It is worth looking at Florida’s altered version of the UMA because it is one of the states that certifies mediators and regulates the practice of mediation. Florida’s mediation statute provides for confidentiality and allows for many of the same UMA exceptions. However, the Florida statute provides that those who “knowingly and willfully” disclose mediation communications will be liable for damages. The remedies provided by the statute include equitable relief, compensatory damages, attorney’s fees, mediator’s fees, and costs incurred in the mediation. See, http://www.flcourts.org/gen_public/adr/chapter44.shtml.

Why does it matter what other states are doing re statutes governing mediation?
Answer: Because litigation and thus mediation frequently crosses state lines and it is not always clear what law governs the mediation and, in particular, mediation confidentiality.

V.

PANEL BIOS



Rebecca Callahan is a 30-year, AV-rated attorney who acts as a mediator, arbitrator and ADR consultant. Rebecca earned a post-graduate degree in dispute resolution (LLM in Dispute Resolution) from the Straus Institute where she is an adjunct professor. She has been in the ADR trenches for 15+ years and knows how to put theory into practice. Her experience covers a broad spectrum – including real property, employment, wills and trusts, elder abuse and general business – and is dedicated to helping parties resolve their disputes in a way that is efficient, economical and effective. No matter what dispute resolution process is used, Rebecca’s goal is the same: help parties achieve a durable resolution. Rebecca received her JD from the University of California at Berkeley and her undergraduate degree from the University of Southern California.



Phyllis Cheng is Director of the California Department of Fair Employment and Housing (DFEH). Appointed in January 2008 and unanimously confirmed by the Senate, she heads the largest state civil rights agency in the nation. The DFEH takes in, investigates, conciliates, mediates and prosecutes discrimination complaints against employers, housing providers and businesses throughout California. The Department enforces the Fair Employment and Housing Act (FEHA), Unruh Civil Rights Act, Disabled Persons Act and Ralph Civil Rights Act. Under her direction, Ms. Cheng has transformed the Department into a proactive and innovative agency, including the creation of an attorney-staffed dispute resolution division to encourage out-of-court settlements. Ms. Cheng received her B.A. and M.Ed. from UCLA, her Ph.D. from USC, where she was a James Irvine Fellow, and her J.D. from Southwestern Law School. She is an immigrant from Hong Kong and a native speaker of Chinese in three dialects.



Rex S. Heinke is co-head of the Supreme Court and Appellate practice at Akin Gump Strauss Hauer & Feld LLP. He has argued over a hundred appeals in federal and state courts throughout the country. Several of his current appeals involve the enforceability of arbitration clauses. Mr. Heinke also has served as lead trial and appellate counsel on behalf of the media in First Amendment, intellectual property, entertainment, and Internet disputes. He has lectured on media, entertainment, Internet, intellectual property, advertising, constitutional, and appellate law for programs presented by many professional and educational organizations. He has also written numerous articles on these issues and is the author of *Media Law* (BNA). Mr. Heinke is a former president of numerous organizations including the Los Angeles County Bar Association and Public Counsel. He is a member of the American and California Academies of Appellate Law.



Jeff Kichaven is an independent mediator with a nationwide practice, based in Southern California. He is an Honors Graduate of Harvard Law School and a Phi Beta Kappa graduate of the University of California, Berkeley. He has been named California Lawyer Attorney of the Year in ADR and has appeared on the Daily Journal's list of California's Top Neutrals seven times. He has also taught the Master Class for Mediators for Harvard Law. He is a Member of the American Law Institute and his views on mediation have been cited in The New York Times and The Wall Street Journal.



Michelle Reinglass is a full-time mediator and arbitrator with Judicate West, following a 30-year litigation career handling all areas of employment law, including discrimination, harassment, retaliation, termination, wage-and-hour, business and injury cases. She is also on AAA's employment panel. She is AV-rated by Martindale-Hubbell, a member of ABOTA, a Fellow in the College of Labor and Employment Lawyers, past chair of the California Employment Lawyers Association, past president of the Orange County Bar Association, and a frequent author and speaker on employment law, litigation, and ADR. *The Los Angeles Daily Journal* named her as one of California's Top 50 Neutrals, a Top Female Litigator and a Top Labor and Employment Lawyer. She has received OCTLA's Top Gun Award for Employment and Business Litigation, been inducted into WSU College of Law's Hall of Fame, included in *The Best Lawyers in America*, and has been recognized by *Southern California Super Lawyers* in its Top 50 Women, Top 50 Orange County, and Top 100 Southern California categories.



Deborah Rothman, a *magna cum laude* graduate of Yale College, holds a J.D. from NYU Law School and a Masters in Public Affairs from the Woodrow Wilson School at Princeton University. She is on the Large Complex, International, Employment and Commercial panels of AAA, and the rosters of CPR and Judicate West. A full-time mediator and arbitrator since 1992, she has been named a Southern California Super Lawyer ('2006-'13) and a Best Lawyer in America ('2006-'13). In 2012 Best Lawyers named her best Los Angeles arbitrator, in 2007 the Hollywood Reporter named her one of 32 Power Mediators nationally, and in 2009 she was named one of the top arbitrators in California by Who's Who Legal. She is V.P. of the College of Commercial Arbitrators, co-editor of the CCA's "Protocols for Expedient, Cost-Effective Commercial Arbitration," and a contributor to the College's *Guide to Commercial Arbitration*, available through Juris Publishing. Her website is www.DeborahRothman.com.



Honorable Gary Taylor is a retired judge of the U.S. District Court for the Central District of California. He was appointed to the federal bench in 1990 after four years of service as a judge of the Orange County Superior Court. Prior to his appointment to the bench, Judge Taylor spent 20 years as a business litigator with Wenke, Taylor, Evans & Ikola. Judge Taylor is currently serving on the arbitration and mediation panel at JAMS, where he has acted as a neutral in a broad range of disputes. Judge Taylor has received many honors and accolades, including the OCBA Franklin G. West Award in 1998 for lifetime achievement and the UCLA Alumni of the Year Award in 1999 for public and community service. Judge Taylor received both his undergraduate and law degrees from UCLA.

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