

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,” meaning that such circumstance might affect impartiality or create an appearance of partiality. 9 U.S.C. § 10(a)(2). 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.*, 393 U.S. 145 (1968).

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. *Id.* at 152-153. 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.

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;” that “evident partiality” is distinct from actual bias. *Id.* at 147. 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. *Id.* at 149. 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.” *Id.* at 146. 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.” *Id.* at 148-149.

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

In contrast, in *Schmitz v. Zilveti*, 20 F.3d 1043 (9th Cir. 1994), 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. *Id.* at 1044. 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. *Id.* Based on *Commonwealth Coatings*, the court concluded that the standard for evident partiality is whether there are “facts showing a ‘reasonable impression of partiality.’” *Id.* at 1048. 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.”*Id.*

In further contrast, in the Ninth Circuit’s recent decision in *Lagstein v. Certain Underwriters at Lloyds, London*, 607 F.3d 634 (9th Cir. 2010), cert. den., __ U.S. __, 131 S.Ct. 832 (2010), 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 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.” *Id.* at 645. 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.’” *Id.* at 645-646, citing *Woods v. Saturn Distribution Corp.*, supra, 78 F.3d at 427. 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.’” *Id.* at 646, citing *Commonwealth Coatings*, supra, 393 U.S. at 150. 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. *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 the arbitrators had any financial or personal interest in the outcome of the arbitration"). [Note: After remand, there was a further appeal and reported decision concerning the ability of the court to award interest where the arbitration award was silent.]

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.*, 501 F.3d 1101 (9th Cir. 2007). 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 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. *Id.* at 1110-1111.

The federal cases discussed in Section 4, 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. See, *Ventress v. Japan Airlines*, 603 F.3d 676, 679-680 (9th Cir. 2010).

(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 section 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, 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 section 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.

A proposed neutral must timely disclose to the parties “all matters that could cause a person aware of the facts to reasonably entertain a doubt that the proposed neutral arbitrator would be able to be impartial,” including a long list of specific information set forth in Standard 7(d) of the Ethics Rules. Code. Civ. Proc. § 1281.9(a). The disclosures must be made in writing within 10 calendar days of the proposed nomination or appointment. Code. Civ. Proc. § 1281.9(b). 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.¹ 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). Under Code of Civil Procedure section 1281.91(b), disqualification is mandatory; operates as a peremptory challenge; and takes effect when a party timely serves a notice of disqualification.

¹ 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 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).

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

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. In this regard, the Supreme Court cautioned against construing the governing standard too broadly. "A impression of possible bias in the arbitration context means that one could reasonably form a belief that an arbitrator was biased *for or against a party for a particular reason*." Id. at 389 (italics in original). One Court of Appeal (Fourth District) 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. As evidenced by the recent decision of the Second District in *Mt. Holyoke Homes, L.P. v. Jeffer Mangels Butler & Mitchell*, 219 Cal. App. 4th 1299 (2013), the issue of what type of relationships require disclosure on penalty of vacatur just got a little bit broader.

(3) **Conclusion**

Whether operating under Federal or California state law, it is a universal principle 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 5, below, are recent decisions that continue the discussion/dissection of what is a required disclosure 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.

(4) **Cases - Federal**

- (a) **Court Upbraids a Former Appellate Justice for Rendering an Arbitration Award “in Retaliation” and Vacates the Award Due to Evident Partiality in the Way he Decided and Handled the Disqualification Challenge – *Ruhe v. Masimo Corp.*, Case No. 8:11-cv-734-CJC (C.D.Cal., Apr. 3, 2014) (Appeal Taken to the Ninth Circuit)**

This is an employment case in which the plaintiffs complained of wrongful termination from defendant Masimo. In September 2011, the Court ordered the parties to arbitration. That matter proceeded to arbitration and to evidentiary hearing before a JAMS arbitrator, Richard C. Neal (a former Court of Appeal Justice). Thirty-six hours before the final hearing, Masimo makes a for-cause challenge to the continued service of the arbitrator. The challenge was based upon Masimo’s recent discovery that the Arbitrator’s brother (Stephen C. Neal) had represented its chief competitor in two highly contentious litigation losses to Masimo with liability verdicts totaling over half a billion dollars. One of the verdicts obtained against the Arbitrator’s brother was reported as one of the largest jury verdicts handed down in 2005.

Instead of having the challenge heard by JAMS, as required by JAMS’s rules, the Arbitrator himself determined that he was not subject to disqualification. The Arbitrator stated that he was not previously aware of his brother’s representation of Masimo’s rival or the defeats his brother had suffered, that he violated no disclosure obligations,

and that even if he had known of the information concerning his brother's previous representation and losses, it was not "sufficient to cause a person to reasonably doubt [his] ability to be impartial in this case" because "[n]o advantage could flow to [him] from disfavoring a company simply because [his] brother was [a] lawyer for a Masimo opponent." The final hearing was the punitive damages hearing and it proceeded as scheduled on January 10, 2014.

Five days after the hearing, the Arbitrator issued the final award and found in favor of plaintiffs on their wrongful termination claim, awarding the full amount of compensatory damages they had requested – approximately \$310,000. The Arbitrator then assessed Masimo with \$5 million in punitive damages. The Arbitrator acknowledged that this award was more than 16 times the total compensatory damages awarded, but reasoned that it was "in no sense disproportionate [because] it is only a fraction of [Masimo's] annual net income."

Masimo then petitioned the district court to vacate the award under Section 10(a)(2) of the Federal Arbitration Act ("evident partiality or corruption in the arbitrator"). The district court granted the motion, finding that the Arbitrator had demonstrated evident partiality by deciding the disqualification challenge himself and then imposed punitive damages on Masimo for making the challenge and for other reasonable acts of advocacy by its attorneys. The court also took issue with the Arbitrator's "dismissive" statement that there was no conflict because his brother had simply "represented companies adverse to Masimo in litigation." The court found that "[t]he circumstances in reality were much more serious," and that the Arbitrator's decision to decide the disqualification challenge himself, without make additional disclosures or providing facts on the record to refute the alleged conflict, "undermined the fairness of the proceeding and demonstrated his partiality."

(b) Business Relationships Between Arbitrators and Related Parties to the Arbitration are Expected and Tolerated as a Trade-Off for the Expertise and Informality Which Knowledgeable Arbitrators Lend to the Process – *Painters District Council 16 Local Union 294 v. Color New Co.*, 2013 WL 3992128 (E.D.Cal., Aug. 2, 2013)

This is a labor union arbitration matter in which the Union and the employer, both represented by counsel, appeared before a AAA arbitrator. The arbitrator was initially proposed by counsel for the respondent/employer. After hearing the parties' evidence, the arbitrator issued an initial award which found that the respondent/employer had violated the Master Labor Agreement and instructed the

parties to resolve the amount of damages. When the parties were unable to agree on the amount owed, the arbitrator issued an award in favor of the Union for about \$26,000 in wages and benefits.

After the arbitrator's award, the defendant/employer moved to vacate the award alleging, among other things, that the arbitrator failed to disclose material facts establishing his bias in favor of unions. Defendant pointed to a host of prior business or personal relations: e.g., the fact that prior to becoming a neutral, the arbitrator had represented unions for over 40 years; that the arbitrator's former firm still represents unions; that in an online interview, the arbitrator had expressed his support for the "union movement;" and that the arbitrator may have had a friend or acquaintance who worked in the office where the arbitration was held. The court denied the motion to vacate, finding that defendant's suspicions of bias were "speculative at best." *3.

To set aside an award for arbitration partiality, the undisclosed interest or bias must be direct, definite and capable of demonstration rather than remote, uncertain or speculative. While defendant was troubled with the arbitrator's previous association with unions, the court noted that business relationships between arbitrators and related parties to the arbitration are expected and tolerated as a trade-off for the expertise and informality which knowledgeable arbitrators lend the arbitration process. *4. "Courts have recognized the benefits of having a neutral arbitrator with extensive experience in a specific area ... arbitrate those same disputes." In this regard, the Court cited to Justice White's concurrence in *Commonwealth Coatings* where he stated: "It is often because they [arbitrators] are men [and women] of affairs, not apart from but of the marketplace, that they are effective in their adjudicatory function. [This means] that arbitrators are not automatically disqualified by a business relationship with the parties before them if [a party] is unaware of the facts but the relationship is trivial." The Court held that the same analysis applied to the statements the arbitrator had made in the online interview, and that his prior employment and associations were "remote and trivial." *Id.*

(c) District Court Stepped in to Remove an Arbitrator Before Entry of an Award Because Extreme Circumstances Existed – *Sussex v. Turnberry/MGM Grand Towers, LLC*, 2013 WL 6895845 (D.Nev., Dec. 31, 2013)

The underlying arbitration concerned a long-standing dispute brought by purchasers of condominium units developed and sold by defendants. The arbitrator was appointed in February 2010. One month later, the arbitrator founded and incorporated Bowdoin Street Capital LLC, whose website stated that the company's

business purpose was “to provide assistance to claimholders and their law firms in the resolution of disputes.” The website described the arbitrator as having experience as a neutral “in many large complex commercial arbitrations with claims ranging from \$20 to \$200 million,” and his LinkedIn profile announced that he had “refocused his practice to concentrate on the emerging field of Litigation Finance and Funding.” Based on the foregoing, the defendants asked the AAA to review the arbitrator’s appointment based on his failure to disclose his creation of Bowdoin and his pursuit of investment opportunities in litigation finance. In response to the inquiry, the arbitrator sent an email to the case manager in which he said that he had raised no money and made no investments; that with the exception of the company’s website presence, the company had been dormant since its creation. The email was treated as a supplemental disclosure and the decision was made to deny defendants’ removal request. Defendants then filed a motion in the district court seeking to disqualify the arbitrator. The issue presented to the court was whether it had authority under the FAA to address disqualification of the arbitrator before an award had been made. It concluded that it did and granted defendants’ motion disqualifying the arbitrator.

On the issue of stepping in pre-award, the court noted that while Section 10(a)(2) of the FAA does not expressly address a district court’s ability to remove an arbitrator for evident partiality prior to the entry of a final award, the Ninth Circuit in *Aerojet-General Corp. v. American Arbitration Ass’n*, 478 F.2d 248 (9th Cir. 1973) had left open the possibility that a district court could consider such pre-award challenges in “extreme cases.” 478 F.2d at 251. The court also noted that other federal courts had found that a district court may intervene in an ongoing arbitration proceeding under its power of equity. “[I]t simply does not follow that the policy objective of an expeditious and just arbitration with minimal judicial interference is furthered by categorically prohibiting a court from disqualifying an arbitrator prior to arbitration.” *2, citing *Metropolitan Property and Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F.Supp. 885 (D.Conn. 1991). The district court concluded that it made no sense to require the parties to proceed through the arbitration to final award, only to have to go through the whole process again if the arbitrator was then disqualified; that that course would only promote delay and waste in time and resources. *3.

On the issue of evidence partiality, the district court found that the arbitrator’s founding of a company that intends to profit from funding large, potentially profitable litigations of the kind that he was overseeing was likely to give rise to justifiable doubt regarding his impartiality, particularly since he failed to disclose his new pursuit. In this regard, the Court noted that the arbitrator stood to profit from a business hat funds plaintiffs in high-value cases such as the one before him; that the business pursuit he failed to disclose was substantial and his failure to disclose it created a reasonable

impression of partiality. *5. The Court concluded that requiring arbitrators to err on the side of disclosure is consistent with public interest in efficient and final arbitration, especially with regard to business activities that occurring during the course of the arbitration. “[M]id-arbitration disclosures are particularly important because they occur after the initial selection process and are easier for an arbitrator to hide or sweep under the rug.” *6.

The district court reasoned that it had two options. One option was to decline to determine whether there was evident partiality challenges intervene in the arbitration and disqualify the arbitrator

(d) An Example of Strategic Gamesmanship in Arbitration Gone Awry – *Thomas Kinkade Company v. White*, 711 F.3d 719 (6th Cir., Apr. 2, 2013)

Against the backdrop of a tortured set of facts representing the penultimate in gamesmanship aimed at 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].” 711 F3d 720. 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." *Id.* at 724. 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 of 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. at 724-725. 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 725.

(5) **Cases - California**

(a) **Attorney's Membership on the Same Provider Panel as the Arbitrator was a Required Disclosure - *Gray v. Chiu*, 2013 WL 222279 (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.

(b) Arbitrators are Only Required to Disclose Disqualifying Relationships of Which They are Aware – *Wasserman Comden Casselman & Einstein LLP v. Patel*, 2013 WL 5310137 (2nd Dist., Sep. 23, 2013) (Not Published)

In May 2008, the Patels retained Wasserman Comden Casselman & Einstein LLP (the “Wasserman Firm”) to represent them on a contingency fee basis in connection with an inverse condemnation / nuisance dispute involving the City of Glendale and others. In connection with the settlement of the condemnation action, a dispute arose between the Patels and the Wasserman Firm concerning the computation and amount of the Wasserman Firm’s contingent fee. Pursuant to the terms of the written fee agreement, the fee dispute was submitted to arbitration with ADR Services before a panel of three arbitrators: Retired Judges Romero, Hilberman and Collins. William Gwire, of the Gwire Law Offices, appeared for the Patels. David Casselman, of the Wasserman Firm, and Peter Ezzell, of the Law Offices of Peter Q. Ezzell, appeared for the Wasserman Firm. The arbitrators made disclosures of prior arbitrations, mediations and discovery references based upon this information.

After a five-day evidentiary hearing, the arbitrators issued their final binding arbitration award in favor of the Wasserman Firm for \$4.82 million, plus interest, attorney's fees in the amount of \$114,240 and costs in the amount of \$88,527. After the award was issued, the Patels hired new counsel - Jeffrey Huron - to review the arbitration proceedings. Huron was aware that Peter Ezzell served in an "of counsel" capacity to the law firm of Kaufman Dolowich Voluck & Gonzo LLP (the "Kaufman Firm") - a fact not disclosed to ADR Services or the arbitrators. Through discovery, Huron learned that the three arbitrators had a total of 14 undisclosed mediations and arbitrations with the Kaufman Firm, nine of which were initiated while the fee dispute arbitration was pending. When the Wasserman Firm petitioned to confirm the arbitration award, the Patels petitioned to vacate the award based upon the argument that the arbitrators had failed to make mandatory disclosures concerning the Kaufman Firm with whom Ezzell had an "of counsel" relationship. The Wasserman Firm's petition was granted and judgment was entered. The Patels appealed.

On appeal, the Second District affirmed the trial court, and found that there was substantial evidence to support the trial court's finding that none of the arbitrators was aware of Ezzell's relationship to the Kaufman Firm and did not subsequently become aware of that relationship prior to the issuance of the award. Quoting Ethics Standards 7(c) and (f), the court noted that "[a] proposed neutral arbitrator's disclosure obligations are limited to specific matters 'of which the arbitrator is then aware' and matters of which he or she 'subsequently becomes aware.'" *11. The Court of Appeal found that the trial court had properly denied the petition to vacate the arbitration award because CCP § 1286.2(a) permits vacatur only if the arbitrator failed to disclose a ground for disqualification of which the arbitrator was then aware. Quoting *Casden Park La Brea Retail, LLC v. Ross Dress for Less, Inc.*, 162 Cal. App. 4th 468, 477 (2008), the Court noted that the requirement of scienter "is a deliberate expression of the Legislature's intent to prevent the undoing of an arbitration award based upon an arbitrator's unknowing failure to disclose information." See also *Betz v. Pankow*, 31 Cal. App. 4th 1503, 1511-1512 (1995) (an arbitrator "cannot be faulted for failing to disclose facts of which he was unaware").

(c) **Arbitrator's Failure to Disclose that his Resume Listed as a Reference One of the Partners of a Firm Representing One of the Parties Required Vacatur – *Mt. Holyoke Homes, L.P. v. Jeffer Mangels Butler & Mitchell, LLP*, 219 Cal. App. 4th 1299 (2nd Dist., Sep. 24, 2013)**

After a failed effort to develop real estate in Pacific Palisades, clients sued the attorney and law firm who had represented them in that effort. The law firm cross-complained seeking payment of unpaid fees. The matter was ordered to arbitration pursuant to the arbitration provision included in the fee agreement. The parties initially selected retired Superior Court Judge Patricia Collins as the arbitrator, but one of the clients objected to her appointment after Judge Collins disclosed a prior relationship with the law firm's counsel. The parties then selected retired Superior Court Judge Eli Chernow as the arbitrator. Judge Chernow disclosed that he had known one of the attorneys who had worked on the real estate matter (but not a defendant), that he had conducted a mediation in which defendants' counsel had represented a party, and that he had conducted an arbitration and a mediation involving one of the plaintiffs. The parties agreed to Judge Chernow's appointment despite these disclosures of prior relationships and engagements.

After hearing the matter, Judge Chernow concluded that plaintiffs had failed to establish causation and were entitled to no relief on their claims. He also concluded that the defendant law firm was entitled to recover its unpaid legal fees for services provided and its reasonable attorney fees incurred in connection with the arbitration. That awarded amounted to \$18,132 in unpaid legal fees, \$285,000 in attorney fees incurred in connection with the arbitration, and over \$150,000 in costs.

The arbitration award prompted the clients to search the internet for evidence of the arbitrator's bias. On the website of the National Academy of Distinguished Neutrals, one of the clients discovered that Judge Chernow had listed a partner in the defendant law firm (Robert Mangels) as a personal reference. This relationship had not been disclosed by Judge Chernow prior to his appointment as arbitrator. Clients filed a motion to vacate due to Judge Chernow's failure to disclose his relationship with the defendant law firm through Mangels. The law firm opposed the motion and submitted a declaration from Judge Chernow, who stated that his website resume was over 10 years old, that his relationship with Mangels was purely professional and that he last served in a neutral capacity more than five years ago, that he had never discussed with Mangels including him as a reference on his resume, and that he had no personal relationship with Mangels. The trial court confirmed the arbitration award and found

that from the declarations of Mangels and Judge Chernow, the parties had “virtually no relationship beyond Mangels having appeared before Judge Chernow in the past;” that listing Mangels on a 10-year old resume was insufficient to trigger a mandatory disclosure obligation; and that a person aware of the facts would not entertain a doubt as to the impartiality of the arbitrator.

The Second District Court of Appeal disagreed with the trial court and reversed. The Court found that the connection between the undisclosed fact of the arbitrator’s naming an attorney as a reference on his resume and the subject matter of the arbitration, a legal malpractice action against the law firm in which the same attorney is a party, was sufficiently close that a person reasonably could entertain a doubt that the arbitrator could be impartial. “Judge Chernow presumably believed that Mangels had a favorable opinion of his abilities as a neutral and would speak positively about him if asked. An objective observer reasonably could conclude that an arbitrator listing a prominent litigator as a reference on his resume would be reluctant to rule against the law firm in which that attorney is a party as a defendant in a legal malpractice action.... To entertain a doubt as to whether the arbitrator’s interest in maintaining the attorney’s high opinion of him could color his judgment in these circumstances is reasonable, is by no means hypersensitive, and requires no reliance on speculation. We believe an objective observer of the facts reasonably could entertain such a doubt.” 219 Cal. App. 4th at 131.

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. Animal Feeds 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.

Similarly, 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 a consumer contract that 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 class proceeding. In the lower court proceedings before both the district court and the Ninth Circuit, defendant’s motion to compel individual arbitration and stay the class action proceedings was denied based on application of the “Discover Bank Rule” announced by the California Supreme Court in 2005: namely, that when a class action waiver is included in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably involve small amounts of damages, such waivers are unconscionable as a matter of law, making the arbitration agreement unenforceable. See, *Discover Bank v. Superior Court*, 36 Cal. 4th 148, 162 (2005). The Supreme Court reversed the Ninth Circuit, finding that because it “stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress (citation), California’s *Discover Bank* rule is preempted by the FAA.” 131 S.Ct. 1753.

The majority of federal appeals court and district court decisions have followed *Concepcion*. 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 the *Discover Bank* rule); *Litman v. Cellco 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 challenge to the enforcement of class action waivers).

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 443.² That being said, the *Brown* majority did not

² *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 comprehensive enforcement of overtime laws if the class action device is disallowed, the class action waiver must be invalidated.”

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*. 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). 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. See, *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).

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) **Parties' Intent to Permit Class Arbitration May be Expressly Stated or Implied in the Arbitration Provision Language – *Oxford Health Plans LLC v. Sutter*, ___ U.S. ___, 133 S.Ct. 2064 (Jun. 10, 2013)**

Dr. Sutter provided medical services to Oxford Health's insureds under a fee-for-service contract that required binding arbitration of contractual disputes. When Oxford Health failed to pay him fully and promptly for medical services rendered, Dr. Sutter filed a proposed class action in the New Jersey Superior Court. Oxford Health moved to compel arbitration, relying on the following clause in the contract:

"No civil action concerning any dispute arising under this Agreement shall be instituted before any court, and all such disputes shall be submitted to final and binding arbitration in New Jersey, pursuant to the rules of the American Arbitration Association with one arbitrator."

133 S.Ct. at 2067. The state court granted Oxford Health's motion and the matter was referred to arbitration.

In the arbitration, the parties agreed to submit to the arbitrator the issue of whether the parties' contract authorized class arbitration. The arbitrator concluded that

it did. Noting that the question turned on “construction of the parties’ arbitration agreement,” the arbitrator reasoned that the clause sent to arbitration “the same universal class of disputes” that it barred the parties from bringing as civil actions in court; that the intent of the clause was “to vest in the arbitration process everything that is prohibited from the court process.” *Id.* The arbitrator further reasoned that a class action “is plainly one of the possible forms of civil action that could be brought in a court” absent the agreement. Accordingly, the arbitrator concluded that “on its face, he arbitration clause ... expresses the parties’ intent that class arbitration can be maintained.” *Id.*

Oxford Health filed a motion in federal court seeking vacatur of the arbitrator’s decision on the ground that he had exceeded his powers under section 10(a)(4) of the Federal Arbitration Act. The District Court denied the motion and the Third Circuit affirmed. 2005 WL 6795061 (D.N.J., Oct. 31, 2005), *aff’d*, 227 Fed.Appx. 135 (2007). The matter was then returned to arbitration.

During the pendency of the arbitration, the Supreme Court decided *Stolt-Nielsen* – holding that an arbitrator may employ class procedures only if the parties have authorized them. 559 U.S. 662, 684. Oxford Health immediately asked the arbitrator to reconsider his decision on class arbitration in light of the *Stolt-Nielsen* decision. The arbitrator issued a new opinion in which he held that *Stolt-Nielsen* had no effect on the case because the agreement at issue authorized class arbitration. Unlike in *Stolt-Nielsen*, the parties in this case disputed the meaning of their contract and submitted that issue to the arbitrator to decide. The arbitrator had thus been required “to construe the arbitration clause in the ordinary way to glean the parties’ intent.” 133 S.Ct. at 2067. In performing that task, the arbitrator found “that the arbitration clause unambiguously evinced an intention to allow class arbitration.” *Id.* Oxford Health again petitioned the District Court to vacate the arbitrator’s decision under section 10(a)(4) of the Federal Arbitration Act. The District Court again denied the motion and the Third Circuit affirmed, ruling that Oxford Health’s objections to the arbitrator’s rulings were “simply dressed-up arguments that the arbitrator had interpreted its agreement erroneously.” In this regard, the Third Circuit held that so long as the arbitrator “makes a good faith attempt” to interpret a contract, “even serious errors of law or fact will not subject his award to vacatur.”

The Supreme Court granted certiorari and affirmed. In an opinion by Justice Kagan, the Court reasoned that FAA section 10(a)(4) limits a court’s ability to overturn an arbitrator’s decision where it is arguably based on an interpretation of the parties’ agreement. While the Court conceded that the parties’ agreement did not contain any language authorizing class arbitration, it noted that the arbitrator found the arbitration

clause “unambiguously evinced an intention to allow class arbitration” based on construing “the arbitration clause in the ordinary way to glean the parties’ intent.” Tacitly acknowledging the arbitrator’s potentially erroneous interpretation, the Court again made clear that section 10(a)(4) provides that the “arbitrator’s construction holds, however good, bad, or ugly.” Accordingly, the Court upheld the arbitrator’s decision to permit class arbitration under the unique facts of the case (discussed above) in terms of how that issue was teed up for the arbitrator to decide. In so holding, the Court limited the scope of *Stolt-Nielson*, explaining that it applies only where the parties’ agreement lacks *any* basis for allowing class proceedings. The Court pointed out that, there, the parties had entered into a stipulation that left no room for an inquiry regarding the parties’ contracting intent. Therefore, the arbitrators in that case could not have based their decision on a determination of the parties’ intent.

Citing *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003), the Court stated that the issue would have been different had Oxford Health challenged the availability of class arbitration as a “question of arbitrability.” Such questions include preliminary matters such as whether the parties have a valid agreement and are presumptively decided by the courts. Instead, Oxford Health challenged the decision as a matter within the arbitrator’s discretion to decide. Consequently, the Court did not inquire into whether class arbitration is a question of arbitrability.

(b) Class-Action Waiver Clause is Enforceable Even Though it is Uneconomical for Plaintiff to Pursue Federal Statutory Claim – *American Express Co. v. Italian Colors Restaurant*, ___ U.S. ___, 133 S.Ct. 2304 (Jun. 20, 2013)

Merchants doing business with AMEX filed class action alleging that AMEX had charged and received supra-competitive fees in violation of federal antitrust laws. The merchant agreements all contained an arbitration clause with an express class action waiver. AMEX moved to compel individual arbitration pursuant to the terms of the parties’ agreements. The merchants opposed the motion. 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 enforceability of the class action waiver 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 were 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 placed 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. Reconsideration en banc was denied, with five judges dissenting. *In re American Express Merchants' Litigation*, 681 F.3d 139 (2nd Cir. 2012). AMEX then filed a petition with the Supreme Court seeking a writ of certiorari. That petition was granted on November 9, 2012 to consider the question "[w]hether the Federal Arbitration Act permits courts . . . to invalidate arbitration agreements on the ground that they do not permit class arbitration of a federal-law claim." *American Express Co. v. Italian Colors Restaurant*, ___ U.S. ___, 133 S.Ct. 5941 (2012).

On review, the Supreme Court reversed and held that the FAA does not permit courts to invalidate a contractual waiver of class arbitration on the ground that the plaintiff's cost of individually arbitrating a federal statutory claim exceeds the potential recovery. In so holding, the Supreme Court reiterated its prior pronouncements that:

- the FAA reflects the overarching principle that arbitration is a matter of contract, citing *Rent-A-Center West, Inc. v. Jackson*, 561 U.S. 63 (2010);
- courts must "rigorously enforce: arbitration agreements according to their terms, citing *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985); and
- even claims alleging the violation of a federal statute are subject to binding arbitration unless the FAA's mandate has been "overridden by a contrary congressional command," citing *CompuCredit Corp. v. Greenwood*, ___ U.S. ___, 132 S.Ct. 665 (2012).

In the specific fact context of this case – antitrust violations – the Court also addressed and ruled on the "effective vindication" exception, which was discussed in dictum in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985). In *Mitsubishi Motors*, the Court expressed a willingness to invalidate an arbitration agreement on "public policy" grounds where the arbitration agreement operates "as a prospective waiver of a party's right to pursue statutory remedies. 473 U.S. at 637, n. 19. Dismissing concerns that the arbitral forum was inadequate, the Court said that "so long as the prospective litigant effectively may vindicate its statutory cause of action in the arbitral forum, the statute will continue to serve both its remedial and deterrent function." *Id.* That exception would cover a provision in an arbitration agreement forbidding the assertion of certain statutory rights, and would perhaps cover the situation where the filing and administrative fees attached to arbitration are so high as to make access to the forum impracticable. See, *Green Tree Financial Corp.-Ala. v. Randolph*, 531 U.S. 79, 90 (2000). That being said, plaintiffs' argument that it was not worth the expense of proving an antitrust claim on an individual basis did not qualify for exception because that was not the same thing as the elimination of the right to pursue a statutory remedy.

(c) **Arbitration Agreement Found to be Enforceable in Spite of Plaintiff's Claim that he Cannot Vindicate his Statutory Claims if Required to Arbitrate his Claims Individually Rather than on a Class Basis Because the Potential Recovery in Terms of Dollars is too Low – *Miguel v. JP Morgan Chase Bank*, 2013 WL 452418 (C.D.Cal., Feb. 5, 2013) (Superseded by *American Express v. Italian Colors Restaurant*)**

Plaintiff worked for the bank for about one year as an hourly employee. In connection with his employment, Plaintiff signed a statement acknowledging that any employment-related disputes that could not be resolved internally would be submitted to binding arbitration in accordance with the Arbitration Agreement available on the bank's website. The statement Plaintiff signed acknowledged that he had read and understood the Arbitration Agreement, accepted its terms and agreed that it was a condition to his employment.

After leaving the bank's employ, plaintiff filed a putative class action alleging various wage payment violations. In response, the bank moved to compel arbitration in accordance with the Arbitration Agreement that included an express agreement that claims would be submitted "on an individual basis" and no claims could "be arbitrated on a class or collective basis." The district court granted the bank's motion and ordered arbitration. In so doing, the district court rejected plaintiff's various attacks on the validity and enforceability of the arbitration agreement, including plaintiff's argument that if employees were compelled to arbitrate their statutory claims individually, they would lack the means to vindicate their statutory rights because the potential dollar recovery was so low on an individual basis that it would be difficult to secure representation. Relying on the Ninth Circuit's 2012 decision in *Coneff v. AT&T Corp.*, 673 F.3d 1155, 1158 (9th Cir. 2012), the district noted that the Ninth Circuit had interpreted the Supreme Court's holding in *Concepcion* to mean that banning class action waivers would be inconsistent with the FAA. Accordingly, the district court ruled that the arbitration agreement requiring individual arbitrations was enforceable even if plaintiff could not vindicate his statutory rights if required to arbitrate those claims individually. *7.

The district court went on to rule that plaintiff's PAGA claim was likewise arbitrable, agreeing with Judge Fess' decision in *Quevedo v. Macy's, Inc.*, 798 F.Supp. 2d 1122, 1141 (C.D.Cal., 2011) (Judge Fess recognized that the PAA claim was arbitrable to the extent the plaintiff asserted it in his own behalf because "[n]othing in the arbitration Plan Document would appear to preclude Plaintiff from pursuing this *individual* claim

for civil penalties in arbitration, and the agreement expressly provides that the same remedies that would be available in court are available in arbitration.”) In so ruling, the district court rejected the holding in *Urbino v. Orkin Services of California, Inc.*, 2011 WL 4595249 (C.D.Cal., Oct. 5, 2011), which distinguished PAGA claim waivers from *Concepcion* and found there to be a difference between a PAGA claim and a consumer class action. The district court agreed that PAGA’s legislative purpose means that it should be treated differently than a class action for purposes of class certification. However, it disagreed with *Urbino* insofar as it suggested that the nature of PAGA prevents the applicability of the FAA.

(d) Court Upholds Arbitration Agreement that Expressly Waived Plaintiff’s Right to Pursue a Representative PAGA Claim – *Parvataneni v. E*Trade Financial Corporation*, ___ F.Supp. 2d ___, 2013 WL 5340473 (N.D.Cal., Sep. 24, 2013)

Plaintiff claimed that his employer deprived him of overtime pay even when he worked more than forty hours per week. Plaintiff brought suit in state court PAGA violations with respect to unpaid overtime and E*Trade’s alleged failure to maintain adequate time keeping records. E*Trade removed the case to federal court and then filed motions to dismiss and to compel arbitration of plaintiff’s individual claim. The Court granted E*Trade’s motion, noting that there was no dispute between the parties concerning the existence of a valid arbitration agreement, but only whether plaintiff could assert claims on a representative basis under PAGA. Following the Supreme Court’s decision in *Stolt-Nielsen*, the Court found the agreement silent with respect to class arbitration and thus concluded that it could not order the case to proceed as a class. The district court found that there was no evidence that the parties had considered the issue of class arbitration prior to signing the contract and, as such, there was no contractual basis for concluding that they intended to include class arbitration in the terms of the agreement. The Court distinguished the situation and outcome in *Yahoo! Inc. v. Iversen*, 836 F.Supp. 2d 1007 (N.D.Cal. 2011) where the arbitration clause specified that the parties agreed to be bound by the rules of the American Arbitration Association, which in turn permitted class arbitration.

The district court also found that the agreement contained a valid PAGA waiver, stating clearly that “an arbitration agreement that denies a plaintiff the right to pursue a representative PAGA claim is still a valid agreement.” *5, citing *Morvant v. P.F. Chang’s China Bistro, Inc.*, 870 F.Supp. 2d 831, 846 (N.D.Cal., 2010) (holding that “the Court must enforce the parties’ Arbitration Agreement even if this might prevent Plaintiffs from acting as private attorneys general); cf. *Valle v. Lowe’s HIW, Inc.*, 2012 WL 4466523 at *2,3

(N.D.Cal., Aug. 30, 2012) (upholding arbitrator's decision to dismiss plaintiff's representative PAGA claims but permitting him to arbitrate his PAGA claims on an individual basis).

- (e) **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 and currently pending before the California Supreme Court as Case No. S204032.**

This case was included in the 2012 program and the case digest of the lower court proceedings is set forth below. Last year, the court of appeal in *Iskanian*, along with a number of federal courts, found that *Concepcion* applies even to PAGA claims and that the Federal Arbitration Act precludes California courts from ordering class wide arbitration of wage and hour claims unless the parties have expressly agreed to it. See, e.g., *Jasso v. Money Mart Exp., Inc.*, 879 F.Supp.2d 1038, 1043 (N.D.Cal. 2012); *Sanders v. Swift Transp. Co. of Arizona*, 843 F.Supp.2d 1033, 1036-1037 (N.D.Cal. 2012); *Lewis v. UBS Financial Services, Inc.*, 818 F.Supp.2d 1161, 1165-1166 (N.D.Cal. 2011); *Murphy v. DIRECTV, Inc.*, 2011 WL 3319574 (C.D.Cal. 2011); see also *Coneff v. AT&T*, 673 F.3d 1155, ___ (9th Cir. 2012) (held that a Washington state rule deeming class action waivers unconscionable was preempted by the Federal Arbitration Act in light of *Concepcion*). On September 19, 2012, the California Supreme Court granted review. As of July 2013, the matter had been fully briefed, and the matter was argued on April 4, 2014.

Digest from 2012 Program Materials:

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 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.

(f) 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 and currently pending before the California Supreme Court as Case No. S207760

This case was included in the 2012 program and the case digest of the lower court proceedings is set forth below. Last year, the court of appeal in *Franco* held that *Gentry* remained good law and that certain class action waivers were still subject to invalidation per the *Gentry* test because that test does not establish a categorical rule against class action waivers. Following on the heels of the *Franco* decision, the court of appeal in *Truly Nolan of America v. Superior Court*, 208 Cal. App. 4th 487 (2012) held that *Gentry* remained good law pending guidance from a higher court because, while *Concepcion* implicitly disapproved of the reasoning behind *Gentry*, it did not directly address the precise issue presented in *Gentry*. On February 13, 2013 the California Supreme Court granted review of the *Franco* decision. However, further action on that appeal has been deferred pending the disposition of *Iskanian*.

Digest from 2012 Program Materials:

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 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.

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 against 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 Action 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. 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. *Volt Information Sciences, Inc. v. Board of*

Trustees of Leland Stanford Jr. Univ., 489 U.S. 468, 478 (1989). An arbitrator’s authority over the parties and the subject matter of the dispute is consensual and must find its source in the parties’ agreement. *Steelworkers v. Warrior & Gulf Nav. Co.*, 363 U.S. 574, 582 (1960). 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. *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). 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,” and that “any doubts concerning . . . scope . . . be resolved in favor of arbitration.” *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); *Moses H. Cone*, supra, 460 U.S. at 24-25. 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. *KPMG LLP v. Cocchi*, ___ U.S. ___, 132 S.Ct. 23 (2011).³

(2) Cases

(a) **FAA Preempts Prohibition of Arbitration of
“Patient’s Bill of Rights” Claims – *Valley View
Health Care, Inc. v. Chapman*, ___ F.Supp.2d ____,
2014 WL 197778 (E.D.Cal., Jan. 16, 2014)**

California statutes, among them the so-called “Patient’s Bill of Rights” contained in the California Health and Safety Code, prohibit any person or organization from requiring a patient to waive rights to sue in court for violations covered by the statutes. Moreover, the law requires that arbitration clauses be segregated out from the rest of the admission documents, that they be in a specified font and size, and that they are presumptively invalid unless specific measures are taken to ensure a voluntary and knowing waiver of rights to sue in court.

³ In *Cocchi*, 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.

Licensed skilled nursing facilities (SNFs) and their nonprofit professional association brought suit against the Department of Public Health and its director, seeking declaratory and injunctive relief relating to California statutes and regulations restricting arbitration of claims arising out of the California "Patient's Bill of Rights" on the grounds that such laws are preempted by the FAA. In an exhaustive 42-page opinion, the district court found that the laws in question did conflict with the FAA as they picked out an arbitration clause and treated it differently than they did any other contract. In particular, two parts of the law were found defective in this regard. Those parts read:

"A current or former resident or patient of a skilled nursing facility ... may bring a civil action against the licensee of a facility who violates any rights of the resident or patient as set forth in the Patient's Bill of Rights **An agreement by a resident or patient of a skilled nursing facility or intermediate care facility to waive his or her rights to sue pursuant to this subdivision shall be void as contrary to public policy.**" (Bold added by the Court.)

And

"The licensee shall not present any arbitration agreement to a prospective resident as part of the Standard Admission Agreement. Any arbitration agreement shall be separate from the Standard Admission Agreement and shall contain the following advisory in a prominent place at the top of the proposed arbitration agreement '**Residents shall not be required to sign this arbitration agreement as a condition of admission to this facility, and cannot waive the ability to sue for violation of the Resident Bill of Rights.**'" (Bold in original statute.)

The district court granted summary judgment and, in so doing, declared the challenged arbitration laws invalid, unlawful and preempted by the FAA to the extent they bar arbitration of Patient's Bill of Rights claims and enjoined enforcement of the challenged laws to the extent they bar arbitration of Patient's Bill of Rights claims.

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*, 561 U.S. 63 (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) **On an Issue of First Impression, Incorporation of the UNCITRAL Arbitration Rules into an Arbitration Provision in a Commercial Contract Constitutes Clear and Unmistakable Evidence that the Parties Intended to Delegate Questions of Arbitrability to the Arbitrator – *Oracle America, Inc. v. Myriad Group A.G.*, 724 F.3d 1069 (9th Cir., Jul. 26, 2013)**

Myriad is a Swiss mobile software company. Oracle is a U.S. company based in Delaware. Oracle has a community licensing program that allows access to the Java programming language and use of Java trademarks in exchange for royalties. Among the various contract documents Myriad entered into in order to use the Java programming language and have access to Oracles testing protocols was a Source License that included an arbitration clause for any disputes arising out of or relating to the license. As is common in international, commercial contracts, the arbitration clause in the Source License stated that arbitration was to be administered in accordance with the UNCITRAL rules in effect at the time of the arbitration, which rules state (like the AAA Commercial Rules) that the arbitrator has authority to decide his/her/their jurisdiction.

In response to the lawsuit, Myriad moved to compel arbitration. The district court granted the motion with respect to Oracle's breach of contract claim, but denied it as to all other claims. In so ruling, the district court concluded that the incorporation of the UNCITRAL arbitration rules did not constitute clear and unmistakable evidence that the parties intended to delegate questions of arbitrability to the arbitrator. The district court reasoned that the relevant provision of the UNCITRAL rules stated only that the arbitrator had authority, but not exclusive authority, to decide jurisdiction.

Myriad took an appeal to the Ninth Circuit where the parties agreed that the only issue to be decided was whether the parties had agreed to arbitrate arbitrability by incorporating the UNCITRAL arbitration rules into their agreement. The Court noted that this issue was one of first impression for the Ninth Circuit, although the Second and D.C. Circuits have both concluded that incorporation of the UNCITRAL arbitration rules constitutes clear and unmistakable evidence that the parties to the agreement intended to arbitration questions of arbitrability. 724 F.3d at 1073-1075, citing *Republic of Ecuador v. Chevron Corp.*, 638 F.3d 384 (2nd Cir. 2011) and *Republic of Argentina v. BG Group PLC*, 665 F.3d 1363 (D.C. Cir. 2012). Consistent with these circuits, the Ninth

Circuit agreed with Myriad and reversed the district court's partial denial of the motion to compel arbitration of the non-contract claims. The Court noted that "[v]irtually every circuit to have considered the issue has determined that incorporation of the American Arbitration Association's (AAA) arbitration rules constitutes clear and unmistakable evidence that the parties agreed to arbitrate arbitrability;" that the AAA rules contain a jurisdictional provision similar to the one contained in the UNCITRAL arbitration rules; and that it saw no reason to deviate from "the prevailing view" so long as the arbitration agreement is between sophisticated parties. *Id.* at 1074-1075. With regard to the effect of incorporating arbitration rules into a consumer contract, the Court stated that it was expressing no opinion.

(b) The Issue Concerning the Validity of an Arbitration Clause is Distinct from the Contract Claims and, as Such, the Court Should Decide that Issue – *Smith v. JEM Group, Inc.*, 737 F.3d 636 (9th Cir., Dec. 12, 2013)

Rosita Smith filed a putative class action in federal court against JEM Group, Inc. and others, alleging (among other things) that they had charged more for debt-relief services than allowed under Washington law. Under Washington law, a debt-settlement service provider may not charge more than \$25 as an initial payment, 15% of any single payment, or 15% of the debtor's total debt. However, the statute provides an exception for debt-adjustment services performed by attorneys when those services are incidental to the practice of law. According to Smith's complaint, JEM and other debt-adjustment companies, associated with law firms that were willing to lend their names to "the cause" in an attempt to avoid the statutory limits otherwise applicable to debt-relief services.

Smith engaged JEM to assist her with settlement of her debts. Smith signed a 21-page contract that included a four-page, fine-print, attorney retainer agreement with one of the defendant/associated law firms. The attorney retainer agreement contained an arbitration clause on the fourth page of the document. After Smith filed her lawsuit against JEM and the other defendants, JEM and another defendant, who were not parties to the attorney retainer agreement, moved to compel arbitration based on the argument that they were third-party beneficiaries of the arbitration clause included in the attorney retainer agreement. Smith opposed the motion contending that the arbitration clause included in the attorney retainer agreement was unconscionable. The district court denied the motion and JEM appealed (the other defendants having dropped their right to appeal).

On appeal, JEM argued that an arbitrator should have decided the validity of the arbitration clause. The Ninth Circuit disagreed, finding that this case was one in which the invalidity of the arbitration clause was distinct from the contract claims in the case and, as such, the district court properly considered the validity of the arbitration clause. “We have held that ‘the question of arbitrability is for the court to decide regardless of whether the specific challenge to the arbitration clause is raised as a distinct claim in the complaint’ so long as ‘the plaintiff’s challenge to the validity of an arbitration clause is a distinct question from the validity of the contract as a whole....” 737 F.3d at 639, citing *Bridge Fund Capital Corp. v. Fastbucks Franchise Corp.*, 622 F.3d 996, 998 (9th Cir. 2010).

The Ninth Circuit reviewed Washington state law and found that a clause is unconscionable if it is procedurally unconscionable, in contrast to the majority view which requires a showing of both procedural and substantive unconscionability. The Court found that the district court had properly concluded that all requirements for a finding of unconscionability under Washington law existed. Accordingly, the Ninth Circuit affirmed, finding that there was no evidence to suggest that the district had erred.

(c) Whether Arbitration Agreement Provided for Collective Arbitration was Issue for the Court – not the Arbitrator – to Decide – *Parvataneni v. E*Trade Financial Corporation*, ___ F.Supp. 2d ___, 2013 WL 5340473 (N.D.Cal., Sep. 24, 2013)

Plaintiff claimed that his employer deprived him of overtime pay even when he worked more than forty hours per week. Plaintiff brought suit in state court PAGA violations with respect to unpaid overtime and E*Trade’s alleged failure to maintain adequate time keeping records. E*Trade removed the case to federal court and then filed motions to dismiss and to compel arbitration of plaintiff’s individual claim. The Court granted E*Trade’s motion, noting that there was no dispute between the parties concerning the existence of a valid arbitration agreement, but only whether plaintiff could assert claims on a representative basis under PAGA. Following the Supreme Court’s decision in *Stolt-Nielsen*, the Court found the agreement silent with respect to class arbitration and thus concluded that it could not order the case to proceed as a class. The district court found that there was no evidence that the parties had considered the issue of class arbitration prior to signing the contract and, as such, there was no contractual basis for concluding that they intended to include class arbitration in the terms of the agreement. The Court distinguished the situation and outcome in *Yahoo! Inc. v. Iversen*, 836 F.Supp. 2d 1007 (N.D.Cal. 2011) where the arbitration clause

specified that the parties agreed to be bound by the rules of the American Arbitration Association, which in turn permitted class arbitration.

Plaintiff argued that whether the agreement provided for collective arbitration was a matter for the arbitrator – not the court – to decide. The Court rejected that argument, finding that there was no “clear and unmistakable evidence” that the parties intended to arbitrate arbitrability; that the arbitration agreement was “completely silent as to the issue of who should decide questions of arbitrability.” *4. The Court again referred to its decision in *Yahoo! Inc. v. Iversen*, 836 F.Supp. 2d 1007 (N.D.Cal. 2011) and again noted that the parties had chosen to not incorporate the rules of the American Arbitration Association into their agreement; that had they done so, those rules would have permitted an arbitrator to decide the matter. *Id.*

(d) The Issue of Whether Plaintiffs had to Proceed on an Individual Basis or Could Proceed on a Class Basis was a Matter of Contract Interpretation and Thus a Matter for the Arbitrator (not the Court) to Decide – *Lee v. JP Morgan Chase & Co.*, __ F.Supp. 2d __, 2013 WL 6068601 (C.D.Cal., Nov. 14, 2013)

Plaintiffs were employed as appraisers by JP Morgan or its predecessor (WAMU). Plaintiffs filed a class action complaint against JP Morgan alleging violations of various California and federal labor laws and California’s unfair competition law. Based upon the arbitration agreements plaintiffs signed as part of their employment, JP Morgan moved to compel arbitration on an individual basis. The arbitration provision used “standard” and did not contain an express waiver of class, collective or representative claims. Plaintiffs did not dispute the validity of the arbitration agreements, and stipulated that their claims should be resolved in arbitration. The question posed to the court was whether the claims submitted to arbitration had to be submitted on an individual basis or whether they could proceed in arbitration on a class basis. The court thus determined that “the relevant question here is what *kind of arbitration proceeding* the parties agreed to,” and that that question concerned contract interpretation and arbitration procedures, which an arbitrator was “well situated to answer.” *2. Accordingly, the court denied JP Morgan’s motion to compel arbitration on an individual basis and, pursuant to the parties’ stipulation, found that the entire action was subject to binding arbitration and dismissed the court action in its entirety with prejudice. *4.

(e) **The Issue of Whether Litigation Conduct Amounts to a Waiver of the Right to Arbitration is for the Courts Rather Than the Arbitrator to Decide – *Hong v. CJ CGV American Holdings, Inc.*, 222 Cal. App. 4th 240 (2nd Dist., Dec. 18, 2013)**

Minority shareholders brought suit against majority shareholders for breach of fiduciary duty. Plaintiffs filed their original complaint in July 2012. Before defendants responded, plaintiffs filed a first amended complaint. Defendants filed a demurrer to the first amended complaint in September 2012, which was sustained with leave to amend. Plaintiffs then filed a second amended complaint in October 2012. In November 2012, defendants moved the court to require plaintiffs to furnish a bond pursuant to Corporations Code section 800. After the trial court denied that motion, defendants moved to compel arbitration. The plaintiffs opposed that motion on several grounds, including waiver by litigation conduct. The trial court agreed with plaintiffs and denied defendants' motion. Defendants appealed.

On appeal, the Court of Appeal noted that California statutory and decisional authority recognize the issue of waiver by litigation conduct is ordinarily resolved by the trial court and not the arbitrator. 222 Cal. App. 4th at 243, citing Code Civ. Proc. § 1281.2; *Engalla v. Permanente Medical Group, Inc.*, 15 Cal. 4th 951, 982 (1997).

Defendants argued that under the United States Supreme Court's decision in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 84 (2002), that arbitrator – not the court – should decide the issue of arbitrability and any defense to arbitrability, including waiver, citing the following passage from *Howsam*: "So, too, the presumption is that the arbitrator should decide 'allegation[s] of waiver, delay, or a like defense to arbitrability.'" After an extensive analysis, the Court of Appeal concluded that the waiver by litigation issue was not present in *Howsam* or the case it relied upon, so it was "unpersuaded" that *Howsam* required the arbitrator to decide the issue of waive by litigation conduct. In this regard, the Court noted that the United States Supreme Court "has repeatedly emphasized that its decisions are not controlling authority for propositions not considered by it in the case." Id. at 255, citing *Landgraf v. USI Film Products*, 511 U.S. 244, 265 (1994). After reviewing several other Court of Appeal opinions which had directly addressed the issue of waiver by litigation conduct, the Court concluded that the issue of waiver by litigation conduct was for the court – not the arbitrator – to decide.

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 enforcement issues and look at the courts’ treatment and reasoning concerning defenses to the enforceability of an arbitration agreement.

(2) Cases

- (a) **After *Concepcion*, Courts May Continue to Apply State Law Unconscionability Doctrine as a Valid Defense to a Petition to Compel Arbitration – *Sonic-Calabasas A, Inc. v. Moreno*, 57 Cal. 4th 1109 (Oct., 17, 2013)**

This case started as one in which the legal issue presented was whether an employer, as a condition of employment, could require an employee to waive the right to a Berman hearing (a dispute resolution procedure/administrative forum established by the Legislature to assist employees in recovering unpaid wages). In *Sonic-Calabasas A, Inc. v. Moreno*, 51 Cal. 4th 659 (2011) (*Sonic I*), the California Supreme Court held as a categorical rule that it is contrary to public policy and unconscionable for an employer to require an employee, as a condition of employment, to waive the right to a Berman hearing. The Court further held that its rule prohibiting waiver of a Berman hearing does not discriminate against arbitration agreements and is therefore not preempted by the Federal Arbitration Act. The Court did not invalidate the arbitration clause at issue. Instead, it held that if one of the parties was dissatisfied with the result of the Berman hearing, it could move to arbitrate the wage dispute consistent with the arbitration agreement, just as a dissatisfied party could obtain a trial in court absent an agreement to arbitrate.

The United States Supreme Court granted certiorari in *Sonic I*, vacated the judgment and remanded the case to the California Supreme Court for consideration in light of the Court's decision in *Concepcion*, where it clarified the limitations that the FAA imposes on a state's capacity to enforce its rules of unconscionability on parties to arbitration agreements. On remand, the Court concluded that because compelling the parties to undergo a Berman hearing would impose significant delays in the commencement of arbitration, the approach it took in *Sonic I* was inconsistent with the FAA. Accordingly, the Court held that, contrary to *Sonic I*, the FAA preempts a state-law rule categorically prohibiting waiver of a Berman hearing in a predispute arbitration agreement imposed on an employee as a condition of employment. At the same time, the Court concluded that state court may continue to enforce unconscionability rules that do not interfere with fundamental attributes of arbitration. 57 Cal. 4th at 1124, citing *Concepcion*, 131 S.Ct. 1740, 1748.

“Although a court may not refuse to enforce an arbitration agreement imposed on an employee as a condition of employment simply because it requires the employee to bypass a Berman hearing, such an agreement may be unconscionable if it is otherwise unreasonably one-sided in favor of the employer.... The fundamental fairness of the bargain, as with all contracts, will depend on what benefits the employee received under the agreement’s substantive terms and the totality of the circumstances surrounding the formation of the agreement.”

Id. at 1125.

In this case, the employee contended that the particular arbitration scheme provided under the agreement was unconscionable, while the employer contended that it offered adequate protections and advantages to facilitate the determination of the employee’s claim and that it was not unreasonably one-sided. The Court did not reach unconscionability as it pertained to the particular contract at issue in the case because evidence relevant to the unconscionability claims had not been developed in the trial court proceedings below. That matter was thus remanded to the trial court to determine whether the arbitration agreement was unconscionable.

**(b) Non-Signatory Defendant May Not Invoke
Equitable Estoppel Against Signatory Plaintiff to
Compel Arbitration – *Rajagopalan v. NoteWorld,
LLC*, 718 F.3d 844 (9th Cir., May 20, 2013)**

Amrish Rajagopalan accumulated approximately \$15,000 in student loan debt and after losing his job, had difficulty repaying his debts. He decided to seek professional assistance and signed up for First Rate Debt Solutions’ debt settlement program. He picked First Rate after being told that they had skilled lawyers and negotiators that would settle his debts for pennies on the dollar, and that First Rate’s fees would not exceed \$2,000. In order to engage First Rate, Rajagopalan was sent an email with a link to First Rate’s electronic contract document, which he then signed electronically. The contract document was 13 pages long and contained an arbitration clause requiring arbitration of any disputes in Florida. Rajagopalan resided in the state of Washington. NoteWorld was later designated by First Rate as the processing agent who would handle the automatic, monthly debits to Rajagopalan’s bank account, which were then deposited into an account in his name at NoteWorld as a “reserve” to pay creditors as settlements were negotiated.

After less than a year, Rajagopalan was dissatisfied with First Rate's service/results and cancelled his membership. At this point in time, over \$8,200 had been withdrawn from Rajagopalan's account and deposited into his NoteWorld account. NoteWorld refunded \$5,424 to Rajagopalan, but would not refund its fee (\$170) or the amount that had been paid over to First Rate (\$2,865). Rajagopalan complained informally to NoteWorld about the fact that the withheld amounts exceeded what First Rate had represented to him would be the fees incurred in connection with his debt settlement efforts. NoteWorld's in-house counsel responded and explained that NoteWorld is a completely separate entity from First Rate and performed as a "vehicle for payment processing," acting as an independent third-party and not as an agent of First Rate; that NoteWorld was not a debt relief company and did not enter into a contract with Rajagopalan to provide him with debt relief services.

Rajagopalan then filed a class action complaint in federal court in the state of Washington. NoteWorld moved to compel arbitration pursuant to the arbitration clause contained in Rajagopalan's contact with First Rate. The district court denied NoteWorld's motion, finding that the arbitration clause was unconscionable (and thus unenforceable) and, further, that NoteWorld was not a signatory and thus not entitled to enforce the agreement to arbitrate entered into between Rajagopalan and First Rate. NoteWorld appealed.

On appeal, in a *per curiam* opinion, the Ninth Circuit affirmed the trial court's decision. The Ninth Circuit found that the district court correctly held that NoteWorld was not a third-party beneficiary to the contract containing the arbitration clause because, under Washington state law, "both contracting parties must intend that a third party beneficiary contract be created." The Ninth Circuit also found that the district court properly concluded that NoteWorld may not invoke the arbitration clause on the basis of equitable estoppel – a doctrine that precludes a party from claiming the benefits of a contract while simultaneously attempting to avoid the burdens that contract imposes. See, *Mundi v. Union Sec. Life Ins. Co.*, 555 F.3d 1042, 1045 (9th Cir. 2009). The Ninth Circuit noted that where other circuits have granted motions to compel arbitration on behalf of non-signatory defendants against signatory plaintiffs, it was "essential in all of these cases that the subject matter of the dispute was intertwined with the contract providing for arbitration." *Id.*, quoting *Sokol Holdings, Inc. v. BMB Munia, Inc.*, 542 F.3d 354, 361 (2d Cir. 2008). In this case, Rajagopalan did not contend that NoteWorld or any other party breach the terms of the contract he entered into with First Rate. Instead, all that Rajagopalan asserted were statutory claims that were separate from the contract itself. The Ninth Circuit concluded that because Rajagopalan's statutory claims did not arise out of or relate to the contract that

contained the arbitration agreement, NoteWorld could not compel Rajagopalan to arbitrate his claims on the basis of equitable estoppel. 718 F.3d at 847-848.

(c) Absent a Showing of Prejudice, Years of Delay and Court Litigation Does not Amount to Waiver of the Right to Arbitrate – *Richards v. Ernst & Young LLP*, 734 F.3d 871 (9th Cir. – Per Curiam, Aug. 21, 2013) (Rex Heinke Case)

In 2005, several former employees of Ernst & Young LLP filed suit for alleged wage and hour violations. In 2008, Michelle Richards filed a separate wage and house lawsuit against Ernst & Young for herself and others similarly situated. The Richards action was consolidated with the earlier action and in 2011, a class was certified with Richards as the representative plaintiff for a narrowly defined class of employees. After the United States Supreme Court rendered its decision in *AT&T Mobility LLC v. Concepcion*, ___ U.S. ___, 131 S.Ct. 1740 (2011), Ernst & Young filed a motion to compel arbitration of Richards' claims. Richards opposed the motion, arguing that Ernst & Young had waived its right to compel arbitration by participating in the litigation for several years, by conducting discovery, and by failing to assert its right to arbitration as a defense in its answer in the earlier action filed by two other former employees. The district court agreed with Richards and denied Ernst & Young's motion on the grounds of waiver. Ernst & Young appealed.

On appeal, in a per curiam decision, the Ninth Circuit reversed. On the issue of waiver, the Court noted that it has previously held that waiver of a contractual right of arbitration "is not favored," and that any party arguing waiver of arbitration "bears a heavy burden of proof." 734 F.3d at 873, citing *Fisher v. A.G. Becker Paribas, Inc.*, 791 F.2d 691, 694 (9th Cir. 1986). Specifically, a party seeking to prove waiver of a right to arbitration must demonstrate "(1) knowledge of an existing right to compel arbitration; (2) acts inconsistent with that existing right; and (3) prejudice to the party opposing arbitration resulting from such inconsistent acts." *Id.*

Richards argued that she was prejudiced in two regards: First, that there had been "litigation on the merits" in the form of rulings on a motion to dismiss brought by Ernst & Young. Second, that Ernst & Young had conducted discovery during the course of the litigation that had caused her to incur expenses related to same. The Ninth Circuit found that neither argument amounted to a showing of prejudice because the rulings on the motion to dismiss did not reach the merits and there was no showing or contention that Ernst & Young had used discovery in the litigation to gain information about Richards' case that it could not have gained in the arbitration. Absent a finding of

prejudice, the Ninth Circuit concluded that the district court should have compelled arbitration. Additionally, because the arbitration agreement between Ernst & Young and Richards precludes class arbitration, the Court vacated the district court's order certifying a class of litigants with Richards as its representative.

(d) No Procedural Unconscionability Where the Arbitration Clause was not Buried in Fine Print, but was in its Own Section and Clearly Labeled – *Kilgore v. KeyBank National Ass'n*, 718 F.3d 1052 (9th Cir., Apr. 11, 2013)

Students of a failed flight-training school brought a putative class action against the bank that originated their student loans seeking to enjoin the bank from reporting their nonpayment of the student loan notes to credit agencies and from enforcing the notes. The promissory notes signed by the students contained an arbitration clause. Defendants removed the action to federal court and then filed a motion to compel arbitration. The district court denied that motion and defendants appealed. On appeal, the Ninth Circuit vacated, reversed and remanded, finding that the arbitration clause in question was neither substantively nor procedurally unconscionable under California law. The arbitration clause was not buried in fine print, but was instead in its own section and clearly labeled.

With regard to plaintiffs' "public injunction" argument, the Court held that even assuming the continued viability of the *Broughton-Cruz* rule – under which suits for public injunctive relief are exempted from arbitration – that rule did not apply because the relief sought by the putative class action was to vindicate the private rights of the putative class members. "Public injunctive relief 'is for the benefit of the general public rather than the party bringing the action.' . . . A claim for public injunctive relief therefore does not seek 'to resolve a private dispute but to remedy a public wrong.' . . . Whatever the subjective motivation behind a party's purported public injunction suit, the *Broughton* rule applies only when 'the benefits of granting injunctive relief by and large do not accrue to that party, but to the general public in danger of being victimized by the same deceptive practices as the plaintiff suffered.'" 718 F.3d at 1060, citing *Broughton v. Cigna Healthplans of California*, 21 Cal. 4th 1066 (1999).

(e) **Arbitration Agreement Found to be Unconscionable Under State Law and FAA Does not Preempt – *Chavarría v. Ralphs Grocery Co.*, 733 F.3d 916 (9th Cir., Oct. 28, 2013)**

Before obtaining a job as a deli clerk at Ralph's, plaintiff completed an employment application. The application states that by completing the application, all potential employees agree to be bound by Ralph's arbitration policy. That "policy" is not stated in the application and a copy of the policy is not provided with the application. The application does not require the prospective employee's signature and in this case, the application was not signed by plaintiff. Plaintiff worked for Ralph's for six months and, after she left, she filed a putative class action alleging wage and hour violations. Ralphs moved to compel individual arbitration pursuant to its arbitration policy. Plaintiff opposed the motion, arguing that it was unconscionable. The district court agreed with plaintiff and denied Ralph's motion. This appeal followed.

On appeal, the Ninth Circuit agreed with the district court and held that Ralph's arbitration policy was unconscionable under California law and thus unenforceable. The Court also found that the FAA did not preempt California law in this case.

The Court focused on three provisions of the Ralph's arbitration policy. First, Ralph's policy provided that if the parties could not agree on an arbitrator, they were required to go through a process in which each party named three arbitrators and they took turns striking names, with the party who opposed arbitration striking first. Second, with regard to attorney and arbitration fees and costs, the Court found that Ralph's policy provision was "more than a little convoluted," requiring that the arbitrator's fees be apportioned at the outset of the arbitration and split evenly between Ralph's and the employee "unless a decision of the U.S. Supreme Court directly addressing the issue requires that they be apportioned differently." Third, Ralph's policy gave Ralphs the right to unilaterally modify the arbitration policy without notice.

The Ninth Circuit reviewed California law on unconscionability and found that Ralph's arbitration policy was procedurally unconscionable because plaintiff could only agree to be bound by the policy or seek work elsewhere (a classic take-it-or-leave-it situation). Further, relying on its earlier decision in *Pokorny v. Quixtar, Inc.*, 601 F.3d 987 (9th Cir. 2010) where the Court held that procedural unconscionability is enhanced when a contract binds an individual to later-provided terms, the Court noted that in this case, Ralphs did not provide plaintiff with the terms of the arbitration policy she was required to accept as part and parcel of the employment application process, until her orientation three weeks later. The employment application merely contained a one-

paragraph “notice” of the policy, but the policy itself (provided after-the-fact of employment) was a four-page, single-spaced document with several complex terms. See also *Harper v. Ultimo*, 113 Cal. App. 4th 1402 (2003) (holding that a contract was procedurally unconscionable because the customer was forced to obtain the terms from another source “to find out the full import of what he or she is about to sign”). Accordingly, the Court held that Ralphs’ arbitration policy fit squarely within the decisions on procedural unconscionability and that the district court did not err when it so ruled.

With regard to substantive unconscionability, the district court found that several terms rendered Ralphs’ arbitration policy unconscionable and thus unenforceable. First, the court noted that Ralphs’ arbitrator selection provision would always produce an arbitrator proposed by Ralphs in employee-initiated arbitration proceedings. Second, the court cited the preclusion of utilizing institutional arbitration providers – namely AAA and JAMS – which have established rules and procedures in place for the selection of a neutral arbitrator. Third, the court was troubled by the cost sharing/allocation provision. The Ninth Circuit agreed with the district court that the combination of these terms “lacks any semblance of fairness and eviscerates the right to seek civil redress.... To condone such a policy would be a disservice to the legitimate practice of arbitration and a stain on the credibility of our judicial system.” 733 F.3d at 923.

With respect to FAA preemption, the Court wrote that the unconscionability doctrine used to review this case applies equally to all contracts, be they contracts to arbitrate or contracts to do any other thing. Therefore, the FAA was inapplicable as it reserves all traditional contract defenses to parties opposing contracts to arbitrate. On this point, the Court concluded, “[i]f state law could not require some level of fairness in an arbitration agreement, there would be nothing to stop an employer from imposing an arbitration clause that, for example, made its own president the arbitrator of all claims brought by its employees. Federal law favoring arbitration is not a license to tilt the arbitration process in favor of the party with more bargaining power. California law regarding unconscionable contracts, as applied in this case, is not unfavorable towards arbitration, but instead reflects a generally applicable policy against abuses of bargaining power. The FAA does not preempt its invalidation of Ralphs’ arbitration policy.” *Id.* at 927.

(f) ***Concepcion* Preempts *Broughton-Cruz* Rule on Private Attorney General Actions – *Ferguson v. Corinthian Colleges, Inc.*, 733 F.3d 928 (9th Cir., Oct. 28, 2013)**

Corinthian Colleges owns and operates several for-profit academic institutions nationwide. Kevin Ferguson and Sandra Muniz attended two of those institutions. Kevin Ferguson attended Everest Institute for approximately one year and graduated from its “Medical Assistant Program.” Sandra Muniz attended Heald College for three years, taking various courses and completing the business skills program. Both students financed their education through student loans and both were unable to find meaningful employment after graduation.

Ferguson and Muniz brought two separate putative class actions against Corinthian, seeking both money damages and injunctive relief for various state law claims (e.g., unfair competition under Business and Professions Code section 17200 et seq. (“UCL”), false advertising under Business and Professions Code section 17500 et seq. (“FAL”) and violation of consumer protection laws under Civil Code section 1750 et seq. (“CLRA”). Those actions were consolidated. Corinthian then moved to compel arbitration of the entire action pursuant to the arbitration clause contained in the enrollment agreement signed by Ferguson and Muniz when they began their respective courses of study. The district court granted the motion with respect to most of plaintiffs’ claims and stayed those claims pending arbitration. Applying California’s *Broughton-Cruz* rule, the district court declined to compel arbitration of plaintiffs’ requests for injunctive relief under the UCL, FAL and CLRA, though it sent plaintiffs’ requests for damages under those statutes to arbitration. Corinthian appealed.

On appeal, the Ninth Circuit reversed, finding that *Concepcion* preempted the so-called *Broughton-Cruz* rule that arbitration may not be compelled when a plaintiff, acting as a private attorney general, seeks a “public injunction” to enjoin future deceptive practices for the benefit of the general public. In so ruling, the Court rejected the argument that because an injunction is technically a remedy rather than a cause of action, the *Broughton-Cruz* rule is insulated from the FAA. As stated by the Supreme Court in *Concepcion* in 2011 and reiterated in 2010 in *Marmet Health Care Center, Inc. v. Brown*, ___ U.S. ___, 132 S.Ct. 1201 (2012), “[w]hen state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.”

Recognizing that its decision overruled an important aspect of consumer protection in California, the Ninth Circuit offered some hints about how plaintiffs might proceed in the future, but withheld judgment about the success of those possible procedures. “We decline to resolve in advance the question of what, if any, court remedy Plaintiffs might be entitled to should the arbitrator determine that it lacks the authority to issue the requested injunction. That is beyond the scope of this appeal. If the arbitrator comes to that conclusion, Plaintiffs may return to the district court to seek their public injunctive relief. We express no opinion on any question that might arise at that time. Similarly, we decline to resolve now questions that could arise or a motion is brought in court to confirm an arbitration award that includes injunctive relief, or whether it might be necessary for a court to enforce a public injunction awarded by an arbitrator. Those questions can be better addressed in the context of an actual case, with arguments directed more specifically to the questions raised in that case.” *Id.* at 937.

(g) After a Very Long Battle, DirecTV Prevails on Motion to Compel Arbitration – *Lombardi v. DirecTV*, ___ Fed. Appx. ___, 2013 WL 6224642 (9th Cir., Dec. 2, 2013)

In a long saga that resulted in multi-district litigation, DirecTV sought to compel arbitration in a consumer class action alleging that DirecTV had charged improper early cancellation fees. The district court denied a motion to compel arbitration on the grounds that the arbitration agreement contained in the subscription agreement was unconscionable under California, Arizona, Florida and Pennsylvania law. After the decision was made, the Supreme Court decided *Concepcion*, which invalidated the basis for the district court’s finding of unconscionability (the FAA “prohibits States from conditioning the enforceability of certain arbitration agreements on the availability of class wide arbitration procedures”). 131 S.Ct. 1740, 1744.

In the proceedings below, the district court applied California law to residents of other states who originally sued DirecTV in California based on California’s “fundamental policy against the enforceability of class-action waivers.” The Ninth Circuit reversed and held that that policy was no long cognizable in arbitration agreements governed by the FAA after *Concepcion*. Accordingly, the Court ruled that the choice of law provision in the Customer Agreement must be enforced because the plaintiffs have identified no other conflict between the laws of their home states and a fundamental policy of California. Under the various applicable state laws, the Court held that plaintiffs’ argument that the arbitration agreement is substantively unconscionable because it imposes a nonmutual obligation to arbitrate failed.

Accordingly, the arbitration agreement was enforceable and that matter was remanded to the district court.

(h) Deceptive Sign-In Page Results in No Contract Formation and Thus No Arbitration Agreement – *Lee v. Intelius, Inc.*, 737 F.3d 1254 (9th Cir., Dec. 16, 2013)

Lee purchased a background check and report from Intelius on the Internet. After Lee gave his credit card number and clicked to confirm his purchase, he was directed to a new webpage. Intelius was the only company name that appeared on that page. Lee clicked on a large orange button with the words “YES And show my report.” Small print on the page indicated that by clicking the “YES” button, he had thereby ostensibly agreed to a seven-day free trial of a “Family Safety Report” and a monthly obligation to pay \$19.95 for that report. At the bottom of the webpage were two hyperlinks labeled, in small, underlined black print, “Privacy Policy” and “Terms and Conditions.” If Lee had clicked on the “Terms and Conditions” link, he would have been sent to yet another webpage which contained the “TERMS OF MEMBERSHIP AND MEMBERSHIP AGREEMENT.”

Approximately one year after purchasing the background check, Lee discovered that Adaptive Marketing had been billing him each month for the “Family Service Report.” Lee and other named plaintiffs brought a state-law class action against Intelius. Intelius in turn filed a third-party complaint against Adaptive Marketing, who then moved to compel arbitration of both Lee’s and Intelius’ claims based upon the arbitration clause contained in the “Terms of Membership and Membership Agreement” described above. The district court denied Adaptive Marketing’s motion to compel. With regard to Lee’s claims, the court held that Lee did not agree to arbitrate. “Lee was asked to agree only to the ‘Offer Details displayed to the right’ and, given the language of those Details, would have no reason to go looking for other terms and conditions that might apply.” Defendant appealed.

The Ninth Circuit affirmed the trial court’s ruling that found the arbitration clause – buried as it was – inapplicable and unenforceable. The Court wrote that “Washington law requires that the ‘essential elements’ of the contract be set forth in writing. An essential element is identification of the parties to the contract. Adaptive admits that the contract must identify the contracting parties, though it contends that the parties need not be identified by name. There is nothing on the new webpage offering the Family Safety Report, to which Lee was directed, that identified Adaptive or an Adaptive-related entity as the party with which Lee was contracting ... Even an

exceptionally careful consumer, who understood that he or she was being asked to enter into a contract for an additional product, would likely have thought that the contracting party was Intelius. Adaptive's name appeared nowhere on the new webpage. In contrast, Intelius's name and logo were prominently displayed at the top of the page, and Intelius was mentioned several times by name in the text." 737 F.3d at 1260.

The Ninth Circuit agreed with the district court that even if one assumed that Lee had entered into a contract to purchase the Family Safety Report, he did not enter into a contract to arbitrate. The arbitration clause was contained in the "Terms and Conditions" that Lee would have seen only if he clicked on the hyperlink below "OFFER DETAILS" on the right-hand side of the webpage. "Even an exceptionally careful consumer would not have understood that a purchaser of the Family Safety Report, by clicking the orange button, was agreeing to anything more than the "Offer Details." Id. at 1261.

(i) Defendant Waited Too Long to Compel Arbitration After it Concluded that *Gentry* was no Longer Valid under *Concepcion* – *Ontiveros v. Zamora*, 2013 WL 593403 (E.D.Cal., Feb. 14, 2013) (Slip Opinion)

Plaintiff was formerly employed as an auto mechanic. He brought a putative class action against his former employer and related entities in March 2008 alleging that auto mechanics employed by defendants are paid on a "piece rate system," which leaves them unpaid for time when they are not working on a repair job but are required to be at work. The action was voluntarily stayed for approximately 2-1/2 years for various reasons. The case was reopened in July 2012 and a pretrial scheduling order was then issued in September 2012. Defendant then moved to compel individual arbitration, to strike the class allegations and to stay or dismiss the action. Plaintiff opposed that motion, arguing that defendant had waived its right to compel arbitration because it had waited too long to seek arbitration enforcement and had instead proceeded in court as if they were intent on fully litigating the matter. Plaintiff claimed that defendant's actions were inconsistent with the right to arbitrate and also represented an undue delay.

Defendant responded that, at the time plaintiff's action was filed, it had determined that the California Supreme Court's decision in *Gentry* precluded it from enforcing the arbitration agreement and compelling plaintiff to arbitrate the dispute. Three years later, after the United States Supreme court's opinion in *Concepcion*, defendant concluded that the arbitration agreement was now enforceable. The district

noted that there is a marked split among the California Courts of Appeal with regard to the continuing viability of *Gentry* in light of *Concepcion* – some holding that *Gentry* is no longer good law and others holding that *Gentry* remains binding precedent until a higher court says otherwise – and determined that it was not required to take a position to decide the waiver issue raised in this case. “At this juncture, the court does not take a position on *Gentry*’s continued viability, merely noting the (obvious) point that it is an open question of law.” *7.

The district court reviewed similar cases where defendants had successfully raised the same as defendant was asserting in this case,⁴ but found that “[t]he contrast between the diligence of the defendants in *Quevado*, *Reyes* and *Iskanian*, and that of the defendant herein is notable;” that defendant had not promptly moved to compel arbitration after the *Concepcion* decision was announced (April 2011) and the case was reopened (July 2012); that it simply waited too long after the case was reopened to seek to compel arbitration.

(j) Consumer Arbitration Provision Survives Attack on Unconscionability Grounds – *Vasquez v. Greene Motors, Inc.*, 214 Cal. App. 4th 1172 (1st Dist., Mar. 27, 2013), review granted and opinion superseded 154 Cal. Rptr. 2d 778 (Jun. 6, 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.

⁴ In *Quevado v. Macy’s, Inc.*, 798 F.Supp. 2d 1122 (C.D.Cal. 2011), defendant filed its motion to compel arbitration one month after the *Concepcion* decision was announced. In *Reyes v. Liberman Broad, Inc.*, 208 Cal. App. 4th 1537 (2012), the defendant informed the plaintiff that it intended to move to compel arbitration one month after the *Concepcion* decision was announced. In *Iskanian v. CLS Transp. Los Angeles, LLC*, 206 Cal. App. 4th 949 (2012), the defendant sought to compel arbitration less than three weeks after the *Concepcion* decision was announced.

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. 214 Cal. App. 4th at 1194, 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 held that he had failed to carry his evidentiary burden. *Id.* at 1195.

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 1198.

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 1199.

(k) 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*, 214 Cal. App. 4th 1399 (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 *Samaniego v. Empire Today, LLC*, 205 Cal. App. 4th 1138 (2012) (finding procedural unconscionability on similar grounds) 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 *Samaniego* 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 attacking 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. 214 Cal. App. 4th at 1405.

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 1405-1406." 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. 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 1406. 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.

(l) An Ineffective Rescission Does not Mandate Arbitration Under the Terms of the Prior Agreement, and the Court had Discretion to Decide Entitlement to Rescission in the Context of a Motion to Compel Arbitration – *Little v. Pullman*, 219 Cal. App. 4th 558 (2d Dist., Sep. 9, 2013)

In 2005, William Little and David Pullman entered into an agreement to become 50/50 partners in the purchase of rights to residual income from the Screen Actors Guild for the work of bankrupt and deceased actor Sherman Hemsley (who played George Jefferson in the television show *The Jeffersons*). The deal was that Pullman's company would own the residuals and would pay 50 percent to Little. As part of this agreement, Little and Pullman also agreed to arbitrate any controversy or claim arising out of or relating to any of the transactions or services contemplated in the agreement.

Shortly after entering into the agreement, a dispute arose between Little and Pullman and in July 2005, Little filed suit against Pullman alleging that the agreement was illegal and seeking its rescission. Pullman moved to compel arbitration, but the motion was taken off calendar when developments in the Hemsley bankruptcy intervened. In 2006, Little amended his complaint to seek only dissolution of the joint venture with Pullman, not rescission of the agreement representing the formation of that venture, and Pullman then renewed his motion to compel arbitration. That motion was never heard or decided. In 2007, Little and Pullman entered into a settlement agreement in which they resolved their dispute over the Hemsley residuals. The settlement agreement included an integration clause, which stated that all prior agreements were superseded.

In 2008, despite having relinquished all right, title and interest in and to the Hemsley residuals, Pullman informed the Screen Actors Guild that he was claiming a right to the \$10,000 in Hemsley residuals the Guild was currently holding. Over the course of several communications, Pullman also demanded that the Guild not release the residuals to Little and represented that there was "no settlement whatsoever." Little then filed suit against Pullman for breach of contract and fraud, alleging that Pullman interfered with the Hemsley royalty stream by telling the Guild there was no settlement and that Little had no right to the Hemsley residuals. Pullman responded by filing a motion to compel arbitration, contending that because the settlement agreement tied to a resolution of the parties' disputes concerning the 2005 agreement, the present lawsuit effectively involved a dispute under the 2005 agreement (which contained an arbitration clause). Little opposed this motion on several grounds. The trial court denied Pullman's motion to compel on May 19, 2011, and that ruling was affirmed on

appeal, with the Court of Appeal holding that “[o]nce the Settlement Agreement ended the effectiveness of the Original Agreement’s arbitration provision, the parties had no agreement to arbitrate any disputes at all.... By declining to include arbitration as a provision of their Settlement Agreement . . . they opted *not* to agree that they would resolve future controversies with arbitration.”

Pullman then sent Little a notice of rescission with regard to the settlement agreement, followed by the filing of a cross-complaint seeking rescission of same. Pullman then filed a new motion to compel arbitration based upon the original 2005 agreement, which the trial court denied. Pullman again appealed and the Court of Appeal affirmed, finding that the trial court had correctly determined that the rescission was procedurally ineffective due to lack of tender. The Court of Appeal rejected Pullman’s argument that if he rescinds the settlement agreement, the original 2005 agreement containing the arbitration clause will be automatically reinstated. The Court held that what happens if Pullman effects a unilateral rescission of the settlement agreement is that “an ‘action’ happens next, in the course of which the trial court will determine who should obtain what relief,” including whether the original agreement contains a valid agreement to arbitrate and whether Pullman has waived the right to seek arbitration. 219 Cal. App. 4th at 83-85.

(m) As a Condition to Enforcement of an Arbitration Provision in a Retainer Agreement, Indigent Parties were not Required to Pay Their Share of the Costs Associated with the Arbitration – *Roldan v. Callahan & Blaine*, 219 Cal. App. 4th 87 (4th Dist., Sep. 18, 2013)

A large group of elderly residents in an apartment building filed suit against the owner seeking damages arising out of toxic mold contamination in the apartment building. All of the plaintiffs were “low-income” and relied upon Section 8 housing subsidies to pay for their apartments. Prior to trial, plaintiffs’ attorney associated Callahan & Blaine for their experience in handling complex litigation cases and sent plaintiffs the nine-page retainer agreement required by Callahan & Blaine. The retainer agreement included an arbitration clause on the eighth page and that was the only page in the agreement that did not require a signature or initials. The cover letter from their attorney did not explain or discuss any aspect of the retainer agreement, and did not advise plaintiffs to read it before signing.

After the cases were settled, the plaintiffs sued both sets of counsel alleging that the settlements were inadequate and that they had not been properly represented. Callahan & Blaine successfully moved to compel arbitration based upon the arbitration provision contained on page eight, and the Court of Appeal declined to review that decision when plaintiffs petitioned for a writ of mandate. Plaintiffs then filed a motion in the trial court seeking an order compelling Callahan & Blaine to advance the entire up-front cost of the arbitration forum. In support of this motion, plaintiffs contended that they were indigent and could not afford to share in the substantial expense of the arbitration. That motion was denied and this appeal followed.

The Court of Appeal noted that while there is a presumption that someone who signs or acknowledges a contract has read it, “presuming plaintiffs understood they would have to share in the cost of arbitration is as far as these legal fictions take us.” 219 Cal. App. 4th at 94. The Court found that the arbitration provision was written by the lawyers with no respect for the fact that all litigants deserve their day in court and that the provision “reflects no effort to ensure that clients of limited means would have equal access to the alternative forum it mandates.” Id. at 94-95, citing *Gutierrez v. Autowest, Inc.*, 114 Cal. App. 4th 77 (2003) (consumer contract that mandates arbitration is unconscionable if it conditions access to that process on the consumer posting fees he or she cannot afford to pay).

The Court continued, “If, as plaintiffs contend, they lack the means to share the cost of the arbitration, to rule otherwise might effectively deprive them of access to any forum for resolution of their claims against Callahan. We will not do that. Of course, as the trial court recognized, we cannot order the arbitration forum to *wave its fees*, as a court would do in the case of an indigent litigant. Nor do we have authority to order Callahan to pay plaintiffs’ share of those fees. What we can do, however, is give Callahan a choice: if the trial court determines that any of these plaintiffs is unable to share in the cost of the arbitration, Callahan can elect to either pay that plaintiff’s share of the arbitration and remain in arbitration, or waive its right to arbitrate that plaintiff’s claim.” Id at 96.

The Court of Appeal reversed the trial court’s order denying plaintiffs’ motion and remanded the case with instructions to make specific findings concerning the plaintiffs’ claimed inability to pay the cost associated with arbitration. Specifically, the trial court was instructed to estimate the anticipated cost of the arbitration proceeding previously ordered, and then determine whether any of the plaintiffs were financially able to pay their pro rata share of that cost. If the trial court determined that any plaintiff was unable to do so, it was then instructed to issue an order specifying that Callahan had the option of either paying that plaintiff’s share of the arbitration cost or

waiving its right to arbitrate that plaintiff's case and allowing the case to proceed in the trial court. Finally, if the trial court determined that one or more, but not all, of the plaintiffs were unable to pay their anticipated share of the arbitration costs, and if Callahan & Blaine elected to waive its right to arbitrate those plaintiffs' claims, then the trial court was instructed to further consider whether the policy of avoiding conflicting rulings on common issues of law or facts supported an order requiring all of the plaintiffs' claims to be consolidated for trial in the trial court. Id.

(n) Failure to Attach the AAA Rules Referenced in the Arbitration Provision – Standing Alone – Was Insufficient Grounds to Support a Finding of Procedural Unconscionability – *Peng v. First Republic Bank*, 219 Cal. App. 4th 1462 (1st Dist., Oct. 2, 2013)

Plaintiff began work for First Republic Bank as an assistant manager in 2005. In 2007, the bank became a wholly owned subsidiary of Merrill Lynch & Co. In 2009, Bank of America purchased Merrill Lynch and then sold the bank to private investors. The bank emerged as an independent bank in 2010, prior to which time it made a written offer to plaintiff for employment as an assistant manager with the newly chartered bank. That offer was subject to the plaintiff's agreement to be bound by a number of employment conditions and policies, including an agreement to submit any claims to binding arbitration. When the offer was extended, plaintiff had 25 days to consider it. She accepted it after four days and signed all of the paperwork without expressing any objection or reluctance to any of the stated terms of employment. Plaintiff also did not express any concerns about the arbitration agreement included within the terms of her employment during her employment. Plaintiff's employment was terminated in 2011. Plaintiff then filed suit alleging employment discrimination, wrongful termination and other related claims. The bank moved to compel arbitration, and plaintiff opposed that motion, asserting that the arbitration agreement was unconscionable.

The trial court denied the employer's motion and concluded that the arbitration agreement was "permeated" by unconscionability because it required plaintiff to abide by the AAA rules which were not attached or provided to her. The bank appealed and the Court of Appeal found that the trial court had erred in concluding that the arbitration agreement was unconscionable and thus unenforceable. After engaging in a careful review of the various authorities cited by the parties on this issue, the Court concluded that the failure to attach the AAA rules – standing alone – "is insufficient grounds to support a finding of procedural unconscionability."

(o) **Contractual Right to Compel Arbitration Lost Where Parties Delayed and Engaged in “Tons of Litigation” Before Requesting Arbitration – *Eagan Avenatti LLP v. Stoll*, 2014 WL 793136 (4th Dist., Feb. 28, 2014)**

In 2008, former clients entered into a contingent fee agreement with three law firms to represent them as plaintiffs in a malicious prosecution action. The fee agreement contained an arbitration provision for any dispute arising under the contract. The law firms had a separate fee-sharing agreement, which did not contain an arbitration provision. In May 2011, the malicious prosecution action was settled for \$39 million. A dispute then arose between two of the three law firms concerning the allocation of the contingent fee portion of the settlement proceeds. In June 2011, Eagan Avenatti (“EA”) filed a complaint for declaratory relief, seeking a ruling that Stoll Nussbaum & Polakov (“SNP”) was not entitled to any recovery from the settlement. What happens during the course of 2011 and 2012 is a litany of pleadings, discovery, law and motion, and appellate writs between the two sides. In January 2013, the former clients – represented by EA - filed a motion to compel arbitration. That motion was scheduled for hearing in March 2013, along with seven discovery motions, SNP’s motion for summary judgment and the former clients’ demurrer to SNP’s first amended cross-complaint. The motion to compel arbitration was denied as untimely because it was made “after tons of litigation.” This appeal followed.

At the outset, the Court of Appeal noted that whether a party has waived the right to compel arbitration is a question of fact, to be affirmed if the trial court’s findings are supported by sufficient evidence. *4, citing *St. Agnes Medical Center v. PacificCare of California*, 31 Cal. 4th 1187, 1196 (2003). It also noted that the case before it closely resembled a case it decided in 2010 – *Burton v. Cruise*, 190 Cal. App. 4th 939 (2010) – and quoted at length from that reported decision.

While California law favors arbitration, Code of Civil Procedure section 1281.2(a) provides a statutory exception where the right to compel arbitration has been waived. Waiver does not require a voluntary relinquishment of a known right. “[T]o the contrary, a party may be said to have ‘waived’ its right to arbitrate by untimely demand, even without intending to give up the remedy. In this context, waiver is more like a forfeiture arising from the nonperformance of a required act.” *5, citing *Burton*. Citing *St. Agnes*, the Court noted that the California Supreme Court has cautioned that waiver of the right to arbitration must be examined in the context of each case. Citing *Wagner Construction Co. v. Pacific Mechanical Corp.*, 41 Cal. 4th 19 (2007), the Court noted that the Supreme Court has observed that a party’s unreasonable delay in demanding

or seeking arbitration, in and of itself, may constitute a waiver of the right to arbitrate. “We are loathe to condone conduct by which a [litigant] repeatedly uses the court proceedings for its own purposes ... all the while not breathing a word about the existence of an arbitration agreement, or a desire to pursue arbitration” *Id.*, citing *Adolph v. Coastal Auto Sales, Inc.*, 184 Cal. App. 4th 1443, 1452 (2010).

In final analysis, the Court concluded that substantial evidence supported the trial court’s determination that the former clients had waived their right to arbitrate under the attorney-fee contract; that their delay “was considerably more egregious than that in *Burton*” because the facts demonstrated that for an 18-month period, the parties had engaged in litigation before moving to compel arbitration. “Hardly a month went by without motions being filed, opposed, replied to, or heard and ruled on. On March 7, 2013, the date of the hearing on the petition to compel arbitration, there were 10 other motions on calendar - And for all this time – through trial setting conference, the posting of jury fees, and an answer the former clients never ‘breathed a word’ about arbitration under the attorney-client fee contract.” *6.

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. Cal. Civ. Proc. Code § 1283.4. There are, however, rules governing the award process that have been adopted by various provider organizations.

As a matter of statutory law, the arbitrator is not required to issue formal findings of fact or conclusions of law. *Cothron v. Interinsurance Exchange*, 103 Cal. App. 3d 853, 861 (1980). Likewise, the arbitrator is not required to disclose his or her rationale or reasons for the award. *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).⁵ However, some provider organizations require that the arbitrator issue an award that includes a

⁵ 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.”).

statement of the reasons for the award, unless the parties agree otherwise. See, e.g., JAMS Rules, Rule 24. Other provider organizations give the parties the option of requesting a “reasoned award” as part of the process. See, e.g., American Arbitration Association Commercial Rules, Rule R-42. Beyond what is stated in the arbitrator’s award, parties may not depose the arbitrator to establish and then challenge his or her reasoning. *Hoelt v. MVL Group, Inc.*, 343 F.3d 57, 66-68 (2d Cir. 2003).

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. 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).

In order to enforce an arbitration award, the prevailing party must ask a judge to confirm the award. Cal. Civ. Proc. Code §§ 1285, 1287.4. That request is made by filing a petition with the court. For purposes of creating a record in these court proceedings, the petition must name as respondents all parties to the arbitration. Cal. Civ. Proc. Code § 1285; see *Walter v. National Indem. Co.*, 3 Cal. App. 3d 630, 634 (1970). 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. Cal. Civ. Proc. Code § 1285.4. 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. Cal. Civ. Proc. Code §§ 1290, et seq. 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. 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. 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 (1994). Such relief is sought by petitioning to vacate the award and may be filed by any party. *Baldwin v. Rainey Const. Co.*, supra, 229 Cal. App. 3d at 1058. 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. Generally speaking, an arbitrator's decision is not reviewable for errors of fact or law. *Moncarsh*, supra, 3 Cal. 4th at 6; *City of Palo Alto v. Service Employees Int'l Union*, 77 Cal. App. 4th 327, 333 (1999). 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;⁶ the award was procured by corruption, fraud or other undue means or corruption in any of the arbitrators;⁷ the award was issued by an arbitrator required to disqualify himself or herself;⁸ the rights 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

⁶ 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).

⁷ 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).

⁸ 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 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).

refusal to hear evidence material to the controversy or other misconduct.⁹ 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.¹⁰

For arbitrations governed by the FAA, there are two additional, common law grounds for seeking vacatur of an award, which are quite narrow. 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,¹¹ or where an

⁹ 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).

¹⁰ 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 Sequeros y Reasegueros 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.

¹¹ 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.*

obvious error of law exists.¹² “For an arbitrator’s award to be in manifest disregard of the law, it must be clear from the record that the arbitrator recognized the applicable law and then ignored it” *Matthews v. Nat’l Football League Mgmt. Council*, 688 F.3d 1107, 1115 (9th Cir. 2012). The second additional common law ground is the “arbitrary and capricious” exception, which allows the award to be vacated where no ground for the decision can be inferred from the facts, which is not yet uniformly accepted.¹³

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

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

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).

¹² 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).

¹³ 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).

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,” 552 U.S. at 552, 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. See, *Cable Connection, Inc. v. DirecTV, Inc.*, 44 Cal. 4th 1334, 1354-1355 (2008). 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.” 44 Cal. 4th at 1364.

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 appealable and is subject to the rules and procedures applicable generally to appeals of civil judgments. Cal. Civ. Proc. Code § 1294(d). Likewise, an order denying a petition to confirm the award is appealable. Cal. Civ. Proc. Code § 1294(c); *Ray Wilson Co. v. Anaheim Mem. Hosp. Ass’n*, 166 Cal. App. 3d 1081, 1085 n. 1 (1985). 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 support the award. *Alexander v. Blue Cross of Calif.*, 88 Cal. App. 4th 1082, 1087 (2001); *Pierotti v. Torian*, 81 Cal. App. 4th 17, 24 (2000). 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. *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).

(2) Cases

- (a) **Serious Errors of Law or Fact will not Subject an Arbitrator's Award to Vacatur Under FAA § 10(a)(4) so Long as the Arbitrator Makes a Good Faith Attempt to Interpret a Contract - *Oxford Health Plans LLC v. Sutter*, ___ U.S. ___, 133 S.Ct. 2064 (Jun. 10, 2013)**

Dr. Sutter provided medical services to Oxford Health's insureds under a fee-for-service contract that required binding arbitration of contractual disputes. When Oxford Health failed to pay him fully and promptly for medical services rendered, Dr. Sutter filed a proposed class action in the New Jersey Superior Court. Oxford Health moved to compel arbitration, relying on the following clause in the contract:

"No civil action concerning any dispute arising under this Agreement shall be instituted before any court, and all such disputes shall be submitted to final and binding arbitration in New Jersey, pursuant to the rules of the American Arbitration Association with one arbitrator."

133 S.Ct. at 2067. The state court granted Oxford Health's motion and the matter was referred to arbitration.

In the arbitration, the parties agreed to submit to the arbitrator the issue of whether the parties' contract authorized class arbitration. The arbitrator concluded that it did. Noting that the question turned on "construction of the parties' arbitration agreement," the arbitrator reasoned that the clause sent to arbitration "the same universal class of disputes" that it barred the parties from bringing as civil actions in court; that the intent of the clause was "to vest in the arbitration process everything that is prohibited from the court process." *Id.* The arbitrator further reasoned that a class action "is plainly one of the possible forms of civil action that could be brought in a court" absent the agreement. Accordingly, the arbitrator concluded that "on its face, the arbitration clause ... expresses the parties' intent that class arbitration can be maintained." *Id.*

Oxford Health filed a motion in federal court seeking vacatur of the arbitrator's decision on the ground that he had exceeded his powers under section 10(a)(4) of the Federal Arbitration Act. The District Court denied the motion and the Third Circuit affirmed. 2005 WL 6795061 (D.N.J., Oct. 31, 2005), *aff'd*, 227 Fed.Appx. 135 (2007). The matter was then returned to arbitration.

During the pendency of the arbitration, the Supreme Court decided *Stolt-Nielsen* – holding that an arbitrator may employ class procedures only if the parties have authorized them. 559 U.S. 662, 684. Oxford Health immediately asked the arbitrator to reconsider his decision on class arbitration in light of the *Stolt-Nielsen* decision. The arbitrator issued a new opinion in which he held that *Stolt-Nielsen* had no effect on the case because the agreement at issue authorized class arbitration. Unlike in *Stolt-Nielsen*, the parties in this case disputed the meaning of their contract and submitted that issue to the arbitrator to be decided. The arbitrator had thus been required “to construe the arbitration clause in the ordinary way to glean the parties’ intent.” 133 S.Ct. at 2067. In performing that task, the arbitrator found “that the arbitration clause unambiguously evinced an intention to allow class arbitration.” *Id.* Oxford Health again petitioned the District Court to vacate the arbitrator’s decision under section 10(a)(4) of the Federal Arbitration Act. The District Court again denied the motion and the Third Circuit affirmed, ruling that Oxford Health’s objections to the arbitrator’s rulings were “simply dressed-up arguments that the arbitrator had interpreted its agreement erroneously.” In this regard, the Third Circuit held that so long as the arbitrator “makes a good faith attempt” to interpret a contract, “even serious errors of law or fact will not subject his award to vacatur.”

The Supreme Court granted certiorari to address a circuit split on whether section 10(a)(4) of the Federal Arbitration Act allows a court to vacate an arbitral award in similar circumstances. *Id.* at 2068. The Court started its analysis by noting that Oxford Health was seeking vacatur under section 10(a)(4), and that a party seeking relief under that provision bears a very heavy burden; that it is not enough to show that the arbitrator committed error or even serious error. “Because the parties ‘bargained for the arbitrator’s construction of their agreement,’ an arbitral decision ‘even arguably construing or applying the contract’ must stand, regardless of a court’s view of its (de)merits.” *Id.*, citing *Eastern Associated Coal Corp. v. Mine Workers*, 531 U.S. 57, 21 (2000). The Court concluded that the sole question before it was whether the arbitrator interpreted the parties’ contract, not whether he got its meaning right or wrong. In this regard, the Court noted that it would have faced a different issue if Oxford Health had argued below that the availability of class arbitration was a “question of arbitrability,” which is presumptively for the court to decide. In this context, a court may review an arbitrator’s determination of arbitrability *de novo* absent clear and unmistakable evidence that the parties wanted an arbitrator to decide that issue. *Id.* n. 2, citing *AT&T Technologies, Inc. v. Communications Workers*, 475 U.S. 643, 649 (1986). It also noted that in *Stolt-Nielsen*, the court had made clear that the court “has not yet decided whether the availability of class arbitration is a question of arbitrability. See, 559 U.S. at 680.

On the contract interpretation issue, the court found that the arbitrator's first ruling recited the "question of construction" that parties had submitted to him for decision. To resolve that matter, the arbitrator focused on the arbitration clause's text, analyzing the scope of both what it barred from court and what it sent to arbitration. The arbitrator concluded, based on that textual exegesis, that the clause "on its face ... expresses the parties' intent that class action arbitration can be maintained." When Oxford Health requested reconsideration in light of *Stolt-Nielsen*, the arbitrator explained that his prior decision was "concerned solely with the parties' intent as evidenced by the words of the arbitration clause itself." He then reiterated his conclusion – nothing in the text having changed since the first ruling. Based upon this record, the Court found that it sufficed to show that the arbitrator had not exceeded his powers. *Id.* at 2069.

Oxford Health argued that *Stolt-Nielsen* stood for the proposition that the court could vacate an arbitral decision like the one before the court for misconstruing a contract to approve class proceedings. The Court found that Oxford Health's argument was based upon a misreading of *Stolt-Nielsen*, and stated that the arbitral decision in that case had been vacated because it lacked any contractual basis for ordering class procedures – not because it lacked a "sufficient" one. *Id.* Significantly, in *Stolt-Nielsen*, the parties had stipulated that they had never reached an agreement on class arbitration. Against this factual backdrop, the decision was not based and could not have been based on a determination of the parties' contractual intent because they agreed that they had none on the subject of class arbitration.

(b) Non-Appealability Clause Invalidated – *In re Wal-Mart Wage & Hour Employment Practices Litigation*, 737 F.3d 1262 (9th Cir., Dec. 17, 2013)

After the underlying class action was settled in mediation, the attorneys representing the class had a dispute with Wal-Mart over how to split the fees that Wal-Mart was to pay them. The dispute went to arbitration, where the three law firms were each awarded various sums of money. One firm moved to confirm, one firm moved to vacate and the third firm took no position. The district court found no reason to vacate the award and granted the motion to confirm. The firm whose motion to vacate was denied then took an appeal.

The prevailing firm argued that the appeal was improper because the firms had entered into a non-appealability agreement in the global settlement agreement. That agreement read, in pertinent part:

“Class Counsel agree on behalf of themselves, their clients, and all Class Counsel to submit any disputes concerning fees (including, but not limited to, disputes concerning the fee allocation to any Class Counsel as recommended by Co-Lead Counsel, and disputes between Co-Lead Counsel regarding the determination of appropriate fee allocations) to binding, non-appealable arbitration to the Honorable Layn Phillips within fourteen (14) days of the fee allocations set forth by and/or recommended by Co-Lead Counsel.”

The Ninth Circuit rejected this argument. Noting that the Supreme Court has already clarified that the statutory grounds for judicial review in the FAA are exclusive, and may not be supplemented by contract, the Ninth Circuit ruled that the statutory grounds for vacatur listed in section 10 of the FAA could not be waived or eliminated by contract. 737 F.3d at 1267-1268, citing *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 578; see also *Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 1000 (9th Cir. 2003) (en banc) (“Private parties’ freedom to fashion their own arbitration process has no bearing whatsoever on their inability to amend the statutorily prescribed standards governing federal court review.”). The Ninth Circuit then affirmed the district court’s denial of the motion to vacate.

(c) Appeal Not Available from Order Compelling Arbitration – *MediVas, LLC v. Marubeni Corp.*, 741 F.3d 4 (9th Cir., Jan. 27, 2014)

MediVas is a small biomedical company based in San Diego that specializes in developing new methods for pharmaceutical drug delivery. Marubeni is a Japanese multinational trading corporation. MediVas and Marubeni executed various contracts in connection with a \$5 million loan from Marubeni to MediVas. One of these contracts required the parties to submit contractual disputes to international arbitration venued in Tokyo, Japan, whereas another designated the courts of San Diego as the exclusive forum for such disputes.

After MediVas defaulted on the loan, Marubeni foreclosed on promissory notes held by MediVas and threatened to foreclose on additional MediVas assets. In response, MediVas and several individual plaintiffs filed suit against Marubeni in San Diego Superior Court raising numerous state law claims arising out of this series of transactions. Marubeni removed the action to federal court and then moved to compel arbitration. MediVas opposed arbitration, relying on the forum selection clause, and moved to remand the matter back to state court.

The district court ruled that many of MediVas' claims against Marubeni were subject to the arbitration clause and ordered arbitration of those claims. Because it concluded that federal jurisdiction rested solely on the New York Convention, the court remanded the remaining claims, including all claims brought by the individual plaintiffs, to state court. Neither order explicitly stayed or dismissed the arbitrable claims, and no judgment was entered in the action.

The arbitration panel ruled in favor of Marubeni on all claims save one, which the panel concluded fell outside its jurisdiction. Marubeni then filed a second action in federal district court to confirm the arbitration award. A few days later, MediVas filed a notice of appeal in the original action seeking review of the district court's earlier order granting Marubeni's motion to compel arbitration.

The Ninth Circuit dismissed the appeal finding that while the FAA permits immediate appeals of final decisions with respect to arbitration, an order compelling arbitration does not fall into this category where the underlying action is stayed (versus being dismissed with prejudice). The Court found that the district court's order showed that the arbitrated claims were implicitly stayed pending the conclusion of the arbitration. "[W]e adopt a rebuttable presumption that an order compelling arbitration but not explicitly dismissing the underlying claims stays the action as to those claims pending the completion of the arbitration." Accordingly, the Ninth Circuit found that because the district court's order was not a "'final decision' with respect to an arbitration," it was without jurisdiction to review it. 741 F.3d at 9-10.

(d) Party's Purported Lack of Notice of the Arbitration does not Amount to Misconduct on the Part of the Arbitrator for Purposes of Vacatur Under FAA § 10(a)(3) – *Miss Universe L.P., LLLP v. Monnin*, 952 F. Supp. 2d 591, (S.D.N.Y. Jul. 2, 2013)

This case involves some rather harsh facts and demonstrates just how limited the grounds for vacatur are under the FAA and how literal the FAA will be interpreted and applied.

Sheena Monnin was crowned Miss Pennsylvania and went on to compete in the Miss USA Pageant. Based on a backstage conversation she had with another contestant, Monnin left the competition believing that the finalists and overall "winner" had been pre-selected before the final "voting." Monnin resigned as Miss Pennsylvania and posted her resignation on her Facebook page with a statement about her belief that the

pageant organization was “fraudulent” and “lacking in morals.” She then posted another statement in which she set forth what she witnessed and heard backstage at the Miss USA Pageant. A media frenzy then occurred with Donald Trump squaring off in one corner and Monnin squaring off in the other.

Monnin’s contract with the Miss Universe Organization (“MUO”) provided that in the event of any controversy or claim arising out of or relating to the pageant agreement that could not “be settled through direct discussions,” the parties agreed to attempt to resolve the matter first through mediation and, if that failed, through binding arbitration. Monnin failed to participate in mediation. MUO then filed a demand for arbitration seeking compensatory damages of \$10 million for alleged defamation, breach of contract, etc. Monnin was represented by counsel in the arbitration and the record showed that both Monnin and her counsel had notice of the proceedings and had exchanged significant correspondence with MUO’s attorney. Based upon her attorney’s advice, Monnin did not participate in the arbitration and Monnin failed to appear at the arbitration hearing that took place on November 5, 2012.

The evidentiary hearing proceeded without Monnin, with MUO submitting documentary and testimonial evidence, including an expert witness who testified regarding MUO’s damages. On December 10, 2012, the arbitrator issued his award. The arbitrator found that Monnin had published defamatory statements about MUO on Facebook and on the Today show and concluded that Monnin had made the statements with “actual malice.” With regard to damages, the arbitrator found that MUO had proved that it lost \$5 million due to a new pageant opportunity being lost as a result of the “rigging allegations.” Monnin then petitioned to vacate the award on several grounds, including her purported lack of notice of the arbitration as constituting misconduct on the part of the arbitrator and, in turn, denying her a fundamentally fair hearing.

The district court denied Monnin’s motion, finding that she had misconstrued her purported lack of notice as somehow representing misconduct on the part of the arbitrator. Moreover, the court found that there was extensive evidence that Monnin was directly made aware of the pendency of the arbitration, and her attorney was notified of the arbitration hearing per his instructions that communications be directed only to him and specifically mandating that communications not be sent directly to Monnin. The attorney did not pass the information about the arbitration hearing on to Monnin until after the fact, and then did so with a communication that told her that the arbitration had proceeded without anyone present on her behalf; that the attorney was not licensed to practice law in New York and therefore could not (now) give her advice on the matter. Citing an extensive list of authorities, the court held that “it is well

established that notice to an attorney constitutes notice to the represented client.” 952 F.Supp. 2d at 606. The court concluded that Monnin’s attorney’s failure to communicate properly with Monnin could not be attributed to any flaw in the arbitral proceedings. Id. at 607. In terms of the fairness of the proceedings, the record showed that the arbitrator did not merely enter a default judgment against Monnin for failure to appear but, instead, carefully considered the evidence presented and that relevant law before rendering an arbitration award. Id.

(e) 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.

G. MISCELLANEOUS

- (1) Trial Court Could not Award Interim Contractual Attorney's Fees for Successful Petition to Compel Arbitration – *Roberts v. Packard Packard & Johnson*, 217 Cal. App. 4th 822 (2d Dist., Jul. 3, 2013)**

Packard Packard & Johnson (the "Packard Firm") represented Neal Roberts and Norman Rille in a series of lawsuits they brought on behalf of the United States under the False Claims Act against a number of technology companies. The Packard Firm's contingency fee agreement contained a broad arbitration clause covering any dispute or controversy concerning services rendered by the firm. After several of the FCA cases were settled, a dispute arose between plaintiffs and the Packard Firm when the Packard Firm claimed that plaintiffs had an obligation to reimburse the firm for over \$1.3 million in "unpaid" and "unrecovered" costs out of their share of the settlement recovery and refused to disburse those settlement funds to plaintiffs. Plaintiffs filed suit to force the Packard firm to pay over the \$1.3 million, alleging claims for breach of fiduciary duty, conversion and declaratory relief. The Packard Firm then moved to compel arbitration, which the trial court granted.

The Packard Firm then filed a motion to recover its attorney's fees and costs in bringing the successful motion to compel based upon the attorney's fees clause contained in the fee agreement, which stated: "If any action arising out of this Agreement is institute by any Party against another Party, the prevailing Party shall be entitled to recover from the non-prevailing Party reasonable attorneys' fees and costs." In opposition, plaintiffs argued that the motion to compel was not an "action" because it was filed in the existing lawsuit and that the trial court could not determine which party, if any, was the prevailing party until after the arbitrator had determined the merits of the claims asserted. The trial court determined that "on balance the movants have the better of it," and awarded the Packard Firm its fees and costs in bringing the motion to compel arbitration. Plaintiffs appealed.

The Court of Appeal reversed, noting that [p]rocedural steps taken during pending litigation are not an 'action' within the meaning of section 1717. 217 Cal. App. 4th at 832. The case includes an extensive discussion of various cases in which

attorney's fees were and were not awarded for "actions" taking during litigation. Ultimately, the court concluded that a motion to compel was not an "action" for which the prevailing party could recover its fees and costs because, when such a motion is granted, the proceedings are not terminated. "The underlying causes of action must still be heard by an arbitrator. Consequently, in ruling on the petition to compel arbitration, the trial court cannot yet determine which party, if any, 'recovered a greater relief in the action on the contract.'" *Id.* at 833, citing, *Westamerica Bank v. MBG Industries, Inc.*, 158 Cal. App. 4th 109, 134 (2007) and *Salaway v. Ocean Towers Housing Corp.*, 121 Cal. App. 4th 664, 673 (2004).

(2) Motion to Compel Arbitration of Dispute Between Trust Beneficiary and Trustee-Beneficiary Denied Because There was no Evidence that the Beneficiaries of the Trust Gave Either Their Consent to or Consideration for the Arbitration Provision – *McArthur v. McArthur*, ___ Cal. App. 4th ___, 2014 WL 939789 (1st Dist., Mar. 11, 2014)

In *Diaz v. Bukey*, 195 Cal. App. 4th 315 (2011), the Court of Appeal for the Second District held that the trust beneficiary was not required to submit disputes with the trustee concerning administration of the trust to arbitration because, while the trust instrument contained an arbitration provision, the trustee did not establish the existence of a contract binding the beneficiary to participate in arbitration. On August 10, 2011, the California Supreme Court granted review (Case No. S194150), but then deferred action in the matter "pending consideration and disposition of a related issue in *Pinnacle Museum Tower Ass'n v. Pinnacle Market Development* (then pending before the Court as Case No. S186149). On August 16, 2012, the Supreme Court issued its decision in the *Pinnacle* case, in which it enforced an arbitration provision contained in CC&R's against non-signatory members of a condominium association. 55 Cal. 4th 223 (2012). Thereafter, in the *Diaz* case, the Supreme Court transferred the cause back to the Court of Appeal with directions to vacate its decision and to reconsider the cause in light of the *Pinnacle* decision. The parties in the *Diaz* case then stipulated and requested dismissal of the appeal, which was granted on December 5, 2012. This set of circumstances caused one commentator to remark that on the issue of whether trust beneficiaries can be required to arbitrate based on the inclusion of an arbitration provision in the trust instrument (to which they are not signatories): "We will now never know what the Court of Appeal would have done, but its original decision is no longer good law." Richard J. Collier, "So – Can Trust Beneficiaries be Required to Arbitrate?" Cooper Alerts (Dec. 13, 2012), www.cwlaw.com/publications/alertDetail.aspx?id=679.

In *McArthur v. McArthur*, decided by the Court of Appeal for the First Circuit on March 11, 2014, we now have a post-*Pinnacle* decision on the enforceability of arbitration provisions contained in trust instruments to which the beneficiaries are not signatories, and that decision agrees with the analysis offered by Richard J. Collier in December 2012 as to why the *Pinnacle* holding should not apply to the enforcement of arbitration provisions against non-signatories in the context of wills and trusts disputes. The following is a discussion of the *McArthur* case and holding.

In 2001, Frances McArthur created an inter vivos trust naming her three daughters – Deborah, Kristi and Pamela – as coequal beneficiaries. In 2011, Frances amended the trust instrument to allocate a greater portion of the trust property to Kristi and add a provision requiring arbitration of disputes. After Frances’s death, Pamela sued Kristi, alleging financial elder abuse and claiming that the 2011 amendment was invalid due to Kristi’s undue influence and Frances’s lack of testamentary capacity. Kristi moved to compel arbitration of Pamela’s claims under the terms of the 2011 trust amendment. The trial court denied the motion because Pamela was not a signatory to the arbitration agreement. Kristi appealed and the Court of Appeal affirmed.

The Court of Appeal viewed its job in deciding the issues raised on appeal as that of completing “the assignment originally given by the Supreme Court to our colleagues in *Diaz v. Bukey*” to consider the enforceability of an arbitration clause included in a trust instrument against non-signatory beneficiaries. *5. The Court of Appeal agreed with the trial court that *Pinnacle* “is materially distinguishable.” *Id.* In so ruling, the court noted that the agreement in *Pinnacle* was a recorded declaration establishing a common interest development and governing its operation subject to an extensive statutory scheme which, among other things, establishes that the terms of the recorded CC&R’s are “enforceable equitable servitudes, unless unreasonable, and shall inure to the benefit of and bind all owners of the separate interests in the development.” 55 Cal. 4th at 238-239, citing Cal. Civ. Code [former] § 1354(a). That same statutory scheme provides “various protections to help ensure that condominium purchasers know what they are buying into.” *Id.* Critically, in the *Pinnacle* decision, the Supreme Court stated: “In light of the foregoing, it is no surprise that courts have described recorded declarations as contracts,” *Id.* at 240, thus conforming to California Arbitration Act’s treatment of arbitration as a creature of contract. See, Cal. Code Civ. Proc. § 1281. In the *McArthur* case, the Court of Appeal found that “there is no similar statutory scheme that would require that a trust beneficiary be bound by an arbitration clause in a trust instrument,” specifically noting that unlike probate statutes in other states, “our Probate Code contains no specific legislative authorization for predispute trust arbitration provisions, despite otherwise establishing specific remedies and procedures for trust

beneficiaries.” *6. The court thus concluded that the doctrine of delegated authority to consent articulated in *Pinnacle* was inapplicable in the context of a trust. *Id.*

On appeal, Kristi also argued that California courts have characterized trusts as contracts between settlers and trustees, and contends that because the trusts are formed for the benefit of the trust beneficiaries they should be enforceable against non-signatory beneficiaries as with other third-party beneficiary contracts. The Court of Appeal rejected this argument because “the case law in fact requires that the third party *claim* benefits or rights under the contract before he or she will be bound to arbitrate.”

*6. In this case, Pamela had not accepted benefits under the 2011 trust and had not attempted to enforce rights under the amended trust instrument. Instead, Pamela claimed that the 2011 trust was invalid and was seeking to have it set aside.

(3) Court Does not Lack Authority to Award Interest on an Arbitration Award Where the Award is Silent – *Lagstein v. Certain Underwriters at Lloyd’s of London*, 725 F.3d 1050 (9th Cir. Aug. 5, 2013)

After undergoing major heart surgery in 2001, Dr. Lagstein made a claim on a disability policy he had purchased from Lloyd’s of London. After several years, Lloyd’s finally denied the claim, and Dr. Lagstein filed suit in federal district court. Lloyd’s then moved to compel arbitration pursuant to the arbitration clause contained in the insurance policy and that motion was granted. The resulting arbitration was “wildly successful” for Dr. Lagstein who was awarded over \$6 million in damages. Unhappy with the result, Lloyd’s moved the district court for vacatur and that motion was granted. Dr. Lagstein appealed, and the Ninth Circuit reversed and remanded with instructions to confirm that arbitration award. 607 F.3d 634 (9th Cir. 2010).¹⁴ The district court did as it was instructed, but denied Dr. Lagstein’s request for interest and fees. This appeal followed and the Ninth Circuit reversed.

The award at issue included interest on the contract damages portion of the award, but was silent as to interest on the non-contract damages – specifically, the \$4 million awarded in punitive damages. As a threshold issue, the Ninth Circuit held that the fact that the arbitrators had awarded interest on the contract damages portion of the

¹⁴ In the earlier proceedings, Lloyd’s moved the district court to vacate the arbitration award on several grounds, including arbitrator disqualification for failure to make required disclosures. The district court vacated the award as requested and the Ninth Circuit reversed and remanded with instructions. The portion of the decision dealing with arbitrator disclosures is discussed in Section I(A)(1), above.

award did not foreclose the district court from awarding interest on the remaining portions of the award; that courts do not lack authority to award interest where an arbitration award is silent. “While the arbitrators’ explicit award of interest on the contract damages should be respected, their failure to speak on interest otherwise does not constitute a denial of interest on the other parts of the award. . . . Once the arbitration panel set the amount of punitive damages, Lloyd’s could not delay payment so as ‘to make money during the [confirmation] process on what has been ordered to be paid to the plaintiff.’” (Citations omitted.)

(4) Effective November 1, 2013, the American Arbitration Association’s Optional Appellate Arbitration Rules Become Effective

Alternative dispute resolution provisions in contracts commonly provide for final and binding arbitration of all disputes arising between the parties. Very often parties designate the American Arbitration Association (AAA) as the forum in which disputes will be heard and determined, and specify AAA rules for commercial and other types of disputes to control the process. The parties’ objective in arbitration is a fair, efficient and economical outcome and, in particular kinds of cases, a result determined by an expert in the particular field of dispute. In exchange for expediency and control over designating the process and the decision maker, the parties give up the right to appellate review in the courts. Barring grounds for vacatur (which are quite limited), the arbitrator’s award is final and binding and may be enforced with the same force and effect as a judgment.

The benefits of arbitration are offset by one major drawback: namely, there is almost no way to overcome an aberrant decision by the arbitrator. Even when the arbitrator applies the wrong law or plainly mistakes the facts, courts will rarely disturb the award. To address this concern, the AAA has created new, optional appellate rules to provide an expedited and complete review of the arbitration decision – albeit, in the arbitral forum and not the courts.

The *AAA Optional Appellate Arbitration Rules*, effective November 1, 2013, allow parties to include, as part of their contractual arbitration provisions, a further provision that the decision of arbitrators may be appealed to a newly established AAA Appeal Tribunal which, specifically, may review those decisions based upon alleged errors of law that are materials and prejudicial to a party, and determinations of fact that are “clearly erroneous.” The Appeal Tribunal is comprised of arbitrators selected from a AAA “appellate panel,” and may affirm or reverse the underlying arbitration decision. The decision of the Appeal Tribunal is the final decision in the case.

As compared to appellate review in the court system, where appeal of a final decision is a matter of right, appeal to the AAA Appeal Tribunal is only available by agreement of the parties. Just as arbitration is a matter of contract between the parties, so too is appeal to the AAA Appeal Tribunal.

The ability of the Appeal Tribunal to address “material and prejudicial” errors of law, and “clearly erroneous” fact determinations by the original arbitrator/arbitration panel is the central feature of the new AAA appeal procedures. For this to happen, however, a sufficient record on appeal must exist, which means planning at the time of the evidentiary hearing to “make the record on appeal.” The Appeal Tribunal will not rehear the case. Like the appellate court, the Appeal Tribunal reviews the record of what transpired in the hearing on the merits. So, clearly, a “record” of the arbitration must exist in the form of hearing transcripts, documentary evidence, written argument in the form of trial and pocket briefs, and other materials admitted in the original proceeding.

Key aspects of the AAA optional appeal procedures include the following:

- The appeal must be initiated within 30 days of the underlying award through a notice of appeal which specifies the errors alleged.
- Any cross-appeal must be filed within 7 days of the notice of appeal.
- The appeal will be heard and determined by an “Appeal Tribunal” comprised of three arbitrators that the parties may themselves appoint or which, the AAA will appoint based upon a selection procedure by which the parties may strike and rank arbitrators on a list chosen by the AAA from its “Appellate Panel.”
- The Appeal Tribunal will be comprised of three arbitrators unless the parties agree that the appeal may be heard by a single arbitrator.
- The record on appeal is compiled by the parties and may include transcripts of the arbitration hearing, briefs provided to the arbitrator, and all relevant evidence presented at the arbitration hearing.

- The appeal will be determined on the basis of the record and the appellate briefs submitted by the parties in accordance with a schedule and page limits established by the rules of the Appeal Tribunal. There will be no oral argument unless requested by the parties and permitted by the Appeal Tribunal.
- Unless agreed otherwise by the parties, the initial brief is due 21 days after service of the notice of appeal; the answer brief is due 21 days following service of the initial brief; and the reply brief is due 10 days after service of the answer brief. If oral argument is requested and approved, it shall take place within 30 days of the last brief filed.
- The Appeal Tribunal must provide its decision within 30 days of the last brief or oral argument.
- The Appeal Tribunal may adopt the underlying award, substitute its own award, or request additional information from the parties. The Appeal Tribunal may not order a new arbitrator or remand the matter to the original arbitrator for further proceedings. *Functus officio* still applies and controls. [*Functus officio* is a Latin term meaning “having performed his or her office.” With regard to the office of arbitrator, it means without further authority or legal competence once the duties and functions of the original commission have been fully accomplished.]
- The party seeking appellate review must pay a non-refundable \$6,000 administrative fee. This fee does not include the fees of the arbitrators or the cost of the hearing facilities.

NOTE: Appellate review within the arbitral forum is not new. Many ADR providers offer an appeals process and JAMS created its appellate procedure rules 10 years ago. Fueling this development of appellate review within the arbitral forum is the United States Supreme Court’s decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008) where the Court held that parties may not, by contract, expand on the statutory grounds for challenging arbitral awards.

(5) Punitive Damages Awarded in Arbitration are not Subject to Judicial Review Even When No Evidence was Presented on the Defendant's Net Worth – *American State University v. Kiemm*, 2013 WL 1793931 (2nd Dist., Apr. 29, 2013) (Not Reported)

Plaintiffs filed a complaint against the Kiemms and others concerning the 2010 purchase of shares of stock of American State University. In addition to their breach of contract claims, plaintiffs asserted several intentional tort claims, including trade libel, fraud, and conversion. One of the Kiemms' co-defendants moved to compel arbitration and that motion was granted. At the conclusion of the arbitration proceeding, the arbitrator found in favor of the plaintiffs and awarded \$900,000 in compensatory damages, \$500,000 in punitive damages and \$50,000 in attorney fees. When plaintiffs petitioned to confirm the arbitration award, the Kiemms responded by filing a petition to vacate on several grounds, including the contention that the arbitrator's punitive damages award was erroneous because no evidence was presented on the Kiemms' net worth, which was only \$400,000. The trial court confirmed the award and judgment was entered in favor of plaintiffs. The Kiemms appealed.

On appeal, the Kiemms claimed that the arbitrator's award should be vacated on several grounds, including the failure of the arbitrator to take evidence as to the Kiemms' net worth before making a determination as to the amount of the punitive damages awarded. The Court of Appeal rejected the Kiemms' argument, stated that "with respect to the punitive damages issue, judicial review of a punitive damages award is not available in arbitration." *3, citing, *Shahinian v. Cedars-Sinai Medical Center*, 194 Cal. App. 4th 987, 1007-1008 (2011); *Rifkind & Sterling, Inc. v. Rifkind*, 28 Cal. App. 4th 1282, 1291 (1994). In this regard, the Court noted that the rationale for this rule "is that punitive damages awards in judicial proceedings are limited by the due process clause of the Fourteenth Amendment ... which limits state action But, private arbitration, which occurs by voluntary agreement, does not involve state action." *Id.* (citations omitted). The judgment entered on the arbitrator's award was affirmed in all regards.

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. 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). 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 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

As a matter of federal common law, the Supreme Court has emphasized that testimonial privileges are not favored.

“The common-law principles underlying the recognition of testimonial privileges can be stated simply. ‘For more than three centuries it has now been recognized as a fundamental maxim that the public . . . has a right to every man’s evidence.. When we come to examine the various claims of exemption, we start with the primary assumption that there is a general duty to give what testimony one is capable of giving,

and that any exemptions which may exist are distinctly exceptional, being so many derogations from a positive general rule.”

Jaffee v. Redmond, 518 U.S. 1, 9 (1923), citing *United States v. Bryan*, 339 U.S. 323, 331 (1950). So, 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,” *Josephs v. Pac. Bell*, 443 F.3d 1050, 1064 (9th Cir. 2006), 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. *Molina v. Lexmark Int’l, Inc.*, No. CV 08-04796 MMM (FMx), 2008 WL 4447678, at *11-12 (C.D. Cal. Sept. 30, 2008).

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.¹⁵ 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 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

¹⁵ 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).

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. 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.”). Numerous district court decisions have used the settlement letter to establish the amount in controversy.¹⁶

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 law¹⁷ and may not be augmented by local court rules.¹⁸ In diversity

¹⁶ 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).

¹⁷ *Id.* See also *Religious Tech. Ctr. v. Wollersheim*, 971 F.2d 364, 367, n.10 (9th Cir. 1992).

¹⁸ 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

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. 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)).

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.¹⁹ That being said, the Ninth Circuit has also held that “[i]n determining the federal law of privilege in a federal question case, absent a controlling statute, a federal court may consider state privilege law.” See, *Lewis v. United States*, 517 F.2d 236, 237 (9th Cir. 1975) (citations omitted).

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 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.

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.*

¹⁹ *Id.* at n.10 (court refused to apply California litigation privilege in copyright action with pendent state law claims); *Folb v. Motion Picture 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).

(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), amended 705 F.3d 919 (9th Cir., Jan. 14, 2013)**

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,²⁰ 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.

²⁰ 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) Plaintiff's Counsel Denied Fees for Time Spent Litigating Defendants' Motion Because He "Knowingly and Repeatedly" Disclosed Confidential Mediation Communications in Violation of the Court's Local Rules – *Jones v. Metropolitan Life Ins. Co.*, 845 F.Supp. 2d 1016 (N.D.Cal., Feb. 24, 2013)

Jones is an ERISA case. At issue was Plaintiff's request for attorney fees. Plaintiff requested an award of nearly \$375,000.00. The court cut the request by 49%, awarding only \$191,290.50. Among the cuts the court made was the disallowance of fees that related to Plaintiff's counsel's violation of the court's local rules regarding the confidentiality of mediation materials and proceedings. Plaintiff's counsel repeatedly violated those rules by fling documents with the court which included evidence of those materials and proceedings. Defendant's counsel objected to and moved to strike the evidence, which Plaintiff's counsel opposed. The court disallowed Plaintiff's fees in unsuccessfully opposing the motions to strike the confidential information, holding that those oppositions were unreasonable and unnecessary. The opinion also addresses several other reasons why the fee request was cut so severely. It's worth reading this cautionary tale for those discussions as well.

(iii) Trial Court Grants Ex Parte Application to Allow Evidence of the Identification of Parties Who Attended a Mediation as not Being Confidential Information "Relating to the Subject Matter of the Case in Mediation" – *Neighborhood Assistance Corporation of America v. First One Lending Corporation*, 2013 WL 327478 (C.D.Cal., Jan. 29, 2013)

Neighborhood Assistance Corporation of America ("NACA") is a national non-profit corporation that offers free assistance to homeowners seeking housing counseling and mortgage-related services. NACA sued First One Lending and several individual defendants (John Vescera, Bill Mariner and Randa El-Farra) for illegally misleading homeowners into believing that First One was affiliated with NACA and then charging homeowners fees for services that NACA provides at no charge. Plaintiff requested and was granted a preliminary injunction freezing the assets of First One and John Vescera. That application included evidence that Vescera had introduced forged or false declarations from Mariner that suggested Mariner, not Vescera, was the head of First

One Lending. Vescera and First One filed an *ex parte* application for an order allowing them to introduce evidence that at an early mediation in the case, Mariner had introduced himself to Plaintiff and Plaintiff's counsel, as the "Vice President of Operations" for First One. Defendants argued that this evidence was relevant to plaintiff's claim that Vescera and First One had misrepresented Mariner's position at the company, and called into question Mariner's later depositions and declarations in which he denied having made declarations in support of defendants' initial motion to dismiss.

On the issue of confidentiality, defendants argued that Local Rule 16-15.8 treated as confidential anything that happened or was said pursuant to a mediation "relating to the subject matter of the case in mediation," and that the participants identifies and how they introduced themselves was not that. Plaintiff argued that confidentiality protection extended to any statement made during a mediation. The trial court agreed with defendants and granted the *ex parte* application to allow evidence of Mariner's alleged introduction as "Vice President of Operations," but specifically stating that "[n]othing in the Order may be construed as allowing any party to disclose any 'confidential information' related to mediation" and instructing defendants to "take care to limit their evidentiary submissions to the very narrowly defined subject of Mariner's alleged introduction." *3.

UPDATE: Judge David O. Carter granted Plaintiff's request for a preliminary injunction freezing Vescera's and First One's assets. The order made no mention of Mariner or his role with the company. Shortly thereafter, the case settled.

(iv) Report Prepared for Use in a Consensual Mediation Excluded as a Sanction, but not Because of Mediation Confidentiality – *Bradford Technologies, Inc. v. NCV Software.com*, 2013 WL 4033840 (N.D.Cal., Aug. 6, 2013)

This case is primarily notable for the parties' and court's blithe disregard for the confidentiality of mediation proceedings.

Bradford sued NCV on various causes of action based upon the central allegation that NCV had pirated Bradford's source code. After the lawsuit was filed, the parties' counsel negotiated a stipulated protective order in preparation for mediation, which order was approved by the court. Under the terms of the protective order, the parties themselves were not supposed to look at or manipulate one another's source codes.

Pursuant to the protective order, the parties exchanged their source codes so they could be analyzed by experts to see if they had any similarities. At the mediation, the parties were then going to exchange their respective expert reports.

Plaintiff did not hire an outside expert and, instead, plaintiff's president (Jeff Bradford) analyzed defendant's source code himself. The discs containing defendant's source code were in zip files that were password protected. The only way Bradford could open those files was by his attorney providing him with the password. These actions were, of course, in violation of the protective order.

Prior to the mediation, Bradford asked one of its officers (Mark Linne) to put together a document comparing the user interface elements of Bradford's and NCV's applications for use at the mediation. Linne created a PowerPoint that compared screenshots of the two applications. Linne did not have access to defendant's source code, and had no training in source code, but after the mediation Linne tendered his resignation to plaintiff and then wiped the hard drive on his laptop (thereby eliminating the PowerPoint file).

It was at the mediation that defendants learned that the protective order stipulation had been violated by plaintiff's attorney delivering the highly confidential discs to Bradford and giving him the password to open the zip files on the discs, and by Bradford reviewing and analyzing defendant's source code and copying the information on the discs onto his personal laptop computer. After various motions and discovery related to plaintiff's violation of the protective order, defendants' moved to terminating sanctions. The court was troubled by the unavailability of Linne's computer and its history. As part of the sanction order meted out by the court, she prohibited Plaintiff from using Linne's report in any subsequent hearings or trial. This part of the ruling is curious because Linne's report apparently no longer existed, and also because it might arguably be protected by the privilege for confidential mediation documents. From the decision, it appears that neither the parties nor the court addressed the issue of mediation confidentiality concerning Linne's report or use of the information defendants' acquired during the mediation concerning Bradford's actions.

(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.” Cal. C. Civ. Proc. § 1775(a). 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.” Cal. C. Civ. Proc. § 1775(c). 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. *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.” Cal. Evid. C. § 1115(c). 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.” Cal. Evid. C. § 1115(a). 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. *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.” 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 (Cal. Evid. C. § 1119(a)); (b) any writing prepared for the purpose of, in the course of, or pursuant to, a

mediation or mediation consultation (Cal. Evid. C. § 1119(b)); and (c) all “communications, negotiations, or settlement discussions” by and between participants in the course of a mediation or mediation consultation (Cal. Evid. C. § 1119(c)). 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 protection intended by the statute is unqualified, clear and absolute, and is not subject to judicially crafted exceptions or limitations. 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); *Simmons v. Ghaderi*, 44 Cal. 4th 570, 588 (2008); *Cassel v. Superior Court*, 51 Cal. 4th 113, 124 (2011). 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.

Absent 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.” Cal. Evid. Code § 1125(a)(5). Where the parties convene a mediation and commence settlement negotiations in that environment, their post-mediation negotiations will be protected for the ten-day period following the mediation. See, *Rodriquez v. United Nat’l Ins. Co.*, 2012 WL 541512 (2012) (when a mediation ends is defined by statute and does not occur when one party walks out of the mediation).

(b) Cases

**(i) Once Confidential, Always Confidential –
Castaneda v. Dept. of Corrections &
Rehabilitation, 212 Cal. App. 4th 1051 (2nd
Dist., Jan. 15, 2013)**

Francisco Castaneda was in State custody after being convicted of illegal possession of a controlled substance with intent to sell. During his incarceration, he complained of pain and various health problems. Castaneda died from complications from cancer which allegedly was not properly diagnosed or treated while he was a prisoner of the state. Before he died, Castaneda presented a timely government tort claims and after it was rejected, filed suit against the California Department of Corrections and Rehabilitation (CDCR) for violation of the statutory duty to summon medical care for a prisoner. He died before the matter could proceed to trial. Sixteen months later, Castaneda’s sister was substituted in on behalf of Castaneda’s estate with

respect to the survivor action. Castenada's daughter was the beneficiary of his estate. The complaint was then amended to allege a new, separate cause of action for wrongful death. A government tort claim was never filed concerning this claim.

The State moved for judgment on the pleadings on the grounds that both Castenada's estate and his daughter had failed to comply with the government tort claims act and, as a result, they were barred from bringing suit against the State. Plaintiffs argued that the State was barred by the doctrine of estoppel from raising the failure to comply with the Act. The trial court agreed with plaintiffs and allowed their amendments to the complaint and denied the State's motion for judgment on the pleadings. The matter proceeded to trial, after which the jury returned a verdict in favor of the Castenada's estate and daughter in the amounts of \$234,557 and \$1.5 million, respectively. The CDCR appealed.

In denying the State's motion for judgment on the pleadings, the court based its ruling on the State's "affirmative conduct" in the subject litigation and a related federal court proceeding, which estopped it to assert noncompliance with the Act. Among the "conduct" cited by the trial court were discussions had in an early mediation which included discussion about the daughter's wrongful death cause of action and the State's failure to raise the issue of noncompliance for over a year after the expiration of the time to present a late claim. The trial court ruled that through the mediation discussions, the State was on notice of the claim and would suffer no prejudice from the amendment of the complaint to add the wrongful death claim.

On appeal, the Court of Appeal reversed the trial court's ruling allowing the amendment and reversed the judgment for Castenada's daughter on the wrongful death claim, noting that it was surprised that the trial court based estoppels on statements made, or discussions had, during mediation. Citing *Simmons v. Ghaderi*, 44 Cal. 4th 570, 580 (2008), the Court held that statements made during mediation are confidential not only during the mediation, but also after the mediation ends. "[T]he conduct cited by the trial court does not amount to any affirmative acts designed to induce Vinessa to refrain from complying with a condition precedent to filing suit." 212 Cal. App. 4th at 1064.

**(ii) So Much for Mediation Confidentiality!
Breach of Mediation Confidentiality Leads
Court to Quote from Confidential Mediation
Brief to Support its Findings – *Limandri v.
Wildman Harrold Allen & Dixon*, 2013 WL
2451322 (2nd Dist., Jun. 6, 2013) (Not
Reported)**

Charles LiMandri represented former Miss California USA Carrie Prejean in her litigation arising out of the 2009 Miss USA Pageant. Prejean was first runner-up and sued various pageant related parties alleging that she was discriminated against because of an answer she gave regarding legalization of same sex marriage. In the course of that litigation, the parties participated in a mediation in New York. During the mediation, attorneys for one of the defendants showed sexually explicit pictures and a video of Prejean to the Mediator, LiMandri, Prejean, and her mother. The point of the demonstration was to give Prejean a little taste of the public embarrassment she would suffer if she did not settle in defendants' bid to discredit and impeach her as an espoused "conservative Christian" with strong family values. Prior to attending the mediation, Prejean was unaware of defendants' possession of the video and, accordingly, was demanding millions of dollars in damages. Shortly after the video was revealed during the mediation, a settlement was achieved for approximately \$100,000. The settlement included a confidentiality clause and required all parties and counsel to destroy all copies of the photos and video, and to keep all aspects of the mediation and settlement confidential.

The attorney who had shown the photos and video at the mediation allegedly breached the settlement agreement by leaking information about the photos, video and settlement agreement to the media in violation of the confidentiality provisions. LiMandri sued for breach of contract, among other claims. Defendants filed Anti-SLAPP motions which the trial court denied, except as against LiMandri's claim for fraudulent inducement. The appellate court affirmed.

The appellate court agreed with the trial court that by signing the confidentiality provisions of the settlement agreement, the parties gave up their first amendment rights to talk about the settlement after the lawsuit was over. Therefore, the Anti-SLAPP statute would not protect them. Because the fraudulent inducement claim involved pre-dismissal communications, they were protected by the litigation privilege, Civil Code §47(b).

Although the court makes reference to the mediation confidentiality agreement signed by the parties prior to the mediation, and California Evidence Code §1126, which provides that confidential information introduced in a mediation remains confidential afterward, neither of these appear to form the basis for the decision. Rather than upholding the mediation privilege, the appellate court even quotes from the defendants' mediation brief. The court uses the quote to show how the post-settlement statements made by defendants' counsel actually followed through on threats described in the brief, namely that Prejean would be exposed as a hypocrite, and not as the pure and devoted Christian that she portrayed herself to be. Nevertheless, LiMandri was allowed to pursue his claims based on alleged violations of the confidentiality provisions of the settlement agreement itself.

**(iii) Asserting the Mediation Privilege Did Not
Deny Defendant a Fair Trial – *Kurtin v. Elieff*,
215 Cal. App. 4th 455 (4th Dist., May 8, 2013)**

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. A very complicated and protracted set of court and arbitration proceedings then ensued, with a jury returning a verdict in favor of Kurtin in May 2010.

A number of terms of the 2005 settlement agreement were relevant to the determination of the issues raised in the litigation. At trial, Elieff contended that those terms were ambiguous, and 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; that he should have been allowed to present evidence otherwise precluded by the mediation privilege to defend himself or Kurtin should have been required to drop his claims.

The Court of Appeal rejected Elieff's argument and held that Kurtin's invocation of the mediation privilege did not deny Elieff a fair trial. In so holding, the Court noted that the Supreme Court "has clearly signaled the policy behind the mediation privilege is so strong that California law is willing to countenance the 'high price' of the loss of relevant evidence to protect the privilege." 215 Cal. App. 4th at 470, citing *Cassel v. Superior Court*, 51 Cal. 4th 113, 138 (2011). Elieff attempted to distinguish his situation from *Cassel* by arguing that the application of the mediation privilege was limited to the particularly circumstances of that case: namely, a *plaintiff* trying to present/substantiate a claim (versus a defendant needing evidence to defend against a breach of contract claim where the contract at issue was formed in a mediation). The Court of Appeal rejected Elieff's argument, finding that there was no meaningful difference between plaintiffs and defendants in the mediation privilege situation; that "differentiating between them makes no sense. Looking at its decision in *Provost v. Regents of University of California*, 201 Cal. App. 4th 1289 (2011), where the Court of Appeal rejected the claim of a party seeking to disavow a stipulated settlement arrived at through mediation through alleged coercion from threats of criminal prosecution by the other party, the Court reasoned that "[a]s with *Provost*, if the Legislature is willing to allow even unfair mediated agreements to stand as a result of mediation confidentiality, it certainly is willing to stomach whatever incidental unfairness might result from a party's inability to use mediation evidence to explain allegedly ambiguous terms within a mediated agreement." *Id.* at 478.

(iv) Marital Settlement Agreements Produced as a Result of Mediation Cannot be Presumed to be the Product of Undue Influence – *In re Marriage of Woolsey*, 22 Cal. App. 4th 881 (3d Dist., Oct. 22, 2013)

Clark and Anna Woolsey agreed to participate in a church-sponsored reconciliation session that turned into a mediation. The result of the mediation session was a marital settlement agreement ("MSA") that divided the parties' community property and resolved legal and physical custody of the children, as well as visitation and support. When Anna moved to have the MSA entered as a judgment pursuant to

C.C.P. Section 664.6, Clark objected on various grounds. He argued that the MSA did not comply with the local rules. He argued that it could not become the final judgment of the court because the parties had not exchanged necessary financial disclosures, and he argued that the property split was unequal and the result of undue influence exerted during the mediation session. In the trial court, Clark argued that the mediator exerted undue influence. On appeal, Clark argued that Anna exerted undue influence during the course of the mediation that resulted in her obtaining an unfair division of the marital property. Both the trial court and the appellate court concluded that the mediation confidentiality provisions of the California Evidence Code precluded Clark from setting the MSA aside based on his claims of undue influence.

Clark did not attempt to introduce direct evidence of anything the mediator or Anna said or did during the mediation session to support his claim. He even acknowledged that all such material was privileged and should not be admitted into evidence. Instead, he relied on case law that holds that “[w]hen an interspousal transaction advantages one spouse, “[t]he law, from considerations of public policy, presumes such transactions to have been induced by undue influence.” 220 Cal. App. 4th at 901, quoting *In re Marriage of Haines*, 33 Cal. App. 4th 277, 293 (1995). The Court of Appeal rejected this argument, noting that it had previously held that marital settlement agreements produced as a result of mediation cannot be presumed to be the product of undue influence. See, *In re Marriage of Kieturakis*, 138 Cal. App. 4th 56 (2006). Quoting from its decision *Kieturakis*, the court stated, “Voluntary participation and self-determination are fundamental principles of mediation It can thus be expected that most mediators would ... consider it their duty to attempt to determine whether the parties are ‘acting under their own free will’ in the mediation.... ‘[P]ower imbalance[s] between spouses’ are a recognized concern when family matters are mediated.... Therefore, ‘[d]ivorce mediators generally work to balance the negotiating power between the parties. This tends to produce agreements that are more fair and voluntary, rather than coerced.’ Thus, while mediation is no guarantee against the exercise of undue influence, it should help to minimize unfairness in the process by which a marital settlement agreement is reached.” *Id.* at 902. Moreover, if Clark were allowed to use this presumption to his advantage, Anna would not be able to introduce the privileged mediation communications to rebut it.

(v) By Agreement of the Parties a Mediation Confidentiality Agreement may be Disclosed and Parties may Waive the Automatic Mediation Termination Provisions of Evidence Code § 1125(a)(5) - *Wyner v. Porter*, 2013 WL 6667745 (2nd Dist., Jan. 14, 2014) (Not Reported)

This very convoluted case arose out of a dispute between clients (“Porters”) and their lawyer (“Wyner”). The underlying case involved a lawsuit to obtain special education services for the Porters’ minor child. After a mediation conference, the underlying case settled on favorable terms to the Porters and their son. Then the Porters sued Wyner on various claims, and Wyner countersued the Porters. At trial, Wyner conceded that certain evidence that might be covered by the mediation privilege could be admitted. The jury rendered verdicts in favor of the Porters.²¹ One month later, the California Supreme Court issued its opinion in *Simmons v. Ghaderi* (2008) 44 Cal.4th 570, which held that waivers of mediation confidentiality by either implication or estoppel were not permitted. Based on *Simmons*, Wyner moved for a new trial which was granted. The trial court held that Wyner’s oral waiver of confidentiality at trial was ineffective, meaning that the jury should never have heard the mediation related evidence. The Porters appealed and that led to the Court of Appeal’s first decision in this matter: *Porter v. Wyner*, 183 Cal. App. 4th 989 (2010) (“*Porter I*”).

In *Porter I*, the Court of Appeal ruled that the *Simmons* rule regarding no implied waivers of mediation confidentiality did not apply because the mediation confidentiality rules did not apply to communications between a party and his/her own lawyer. The Supreme Court granted review of *Porter I* and referred the case back to the Court of Appeal to reconsider in light of its 2011 decision in *Cassel v. Superior Court*, 51 Cal. 4th 113 (2011), which held that the mediation confidentiality protections were to be broadly construed to apply to all communications occurring during or pursuant to a mediation, even those between a disputant and his/her own lawyer. 51 Cal. 4th at 128. On remand from the Supreme Court, the Court of Appeal affirmed the trial court’s order granting Wyner’s motion for a new trial and remanded the matter with directions that the trial court rule on Wyner’s motion for judgment notwithstanding the verdict.

²¹ Given the number of times this case has been on appeal, it is perhaps of interest to note the amount of the verdict in favor of the Porters that was the subject of “*Porter I*.” The jury found that Wyner owed the Porters \$51,000 for breach of the fee agreement and owed Deborah Porter \$211,000 for paralegal services she had rendered in connection with the case Wyner had handled on her behalf.

Court of Appeal Case No. B211398 (“*Porter II*”). In so doing, the court of Appeal noted that “evidence potentially subject to mediation confidentiality is so interwoven with otherwise admissible evidence as to require the particularized determination of admissibility that the trial courts, rather than a reviewing court, are more suited to address.”

The trial court did just that. For the most part, the trial court decided that the evidence raised in support of the motion for JNOV was inadmissible, even though that very same evidence had been used to support the original jury verdict. The appellate court, in this its third opinion in the same case, affirmed. Step by step, it reviewed several questions regarding mediation confidentiality. For example, Wyner contended that mediation confidentiality ended for all communications that took place more than 10 days after the last communication with the mediator pursuant to Evidence Code Section 1125(a)(5). The Porters contended that mediation confidentiality did not conclude until a settlement was reached pursuant to Section 1125(a)(1) because, in advance of the mediation, the parties had signed a confidentiality agreement which expressly waived Section 1125(a)(5). Wyner contended that the mediation confidentiality agreement itself was inadmissible as it was not signed by the mediator or one of the other parties. The Court of Appeal concluded that it would be absurd to exclude an agreement that was signed by all of the parties presently before it, because that agreement provided the only evidence available on which to test the Porters’ contention about waiver.

The appellate decision provides analysis of several other mediation confidentiality and JNOV issues. It also notes that although the Supreme Court decision in *Cassel* holds that the mediation privilege extends to communications between a client and lawyer, it did not reach the question of whether any particular communication between client and lawyer might be subject to the privilege.

**(vi) Evidence of Negotiations at Mediation
Excluded as Privileged - *Kim v. Lim Ruger &
Kim*, 2014 WL 470422 (2nd Dist., Feb. 6, 2014)
(Not Reported)**

This is a spectacularly cautionary tale about making sure you carefully craft release provisions in settlement agreements. However, it says very little regarding confidential mediation discussions, other than to uphold the trial court’s exclusion of such evidence.

Plaintiff Kim hired the law firm of Lim, Ruger & Kim (“LRK”) to prepare an estate plan. The lawyers who worked on that plan left the firm after completing that work. Subsequently, Kim was sued by a bank for breach of various loan guarantees for defaulted loans \$12 million. The bank was represented by LRK, who was of several law firm’s on the bank’s “approved counsel” list and who had represented the bank in other matters. Kim moved to disqualify LRK. Kim lost the motion at the trial level, but prevailed on an extraordinary writ. Eventually, Kim and the bank (now with new counsel) participated in a mediation conference that yielded a settlement agreement. The settlement agreement included a broad general release provision that contained what some might view as “standard” language which provided for a release by Kim of the bank and “*each of its agents, employees, attorneys, officers, directors ...from any and all claims, actions, causes of action, demands, ... liabilities whatsoever (contingent, accrued, matured, direct, derivative, personal, individual, collective, assigned, discovered, undiscovered, known, unknown, inchoate or otherwise).*”

After the settlement of the guaranty action, Kim sued LRK for damages alleging various theories of liability for recovery of the attorney’s fees incurred related to the disqualification motion. LRK defended on the basis that Kim’s settlement agreement with the bank provided for a complete release of LRK because the release included the banks attorneys of which LRK was one of many and thus provided a release by Kim of any claims it had against LRK. The trial court agreed with LRK and found that the release in the settlement agreement unambiguously applied to LRK. In so ruling, it declined to allow Kim to introduce evidence of the negotiations with the bank or what the parties contemplated/discussed with respect to the release provision because those negotiations were excluded by virtue of the mediation confidentiality provisions in the Evidence Code. The appellate court affirmed. The appellate decision includes a brief section affirming the trial court’s decision to exclude certain evidence of the negotiations that took place during the mediation. The irony is that had the negotiations between Kim and the bank occurred privately (i.e., without facilitation through mediation), the parties negotiations would have been fair game as evidence.

Unfortunately for Kim, not only was he found to have released LRK in the settlement agreement between him and the bank, LRK also received an award of attorneys’ fees of more than \$230,000.00 as prevailing party pursuant to Civil Code Section 1717. Ouch!

B. BINDING MEDIATION

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 618 (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.

When presented with a similar "binding mediation" situation in 2012, this time the Fourth District Court of Appeal affirmed the trial court's judgment on the mediator's binding mediation award. See, *Bowers v. Raymond J. Lucia Companies, Inc.*, 206 Cal. App. 4th 724 (2012). In *Bowers*, the parties submitted their dispute to binding arbitration. After several days of evidentiary 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." With regard to the latter process, the parties agreed to participate in a full day mediation, and if they were unable to reach agreement at the end of the mediation, they agreed that 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 upon the parties' respective last and final offers, 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.

There were no case developments in 2013 concerning binding mediation. Nevertheless, this section of the 2012 recent developments materials was included in the 2013 materials as a placeholder for future developments concerning this important issue in alternative dispute resolution.

C. MISCELLANEOUS

- (1) **Mediation Provision in Contracts and CC&R's is Enforced and Attack Based on Unconscionability is Rejected – *The McCaffrey Group, Inc. v. Superior Court*, 2014 WL 1153392 (5th Dist., Mar. 24, 2014)**

Homeowners brought suit against builder to recover damages allegedly suffered due to defective construction of their homes. In response, the builder filed a motion to compel the homeowners to submit their construction defect claims to nonadversarial prelitigation procedures before proceeding with the lawsuit based upon provisions in their respective purchase agreements. Those procedures included providing the builder with notice of the claimed defect, giving the builder the right to inspect and correct it, and if the homeowner is still unsatisfied, engaging in non-binding mediation. The homeowners opposed the motion, contending that it was procedurally and substantively unconscionable because it had no deadline for completion of the mediation, and required the homebuyers to pay half of the mediator's fees. The trial court agreed with the homeowners, and denied the builder's motion on the grounds that the mediation clause was unconscionable and thus unenforceable. The trial court held the mediation provision was unconscionable because, among other things, "the provision permits the builder to unilaterally delay the submission of the issue brief and therefore the entire procedure. It also noted that there is no time specified within which the mediator must be selected" to the mediation could be delayed indefinitely.

The builder filed a writ petition, which was granted. The Court of Appeal reversed the trial court and held that reasonable deadlines for the completion of the mediation were implied as a matter of law in the mediation provision through the implied covenant of good faith and fair dealing. The Court also held that even if it was assumed that the mediation clause was presented on a "take it or leave it" basis by the builder, it showed only a low level of procedural unconscionability, and that requiring homebuyers to pay half of a mediator's fees to not render the provision substantively unconscionable.

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.

Class action litigants are increasingly likely to employ the doctrine of *cy pres* to settle complex class actions. See., e.g., Martin H. Redish et al., *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 Fla. L. Rev. 617, 620 (2010) (discussing the “dramatic turn in modern class actions toward the use of *cy pres* relief”). Under a line of cases beginning with *Six Mexican Workers*, supra, 904 F.2d 1303, the Ninth Circuit has required that a *cy pres* award (1) be reasonably certain to benefit the class, and (2) advance the objectives of the statutes relied upon in bringing the suit. See also *Nachshin v. AOL, LLC*, 663 F.3d 1034 (9th Cir. 2011); *Dennis v. Kellogg Co.*, 697 F.3d 858 (9th Cir. 2012).

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) **Settlement Agreement that Provides for the Formation of a New Grant-Making Organization is a Permissible *Cy Pres* Structure and is not Subject to a More Stringent Fairness Standard than that Applied to Extant Charities – *Lane v. Facebook, Inc.*, 696 F.3d 811 (9th Cir., Sep. 20, 2012), rehearing denied, 709 F.3d 791 (9th Cir. 2013)**

In November 2007, Facebook launched a new program called “Beacon,” which was described as a program that allowed its members to share with friends information about what they do elsewhere on the Internet. The program operated by updating a member’s personal profile to reflect certain actions the member had taken on websites belonging to companies that contracted with Facebook to participate in the Beacon program. Thus, for example, if a member rented a movie through the participating Blockbuster website, Blockbuster would transmit information about the rental to Facebook, and Facebook in turn would broadcast that information to everyone in the member’s online network by publishing to his or her personal profile. Although Facebook initially designed the Beacon program to give members the opportunity to prevent the broadcast of any private information, it never required members’ affirmative consent. As a result, many members complained that Beacon was causing publication of otherwise private information about their outside web activities without their knowledge or approval.

In 2008, a group of plaintiffs filed a putative class action in federal district court against Facebook and a number of other entities that operated websites participating in the Beacon program. The class-action complaint alleged that the defendant had violated various state and federal privacy statutes. Facebook denied liability and filed a motion to dismiss plaintiffs’ claims. Before the district court ruled on Facebook’s motion, the parties elected to attempt settlement through private mediation. After two mediation sessions and several months of negotiations, the parties arrived at a settlement agreement in which Facebook agreed to permanently terminate the Beacon program and pay a total of \$9.5 million in exchange for a release of all of the plaintiffs’ class claims. Of the \$9.5 million pay-out, approximately \$3 million would be used to pay attorney’s fees, administrative costs and incentive payments to the class representatives. Facebook would then use the remaining \$6.5 million to set up a new charity organization called the Digital Trust Foundation (“DTF”). The stated purpose of DTF was to “fund and sponsor programs designed to educate users, regulators and enterprises regarding critical issues relating to the protection of identity and personal

information online through user control, and the protection of users from online threats.”

DTF would be run by a three- member board of directors, one of whom was an employee/executive with Facebook. The settlement agreement also provided for the creation of a Board of Legal Advisors within DTF to advise and monitor DTF to ensure that it acted consistently with its mission as articulated in the settlement agreement.

After a hearing, the district court certified the class for settlement purposes and approved the parties’ proposed settlement over the objections of certain class members. The objecting class members then appealed, contending that the district court abused its direction in approving the settlement as fair, reasonable and adequate. When a class action settlement provides for a *cy pres* remedy, the district court should not find the settlement fair, adequate, and reasonable unless the *cy pres* remedy “accounts for the nature of the plaintiffs’ lawsuit, the objectives of the underlying statutes and the interests of the silent class members. . . .” 696 F.3d at 820, citing *Nachshin v. AOL, LLC*, 663 F.3d 1034, 1036 (9th Cir. 2011).

The Ninth Circuit affirmed the district court, finding that “[t]he *cy pres* remedy in this case properly accounts for the factors outlined in *Nachshin*.” *Id.* at 821. The Court found “no substance” in the objects’ argument that the presence of a Facebook employee on DTF’s board of directors made DTF ineligible as the entity to distribute the *cy pres* funds. The Court also rejected the objectors’ claim that the settlement structure was impermissible because the parties elected to create a new grant-making entity, rather than give *cy pres* funds to an already-existing entity. The Court noted that it had “never held that *cy pres* funds must go to extant charities in order to survive fairness review,” and ultimately concluded that DTF’s mission statement provided the “requisite nexus between the *cy pres* remedy and the interests furthered by the plaintiffs’ lawsuit consistent with the principles we announced in *Nachshin*.” *Id.* at 822.

After the above-described decision was handed down, the objecting parties/appellants requested rehearing *en banc*. That request was denied. 709 F.3d 791 (9th Cir. 2013).

(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) after remand, 2013 WL 188307 (S.D.Cal., May 3, 2013)

Consumers filed a class action against a breakfast-cereal producer alleging that the producer had made false and unsubstantiated representations in its advertising and labeling of its Frosted Mini-Wheats products in violation of California's Unfair Competition Law ("UCL") and California's Consumer Legal Remedies Act ("CLRA"), and similar laws of other states. Under the original settlement, all claims arising out of the challenged advertising were released in exchange for:

- a \$2.75 million cash fund for distribution to class members on a claims made basis;
- Kellogg distributing, pursuant to the *cy pres* doctrine, \$5.5 million of food products to charities to feed the indigent;
- Kellogg refraining from using the challenged representations in advertising for three years; and
- approximately \$2 million in attorneys' fees and costs.

The original settlement's cash value thus totaled approximately \$10.5 million. With attorney and claims administration fees and costs subtracted, the cash value to the class totaled approximately \$8.5 million.

But on September 4, 2012, the Ninth Circuit reversed the final settlement approval order, vacated the judgment and award of attorneys' fees, and remanded for further proceedings, finding that the *cy pres* award under the terms of the original settlement failed to target the plaintiff class. See *Dennis v. Kellogg Co.*, 697 F.3d 858, 869 (9th Cir. 2012). While the asserted claims concern fair competition and consumer protection, the *cy pres* award would benefit the indigent. The Ninth Circuit reasoned that "[t]his noble goal ... has 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.*

On remand, the parties renegotiated the settlement. Under the revised settlement, all claims arising out of the challenged advertising were released in exchange for:

- a \$4 million cash fund for distribution to class members on a claims made basis, with any remaining balance to be distributed equally, pursuant to the *cy pres* doctrine, among the Consumers Union, consumer Watchdog and Center for Science in the Public Interest; and
- Kellogg refraining from using the challenged representations in advertising for three years; and
- approximately \$2 million in attorneys' fees and costs.

The revised settlement's cash value thus totaled at most \$4 million. Minus attorney's fees of up to 25%, plus costs of approximately \$550,000 in claims notice and administration costs, the cash value to the class totaled approximately \$2 to 2.5 million.

The district court noted the Ninth Circuit's previous admonishments to the parties over both illusory dollar values and excessive attorney's fees. 697 F.3d at 868 (finding the settlement valuation "unacceptably vague and possibly misleading" and noting that "[t]he issue of the valuation ... must be examined with great care to eliminate the possibility that it serves only the 'self interests' of the attorneys and the parties, and not the class). It also stated that several aspects of the settlement gave the court pause, including the unanswered question as to how the mere identification of proper *cy pres* recipients resulted in such a severe drop in the value of the class's claims. Nevertheless, the district court found that the revised settlement fell within the range of possible approval because it appeared "to be the product of arms-length negotiations by experienced counsel, was reached after considerable litigation and discovery into the asserted claims, and provides considerable cash recovery and injunctive relief. And the Court is satisfied that the proposed *cy pres* recipients, each a well-established and well-regarded consumer protection organization, suffice under the Ninth Circuit's prescriptions." Accordingly, preliminary approval of the revised settlement was granted. Final approval was later given on November 14, 2013. 2013 WL 6055326.

(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.

(d) Alma Mater Connection Between Plaintiffs’ Counsel and a Proposed *Cy Pres* Beneficiary Was not a Significant Relationship Warranting Disqualification Based on the Appearance of Impropriety – *In re Easysaver Rewards Litigation*, 921 F.Supp. 2d 1040 (S.D.Cal., Feb. 4, 2013)

Consumers brought a class against defendants in which they complained that defendants’ practices of enrolling customers in rewards programs was unfair and unlawful because, among other things, they transmitted private payment information without consent, enrolled plaintiffs in a “rewards program” and charged their credit and debit cards fees without their knowledge or consent, and provided plaintiffs with no meaningful benefit. On remand, the parties renegotiated the settlement. After several years of litigation, the parties negotiated a settlement whereby defendants would provide various credits and refunds and would fund a \$12.5 Cash Fund that eligible class members could make claims against for refunds of monthly membership fees. The settlement provided that the Cash Fund was non-reversionary and any remaining funds would be distributed as a *cy pres* award to fund higher education projects relating to internet privacy and consumer protection at California State University at San Diego, University of California at San Diego and University of San Diego Law School. If all class members available themselves of the credits, the total value of the settlement was approximately \$38 million.

The district court approved the settlement and, in doing so, rejected the objections raised with regard to the *cy pres* component of the settlement concerning the perceived conflict of interest owing to a preexisting relationship between a *cy pres* beneficiary (the University of San Diego Law School) and plaintiffs’ counsel. The court reviewed a number of cases in which proposed *cy pres* beneficiaries were not approved due to existing relationships between attorneys on the case and the proposed beneficiary. In contrast to those cases, the court found that the alma mater connections involved in this case were not as significant as the relationships in the other cases and that no allegations had been made of any significant relationships between the attorneys and the law school beyond their alma mater association. 921 F.Supp. 2d at 1050-1051.

The district court also rejected objections raised with regard to the geographic distribution of the *cy pres* funds. Citing the Ninth Circuit's decision in *Nashchin v. AOL, LLC*, 663 F. 3d 1034 (9th Cir. 2011), the objector argued that because the recipients of the *cy pres* award were limited to San Diego, the *cy pres* distribution was therefore impermissible because it failed to account for the nationwide scope of the class. The district court found the unlike the settlement in *Nashchin*, the *cy pres* distribution in this case was directly tied to the statutes underlying plaintiffs' claims. In *Nashchin*, the *cy pres* distributions to the Los Angeles Boys and Girls Clubs and the Los Angeles Legal Aid, would be unlikely to flow to silent class members outside of the Los Angeles area. The district court found that these problematic aspects of the settlement in *Nashchin* were not present here. The *cy pres* beneficiaries here were universities that serve a diverse student population representing many states, they issue widely-distributed publications, and they engage in the overall national academic discourse. Because the internet is not limited by geographic boundaries, the court found that the educational impact of the funded academic programs would have a nation-wide impact. Regardless of the physical location of the schools, "programs furthering the goals of internet security and privacy will benefit users of the internet everywhere." *Id.* at 1052.

(e) The Direction that *Cy Pres* Funds be Paid to Western State for the Specific Purpose of Setting Up a Program and Professorship Regarding Internet Privacy and Data Security was Sufficiently Connected to the Plaintiff Class and Their Underlying Claims – *Cox v. Clarus Marketing Group, LLC*, 291 F.R.D. 473 (S.D.Cal., Apr. 2, 2013)

Consumers who had placed orders on a website, clicked to enroll in website club, and been charged for "free" shipping services without prior authorization, filed a putative class action against the website owner alleging violations of various state and federal consumer protection laws. Approximately one year into the litigation, and after participating in a full-day of mediation, the parties agreed on terms for a class wide settlement. The settlement included a *cy pres* component specifically directing that the *cy pres* payment to California Western be used to set up a program, professorship, etc. regarding internet privacy or internet data security. The district court concluded that the *cy pres* award was "tethered to the nature of the lawsuit" because the award was required to be used to further research or education regarding internet privacy or data security and thus satisfied the "nexus" requirement established by the Ninth Circuit in *Nashchin v. AOL, LLC*, 663 F.3d 1034, 1039 (9th Cir. 2011). *Id.* at 482.

B. STATUTORY OFFERS

(1) State Law - CCP § 998

Under California law, 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).

Section 998 authorizes any party to make a statutory offer to settle an action by allowing a judgment or dismissal to be entered based on the offer’s terms and conditions. Cal. Code Civ. Proc. § 998(b). The statute seeks to encourage settlement by providing parties a financial incentive to make and accept reasonable settlement offers before trial. *Martinez v. Brownco Const’n Co.*, 56 Cal. 4th 1014, 1019 (2013); *Chaaban v. Wet Seal, Inc.*, 203 Cal. App. 4th 49, 54 (2012). If a plaintiff rejects a defendant’s section 998 offer and thereafter fails to obtain a more favorable judgment, (1) “the plaintiff shall not recover his or her post offer costs and shall pay the defendant’s costs from the time of the offer,” and (2) the trial court may, in its discretion, require the plaintiff to pay the reasonable expert witness fees the defendant incurred. Cal. Code Civ. Proc. § 998(c)(1). If a defendant does not accept a plaintiff’s section 998 offer and thereafter fails to obtain a more favorable judgment, (1) the trial court may, in its discretion, require the defendant to pay the reasonable post offer expert witness fees incurred by the plaintiff in preparing for trial and at trial, Cal. Code Civ. Proc. §998(c), and (2) the judgment

against the defendant in any personal injury action shall accrue prejudgment interest at the rate of 10 percent per annum from the date of the offer. Cal. Civ. Code §3291.

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).

The policy behind section 998 is “to encourage the settlement of lawsuits prior to trial.” *T.M. Cobb Co. v. Superior Court*, 36 Cal. 3d 273, 280 (1984). To effectuate this policy, section 998 provides “a strong financial disincentive to a party – whether it be a plaintiff or a defendant – who fails to achieve a better result than that party could have achieved by accepting his or her opponent’s settlement offer.” *Bank of San Pedro v. Superior Court*, 3 Cal. 4th 797, 804 (1993). At the same time, the potential for statutory recovery of expert witness fees and other costs provides parties with “a financial incentive to make reasonable settlement offers.” *Id.* Section 998 aims to avoid the time delays and economic waste associated with trials and to reduce the number of meritless lawsuits. *Culbertson v. R.D. Werner Co., Inc.*, 190 Cal. App. 3d 704, 711 (1987); *Wilson v. Wal-Mart Stores, Inc.*, 72 Cal. App. 4th 382, 390 (1999).

(2) Cases

(a) **“Last Offer Rule” Rejected. Second Offer to Compromise Did not Preclude Award of Expert Fees Incurred After First Offer but Before Second Offer – *Martinez v. Brownco Const’n Co., Inc.*, 56 Cal. 4th 1014 (Cal. Sup. Ct., Jun. 10, 2013)**

In August 2007, plaintiffs Raymond Martinez and his wife, Gloria, served on defendant Brownco two separate offers pursuant to CCP § 998. Mr. Martinez offered to compromise his negligence claim in the amount of \$4.75 million, and Mrs. Martinez offered to compromise her loss of consortium claim for \$250,000. Brownco neither accepted nor rejected these offers within the 30-day period. Just before trial, in February 2010, plaintiffs served defendant Brownco with two separate, reduced compromise offers of \$1.5 million and \$100,000, respectively. Again, Brownco took no action in response to these offers.

At trial, plaintiffs obtained judgments in excess of their second, reduced compromise offers: \$1.6 million for Mr. Martinez and \$250,000 for Mrs. Martinez. Thereafter, plaintiffs filed a memorandum of costs seeking a total of \$561,257 in itemized costs. Brownco objected to \$188,536 in expert fees incurred after the first offer but before the second offer. The trial court agreed and taxed the disputed expert fees. Relying on *Wilson v. Wal-Mart Stores, Inc.*, 72 Cal. App. 4th 382 (1999), the trial court stated that the “most recently rejected offer is the only pertinent offer. All prior offers are extinguished by the subsequent offer.” Plaintiffs appealed and the Court of Appeal reversed, holding that allowance of expert fees incurred from the date of the first rejected offer was consistent with Section 998’s language and purpose, and that contract principles do not compel otherwise. The California Supreme Court granted Brownco’s petition for review and affirmed the Court of Appeal.

In affirming the Court of Appeal, the Supreme Court discussed and rejected the “last offer rule” established by *Distefano v. Hall*, 263 Cal. App. 2d 380 (1968) and *Wilson v. Wal-Mart Stores, Inc.*, supra, to the effect that when a party makes successive, unrevoked and unaccepted 998 offers, the last such offer is the only operative offer with respect to the statutory cost-shifting benefits and burdens. In so ruling, the Supreme Court relied upon its earlier holdings in *Poster v. Southern Cal. Rapid Transit Dist.*, 52 Cal. 3d 266 (1990) and *T.M. Cobb Co. v. Superior Court*, 36 Cal. 3d 273 (1984) that a basic contract law principle may not be applied if it would defeat or conflict with section 998’s policy of encouraging settlement. 56 Cal. 4th at 1024. The Court noted that section 998 provides for cost shifting “[i]f an offer made by a plaintiff is not accepted and the

defendant fails to obtain a more favorable judgment or award.” In the case presented to the Court, it was undisputed that both offers met the statutory time and content requirements; that Brownco did not accept either offer; and that Brownco did not obtain a judgment more favorable than either offer. The Court reasoned that allowing plaintiffs to recover expert fees incurred after the first offer but before the second offer “would further the goals of section 998. . . . to encourage settlement by affording the benefit of enhanced costs to parties who make reasonable settlement offers and imposing the burden of those costs on offerees who fail to obtain a result better than they could have achieved by accepting such offers.” *Id.* at 1025, citing, *Bank of San Pedro v. Superior Court*, 3 Cal. 4th 797, 804 (1992). If the statutory benefits and burdens were to run only from the date of the last offer, the Court reasoned that “in circumstances such as these, plaintiffs may be deterred from making early offers or from later adjusting their demands. This would inhibit settlement opportunities and be at direct odds with our prior recognition that ‘[t]he more offers that are made, the more likely the chance for settlement.’” *Id.*, citing *T.M. Cobb Co. v. Superior Court*, *supra*, 36 Cal. 3d at 281.

(b) What Satisfies the Procedural and Good Faith Requirements of CCP § 998? – *Whatley-Miller v. Cooper*, 212 Cal. App. 4th 1103 (2d Dist., Feb. 6, 2013)

In February 2008, deceased patient’s wife and children filed suit against Dr. Cooper. In June 2008, plaintiffs served Dr. Cooper with a 998 offer in which they agreed to resolve all claims against Dr. Cooper in consideration of \$950,000. The offer stated that if the offer was not accepted within 30 days and a judgment was later entered in favor of plaintiffs that was more favorable than the offer, the judgment would bear interest at the legal rate of 10% per annum, calculated from the date of plaintiffs’ offer, as provided by Civil Code section 3291. At the same time that the offer was served on Dr. Cooper, plaintiffs also served Dr. Cooper with a separate document (in the same envelope as the offer), entitled “Acceptance of Plaintiffs Offer to Compromise Pursuant to [Section] 998 and [Section] 3291. Plaintiffs’ offer was not accepted and the matter proceeded to trial in 2011, at which time plaintiffs obtained a judgment against Dr. Cooper in excess of \$1.4 million. Plaintiffs’ attorney then filed a memorandum of costs in the total amount of \$530,315, of which \$411,100 consisted of prejudgment interest from June 2008 (the date of the compromise offer). The trial court expert witness fees and prejudgment interest as requested under the cost-shifting provisions of section 998. Dr. Cooper appealed on the grounds that the manner in which the offer had been communicated was not in proper form and was not made in good faith because it was made early in the case, just two weeks after providing responses to the doctor’s discovery requests.

With regard to the first issue, the Court of Appeal noted that section 998(b) expressly contemplates and provides an acceptance of a statutory offer may be made “on the document containing the offer or on a separate document of acceptance” as long as it is in writing and signed by counsel for the accepting party or, if not represented by counsel, the accepting party. The Court held that compliance with the procedural aspects of section 998 may be satisfied by an offer of compromise that is comprised of a statement of the offer and a separate document of acceptance; that section 998 does not specify that the acceptance must contain any specific words or that it be made in a particular manner, other than it be in writing and signed by the appropriate person.

With regard to the second issue, the Court of Appeal noted that to effectuate the purpose of the statute, a section 998 offer must be made in good faith to be valid; that good faith “requires that the pretrial offer of settlement be ‘realistically reasonable under the circumstances of the particular case’” and “‘must carry with it some reasonable prospect of acceptance.’” 212 Cal. App. 4th at 1112, citing *Jones v. Dumrichob*, 63 Cal. App. 4th 1258, 1262 (1998). The Court of Appeal then went on to discuss how reasonableness is measured, stating that whether an offer is reasonable “‘depends upon the information available to the parties as of the date the offer was served.’” *Id.*, citing *Westamerica Bank v. MBG Industries, Inc.*, 158 Cal. App. 4th 109, 130 (2007). The Court of Appeal found that the trial court’s finding that plaintiffs’ offer of compromise was “made in good faith” was not the product of an abuse of discretion because that determining was supported by the evidentiary record. In this regard, the Court of Appeal noted that the trial court issued a written ruling in which it “laid out in considerable detail the information regarding decedent’s annual income and the financial impacts of his death produced during discovery . . . prior to the offer.” The trial court also noted that the offer was within Dr. Cooper’s insurance policy limits. Dr. Cooper did not challenge any of the trial court’s factual findings. Instead, his position was that the offer was unreasonable because he was not allowed sufficient time to investigate the facts and evaluate liability and damages prior to the offer expiring. On this point, the Court noted that Dr. Cooper had not asked for more time or advised the plaintiffs that he needed more information to evaluate their offer. Implicitly, the Court concluded that Dr. Cooper did not need more time or information to evaluate the offer in 2008. *Id.* at 1114.

As a side issue, Dr. Cooper challenged the reasonable necessity of the expert fees awarded to plaintiffs as costs. On this issue, the Court of Appeal held that it was Dr. Cooper’s burden to establish that the amounts awarded were not reasonably necessary and that burden required more than simply filing a motion to tax costs. If the items in a cost memorandum appear proper, the verified memorandum constitutes prima facie evidence that the expenses were necessarily incurred by the prevailing party. *Id.* at

1115, citing *Benach v. County of Los Angeles*, 149 Cal. App. 4th 836, 858 (2007). To controvert this evidence, the burden is on the objecting party to present evidence showing the contrary. *Id.* In the present case, Dr. Cooper simply attacked the billing statements of the experts as vague and ambiguous. The Court of Appeal found that this was not enough; that Dr. Cooper needed to present evidence of facts demonstrating that the amounts were unnecessary or unreasonable. *Id.*

(c) Where There is More Than One Plaintiff, a Defendant May Extend a Single Joint Offer if the Separate Plaintiffs Have a Unity of Interest Such That There is a Single, Indivisible Injury – *McDaniel v. Asuncion*, 214 Cal. App. 4th 1201 (5th Dist., Mar. 27, 2013)

Steven McDaniel was killed in a multiple vehicle accident and left behind his wife and daughter. They filed a wrongful death action against multiple defendants, including defendant Loyd Asuncion. Before trial, Asuncion served a joint section 998 offer on plaintiffs in the amount of \$100,000. Plaintiffs did not accept that offer and the matter proceeded to trial against Asuncion and one other defendant. While the jury returned a verdict of over \$3.3 million against the other defendant, it returned a defense verdict in favor of Asuncion. As the prevailing party, Asuncion submitted a memorandum of costs. Because plaintiffs had not obtained a judgment against Asuncion that was more favorable than his section 998 offer, the trial court awarded Asuncion his expert witness fees. Plaintiffs appealed, contending that the trial court erred because Asuncion had made a single, joint offer to the two plaintiffs.

On review, the Court of Appeal acknowledged that generally speaking, a section 998 offer made to multiple parties is valid only if it is expressly apportioned among them and not conditioned on acceptance by all of them. 213 Cal. App. 4th at 1206, citing *Burch v. Children's Hospital of Orange County Thrift Stores, Inc.*, 109 Cal. App. 4th 537, 543 (2003) and *Vick v. DaCorsi*, 110 Cal. App. 4th 206, 210 (2003). However, it held that there is an exception to this general rule if separate plaintiffs have a "unity of interest such that there is a single, indivisible injury." *Id.*, citing *Peterson v. John Crane, Inc.*, 154 Cal. App. 4th 498, 505 (2007). Such is the case in a wrongful death action. Either the heirs or the personal representative of the decedent's estate (on behalf of the heirs) may bring a single, joint, indivisible action for wrongful death, meaning that all heirs should join in a single action and there cannot be a series of suits by heirs against the tortfeasor for their individual damages. *Id.*, citing *Smith v. Premier Alliance Ins. Co.*, 41 Cal. App. 4th 691, 696 (1995) and *San Diego Gas & Electric Co. v. Superior Court*, 146 Cal. App. 4th 1454, 1551 (2007).

The trial court was affirmed, with the Court of Appeal noting that three other Courts of Appeal had considered a joint section 998 offer in a wrongful death action scenario and had reached two different results. *Id.* at 1207, citing *Gilman v. Beverly California Corp.*, 231 Cal. App. 3d 121 (1991) (offer by four plaintiffs to a single defendant was not a valid section 998 offer for purposes of cost-shifting because the joint offer did not afford the defendant the opportunity to evaluate the distinct loss suffered by each plaintiff); *Stallman v. Bell*, 235 Cal. App. 3d 740, 746 (1991) and *Johnson v. Pratt & Whitney Canada, Inc.*, 28 Cal. App. 4th 613, 639 (1994) (joint offer made by multiple plaintiffs held to be valid under section 998 for cost-shifting purposes because there was but a single verdict to be compared to the single offer). That conflict aside, the Court of Appeal for the Fifth District noted that one aspect of this case that distinguished it from *Gilman*, *Stallman*, and *Johnson* was that the offer was made *to* multiple plaintiffs by a single defendant as opposed to having been made *by* multiple plaintiffs.

(d) Offer Communicated Before Case Was “At Issue” Was Reasonable for Purposes of Cost-Shifting Under CCP § 998 and Trial Technology Costs are Allowable/Recoverable Costs – *Bender v. County of Los Angeles*, 217 Cal. App. 4th 968 (2nd Dist., Jul. 9, 2013)

The background facts of this case are rather gruesome and involve the beating, false arrest and detainment of an innocent civilian, followed by parallel criminal and civil proceedings. While plaintiff was being prosecuted criminally, he filed an action against the sheriff deputies who beat him, seeking damages for assault and battery, false arrest and false detainment. The action was filed in July 2010. Plaintiff was fully acquitted in September 2010. Three days after the acquittal, but before the civil action was at issue, plaintiff made a section 998 offer of \$399,000 to the defendants, which they did not accept. The matter proceeded to trial where the jury returned a verdict in favor of plaintiff for economic and non-economic damages in excess of \$500,000, plus an attorney’s fees award of almost \$1 million. Plaintiff was also awarded approximately \$27,000 in costs for expert witness fees and approximately \$24,000 in costs for courtroom technology. Defendants appealed on several issues, including the good faith of the section 998 offer and the availability of courtroom technology costs as allowable cost items.

With regard to the good faith aspect of the section 998 offer, the defendants contended that the offer was unreasonable because the action was not yet at issue when it was made and they therefore had no basis on which to measure the reasonableness of the offer because they had not had the benefit of discovery. Defendants relied on *Najera v. Huerta*, 191 Cal. App. 4th 872, 878 (2011) for the proposition that an “important factor in deciding whether a section 998 offer is unreasonable or in bad faith is whether the offeree was given a fair opportunity to intelligently evaluate the offer.” While the civil action was not at-issue, the criminal trial had been completed, the three deputies and the plaintiff had all testified, and the jury had acquitted and thus found contrary to the deputies’ testimony concerning the plaintiff’s alleged provocation that led to the severe beating. Moreover, the sheriff’s department had conducted an internal investigation and its findings were available to the deputies and their defense counsel. The trial court concluded that under these circumstances, the defendants “had sufficient information to evaluate the 998 offer and, if they required more time to seriously consider it, could have asked for an extension of the offer.” *Id.* at 989. The Court of Appeal agreed and affirmed.

With regard to the courtroom technology costs, that issue concerned the allowability of costs for items that are not mentioned in Code of Civil Procedure section 1033.5(a) or (b) (as expressly allowable or not allowable). Code of Civil Procedure section 1033.5(c)(4) provides that “[i]tems not mentioned in this section . . . may be allowed or denied in the court’s discretion. It further provides that any allowable costs must be “reasonably necessary to the conduct of the litigation rather than merely convenient or beneficial to its preparation,” and reasonable in amount. Cal. Code Civ. Proc. § 1033.5(c)(2), (3). In this case, plaintiff’s memorandum of costs included a claim for the costs associated with a trial video computer, PowerPoint presentation, videotape synchronizing and a trial technician for nine days of trial. In challenging the award of these cost items, defendants relied upon a 1995 case – *Science Applications Internat. Corp. v. Superior Court*, 39 Cal. App. 4th 1095, 1103 (1995) – in which some technology costs were approved and others denied. Based upon the holding in *Science Applications*, defendants argued that the cost items at issue in the present case were “explicitly nonrecoverable.” The Court of Appeal noted that almost 20 years had passed since *Science Applications* was decided, “during which time the use of technology in the courtroom has become commonplace . . . and technology costs have dramatically declined.” The Court noted that “[i]n a witness credibility case such as this, it would be inconceivable for plaintiff’s counsel to forego the use of technology to display the videotapes of plaintiff’s interviews after his beating . . . and key parts of other witnesses’ depositions.” The Court also noted that *Science Applications* was an extreme case, factually, in which the Court was troubled that a party had incurred over \$2 million in expenses to engage in high-tech litigation resulting in a recovery of only \$1

million in damages.” That was not was occurred in this case, so the Court of Appeal found that the trial court had acted well within is discretion in allowing recovery of the courtroom technology costs incurred in this matter.

**(e) Failure to Include an Acceptance Provision
Invalidated Plaintiff’s Offer Under CCP § 998 –
Boeken v. Philip Morris USA, Inc., 217 Cal. App. 4th
992 (2nd Dist., Jul. 9, 2013) (partial publication)**

Deceased smoker’s son sued the cigarette manufacturer for wrongful death. Prior to trial, plaintiff served Philip Morris with an offer to allow judgment under section 998 in the amount of \$4.95 million, which offer Philip Morris did not accept. The matter proceeded to trial and the jury returned a verdict for plaintiff of \$12.8 million. Plaintiff then moved for an award of prejudgment interest pursuant to Civil Code section 3291 on the ground that the jury’s verdict exceeded his section 998 offer. The trial court denied the motion, ruling that plaintiff’s section 998 offer was invalid because it did not contain a provision that if Philip Morris was to accept the offer, it would do so by signing a written statement to that effect. The Court of Appeal affirmed the trial court and, in so doing, rejected plaintiff’s argument that the written statement of acceptance language contained in section 998 should be disregarded because Philip Morris was a sophisticated litigant who had gone on record as never settling these types of personal injury actions. *Id.* at 1003-1004. “[W]e interpret the mandatory requirements of the statute without regard to what occurred in this particular case or the tactics of a party.” *Id.* at 1004.

**(f) Under the Cost-Shifting Offer of Judgment Statute,
a Plaintiff May Fail to Obtain a More Favorable
Judgment Than the CCP § 998 Offer by Voluntary
Dismissal of the Case, Resulting in No Recovery at
All – *Mon Chong Loong Trading Corp. v. Superior
Court* - 218 Cal. App. 4th 87 (2nd Dist., Jul. 23, 2013)**

After a fall that allegedly resulted in a back injury at defendant’s supermarket in August 2010, plaintiff filed suit against the defendant market for damages resulting from negligence and premises liability. In December 2011, defendant served a demand for exchange of expert witness lists and reports, followed by a notice for an independent medical exam. Shortly thereafter, defendant served plaintiff with a section 998 offer to permit entry of judgment in favor of plaintiff for \$10,000 in exchange for a release of all existing and future medical claims. Plaintiff did not respond to the offer, did not appear for the independent medical exam and did not participate in the exchange of expert

witness lists and reports. Instead, on January 20, 2012, plaintiff filed a request for voluntary dismissal of her complaint without prejudice, which was entered that same day. Defendant then filed a memorandum of costs, including expert witness fees of \$3,600. The trial court granted plaintiff's motion to tax the expert witness fees item defendant's writ petition and vacated the trial court's order taxing the defendant's cost bill, with instructions to reconsider. In so ruling, the Court of Appeal held that section 998 does not require that the party who has submitted a valid and reasonable offer under the statute achieve any specific result; that the discretionary award of fees is triggered if the plaintiff fails to obtain a more favorable judgment or award; and that a plaintiff may fail to obtain such a result by failing to obtain any award at all, as in the case of a voluntary dismissal. *Id.* at 94. "Indeed, voluntary dismissal of a lawsuit is always conditioned 'upon payment of costs,' even if the dismissal is without prejudice and the potential exists, as in this case, for a refilling of the same action." *Id.*; citing *Cano v. Glover*, 143 Cal. App. 4th 326, 331 (2006).

(g) The CCP § 998 Offer Was Valid Because it Included Appropriate Instructions on How to Accept the Offer, Even if it Did not Include a Signature Block Below Those Instructions – *Rouland v. Pacific Specialty Ins. Co.*, 220 Cal. App. 4th 280 (4th Dist., Oct. 7, 2013)

Plaintiffs owned a hillside home in Laguna Beach that was damaged in a landslide. When their insurer denied their claim, they sued for breach of contract and insurance bad faith to recover for the damage to their home. Two months before trial, the insurance company served separate offers on each plaintiff offering to pay \$95,000 to one plaintiff and \$35,000 to the other plaintiff in exchange for general releases and dismissals with prejudice. Both offers stated, "If you accept this offer, please file an Offer and Notice of Acceptance in the above-entitled action prior to trial or within thirty (30) days after the offer is made." Plaintiffs did not accept the offer. After a five-week trial, the jury returned a defense verdict for the insurance company, finding that the policy did not cover landslide damage.

The insurance company then filed a memorandum of costs and sought \$385,000 from the plaintiffs, which amount included more than \$330,000 in expert witness fees. Plaintiff's moved to tax the expert witness fees on the grounds that the section 998 offers did not comply with the statutory requirements because they lacked a signature space for the plaintiffs to accept the offers. Plaintiffs also argued that the offers were token gestures, not made in good faith, and that the expert witness fees were unreasonable and unnecessary. The trial court granted the motion to tax and denied the

expert witness fees as costs on the grounds that the offers did not satisfy the acceptance requirements of section 998. In so ruling, the trial court relied on *Puerta v. Torres*, 195 Cal. App. 4th 1267 (2011) for the proposition that section 998 requires strict compliance, but did not identify the specific defect that invalidated the offers in question. The insurance company appealed.

On appeal, the Court of Appeal reversed and found that the insurance company's offers satisfied the requirements of section 998. "Nothing in the statute's language requires an offer to include either a line for the party to sign acknowledging its acceptance or any specific language stating the party shall accept the offer by signing an acceptance statement. Indeed, no "'magic language'" or specific format is required for either an offer or acceptance under section 998." 220 Cal. App. 4th at 288, citing *Berg v. Darden*, 120 Cal. App. 4th 721, 731-732 (2004). Surveying the several recent case decisions on this issue, the Court of Appeal held that an offer's acceptance provision "simply must specify the manner in which the offer is to be accepted (citations omitted)," and that the only statutory requirement for a valid acceptance is "a written acceptance signed by the accepting party or its counsel"; that the court may not impose any additional requirements or limitations that do not appear on the face of the statute. *Id.*, see also *Cadlerock Joint Venture, L.P. v. Lobel*, 206 Cal. App. 4th 1531, 1549 (2012) (a court is not authorized to insert qualifying provisions not included in a statute and may not rewrite the statute to conform to an assumed intention which does not appear from its language).

With regard to plaintiffs' challenge concerning the reasonableness of the expert witness fees sought by the insurance company as costs, the Court of Appeal remanded that matter for the trial court to determine, noting that even when an offer satisfies all of section 998's requirements, the decision whether to award expert witness fees, as opposed to any of the statute's other cost-shifting penalties, is vested in the trial court's sound discretion; that the insurance company was not entitled to its expert witness fees as a matter of right. *Id.* at 289.

(3) Federal Law – FRCP 68

Rule 68 of the Federal Rules of Civil Procedure is the federal counterpart to CCP § 998 with regard to cost-shifting and statutory offers. The primary distinction is that Rule 68 is a one-way provision available to defending parties only. Rule 68 provides that up to 14 days before trial, a defendant may serve a plaintiff with an offer to allow judgment to be taken against the defendant on specified terms with costs as then accrued. To qualify as a valid statutory offer, the offer must specify a definite sum for which judgment may be entered, but need not include an admission of liability by

the defendant. See *Mite v. Falstaff Brewing Corp.*, 106 F.R.D. 434, 435 (N.D.Ill. 1985). A monetary offer must specify a definite sum for which judgment may be entered against the offering defendant so as to provide “a clear baseline from which plaintiffs may evaluate the merits of their case relative to the value of the offer.” *Thomas v. Nat’l Football League Players Ass’n*, 273 F.3d 1124, 1130 (D.C.Cir. 2001). Also, to be valid, a Rule 68 offer must include an agreement to pay plaintiff’s costs incurred as of the date of the offer. See, *Cruz v. Pacific American Ins. Co.*, 337 F.2d 746, 750 (9th Cir. 1964). Thus, an offer to pay reasonable attorney fees and costs prior to the date of the offer does not permit an award for work done thereafter such as preparing the cost bill and motion for fees). See, *Guerrero v. Cummings*, 70 F.3d 1111, 1113 (9th Cir. 1995).

The Supreme Court has interpreted Rule 68 to mean that “[i]f an offer recites that costs are included or specifies an amount for costs, and the plaintiff accepts the offer, the judgment will necessarily include costs; if the offer does not state that costs are included and an amount for costs is not specified, the court will be obliged by the terms of the Rule to include in its judgment an additional which in its discretion [citations omitted] it determines to be sufficient to cover the costs.” *Marek v. Chesny*, 473 U.S. 1, 6 (1985). Where a suit is brought under a statute that provides for an attorney fee award to the prevailing plaintiff, relevant “costs” include attorney’s fees. *Id.* In *Marek*, the Supreme Court interpreted the cost-shifting provision of Rule 68 to apply equally in cases where a plaintiff is entitled to an award of attorney’s fees under 42 U.S.C. § 1988. This means that if a plaintiff rejects a valid Rule 68 offer made by a defendant and subsequently recovers damages in an amount less than the rejected offer or not at all, the plaintiff is not entitled to recover its post-Rule 68 costs and attorney’s fees *and* will have to pay the defendant’s post-Rule 68 offer costs and attorney’s fees. *Id.*

If the offer is accepted in writing within 14 days, either party may file the offer and acceptance with the court. “The clerk must then enter judgment,” Fed. R. Civ. P. 68(a), meaning that the court has no discretion to alter or modify the parties’ agreement. *Webb v. James*, 174 F.3d 617, 621 (7th Cir. 1998), citing *Mallory v. Eyrich*, 922 F.2d 1273, 1279 (6th Cir. 1991). If the offer is rejected and the “judgment that the offeree finally obtains is not more favorable than the unaccepted offer, the offeree must pay the costs incurred after the offer was made.” Fed. R. Civ. Proc. 68(d). The rule’s purpose is to encourage settlement and discourage protracted litigation. *Marek*, *supra*, 473 U.S. at 5.

While Rule 68 does not expressly state that the defendant’s offer must be in writing, it does require that the offer be “served” on opposing counsel. Thus, only a written offer will satisfy the service requirements of Rule 68. See *Magnuson v. Video Yesteryear*, 85 F.3d 1424, 1429 (9th Cir. 1996).

Rule 68 does not apply if the defendant obtains a judgment. *MRO Communications, Inc. v. American Tel. & Tel. Co.*, 197 F.3d 1276, 1280 (9th Cir. 1999), citing *Delta Air Lines, Inc. v. August*, 450 U.S. 346, 351 (1981) (“It is clear that [Fed. R. Civ. P. 68] applies only to offers made by the defendant and only to judgments obtained by the plaintiff. It therefore is simply inapplicable to this case because it was the defendant that obtained the judgment.”)

When an offer of judgment is made in a multi-party case, the offer should specify how much each defendant is offering to each plaintiff. Otherwise, if the offer is rejected, it may be impossible to tell whether the judgment obtained by a particular plaintiff against a particular defendant is “more favorable” than the offer. See *Gavoni v. Dobbs House, Inc.*, 164 F.3d 1071, 1076 (7th Cir. 1999). Where several defendants make a package offer to a single plaintiff, some courts have held that no apportionment is necessary. See *King v. Rivas*, 555 F.3d 14, 19 (1st Cir. 2009); *Le v. University of Pennsylvania*, 321 F.3d 403, 408 (3rd Cir. 2003).

No equivalent procedure exists under federal law for plaintiffs to put cost-shifting pressure on defendants. *Delta Air Lines, Inc. v. August*, 450 U.S. 346, 350 (1981). However, in diversity jurisdiction cases, Rule 68 does not preclude plaintiffs from making settlement demands under the state statutory offer rules. See, *MRO Communications, Inc. v. AT&T Corp.*, 197 F.3d 1276, 1281 (9th Cir. 1999).

(4) Cases

- (a) **To the Extent that an Accepted Rule 68 Offer is Ambiguous, the Court Applies General Principles of Contract Law to Determine the Meaning of the Agreement - *Evon v. Law Offices of Sidney Mickell*, 688 F.3d 1015 (9th Cir. 2012)**

Consumer debtor brought an action against a debt collector, alleging that he had violated the Fair Debt Collection Practices Act (FDCPA) by sending collection notices addressed to the debtor in care of her employer. The district court denied the debtor’s motions for partial summary judgment on the issue of liability and for class certification, but granted the defendant’s cross-motion for partial summary judgment on the class claims finding that neither the act of sending letters to the debtor’s workplace nor the content of the letters violated the FDCPA. The district court denied defendant’s request for summary judgment on the issue of whether defendant had violated the FDCPA by sending a letter to the debtor’s workplace, finding that fact

issues existed as to whether the letter was sent in error. After the district court rendered its decision on the parties' cross-motions for summary judgment, plaintiff/debtor accepted the defendant's Rule 68 offer of judgment on her individual claim.

The Rule 68 offer of judgment provided for plaintiff to recover her reasonable costs accrued as of the date of the offer, as determined by the Court. It also provided for plaintiff to recover her reasonable attorney's fees incurred through the date of the offer, as determined by the Court. Pursuant to the judgment, plaintiff filed an application for attorney's fees and costs in the amount of approximately \$90,000, in response to which the district court awarded her about \$2,300. Thereafter, both parties appealed various rulings by the district court. The principal issue on appeal concerned the district's rulings on the class issues and whether, after voluntarily settling her individual claim by accepting the Rule 68 offer, the plaintiff had retained a "personal stake" in the class certification ruling for purposes of pursuing the appeal. With regard to the Rule 68 issue, the case concerned the interpretation of the language used in the offer of judgment with regard to the scope of the release of claims included within the offer accepted by plaintiff.

To the extent that a Rule 68 offer is ambiguous, the Court applies general principles of contract law to determine the meaning of the agreement, including parol evidence "to shed light on" the meaning of the language used. 688 F.3d at 1022. In this case, the Court found it significant that defendant had made two differently worded Rule 68 offers to the plaintiff. The first offer, which was rejected, expressly stated that acceptance would operate to release all of her individual and class claims. The second offer, which was accepted, made no mention of the class-based claims. Accordingly, the Court found that plaintiff could not be said to have contracted away those claims – or her right to appeal the district court's rulings on the class claims – by virtue of having accepted the second Rule 68 offer.

(b) Silence or Ambiguity Concerning the Inclusion of Attorney's Fees and Costs as Being Within the Scope of the Offer is Resolved Against the Defendant/Offeror – *Sanchez v. Prudential Pizza, Inc.*, 709 F.3d 689 (7th Cir., Mar. 4, 2013)

Employee brought suit against her employer under Title VII alleging sex discrimination, sexual harassment and retaliation. Employee accepted the employer's offer of judgment, which specified that it included "all of Plaintiffs claims for relief." The district court then entered judgment in the employee's favor, but denied her request for attorney's fees and costs in addition to the amount specified in defendant's

Rule 68 offer. The Seventh Circuit disagreed and reversed, finding that if defendant's offer was meant to include attorney's fees and costs, it was silent on such matters and thus ambiguous. The court reasoned that an ambiguous offer puts the plaintiff in a very difficult situation and "would allow the offering defendant to exploit the ambiguity in a way that has the flavor of 'heads I win, tails you lose.'" 709 F.3d at 694. If the plaintiff accepts the ambiguous offer, the defendant can argue that costs and fees were included. If the plaintiff rejects the offer and later wins a modest judgment, the defendant can argue that costs and fees were not included, so that the rejected offer was more favorable than the ultimate judgment and that the plaintiff's recovery of costs and fees should be limited accordingly. *Id.* 693-694.

Because the defendant's offer was silent as to costs and fees, the court held that the ambiguity must be resolved against the offeror. Accordingly, the Seventh Circuit reversed and remanded the case for an appropriate award of attorney's fees and costs. "If an offer recites that costs are included or specifies an amount for costs, and the plaintiff accepts the offer, the judgment will necessarily include costs; if the offer does not state costs are included and an amount for costs is not specified, the court will be obliged by the terms of the Rule to include in its judgment an additional amount which in its discretion it determines to be sufficient to cover the costs.'" *Id.* at 694, quoting *Marek*, *supra*, 473 U.S. at 6.

(c) An Ambiguity as to Attorney's Fees in the Offer of Judgment Will be Construed Against the Defendant/Offeror as Drafter – *Recouvreur v. Carreon*, 940 F.Supp.2d 1063 (N.D.Cal., Apr. 12, 2013)

This matters arose from a complaint in which plaintiff sought a declaration that its satirical website – www.charles-carreon.com – did not infringe on the trademark defendant has on his own name. Shortly after plaintiff filed a motion for an award of attorney's fees and expenses incurred in connection with effecting service of the complaint on defendant, defendant made a Rule 68 offer to plaintiff which provided that plaintiff's use of the domain name and website using defendant's name would be deemed to not violate defendant's rights and that plaintiff would take "a total money judgment inclusive of costs in the amount of \$725, being the sum of the filing fee and service costs claimed." 940 F.Supp. 2d at 1065. Plaintiff accepted this offer and then filed a motion seeking over \$77,000 in attorney's fees.

The Supreme Court has explained that "motions for costs or attorney's fees are independent proceeding[s] supplemental to the original proceeding." *Cooter & Gell v. Hartmarz Corp.*, 496 U.S. 384, 395 (1990). A plaintiff's acceptance of a defendant's offer of

judgment will end the case on the merits, but it does not render moot a motion for attorney's fees. See, *Zucker v. Occidental Petroleum Corp.*, 192 F.3d 1323, 1329 (9th Cir. 1999) (explaining that no Article III case or controversy is needed with regard to attorney's fees "because they are but an ancillary matter over which the district court retains equitable jurisdiction even when the underlying case is moot."). In this case, even though the accepted offer of judgment included a provision for \$725 in costs to plaintiff, the district court found that that provision did not operate to preclude an award of attorney's fees to plaintiff because the wording of the judgment specifically delimited the \$725 as relating to the "filing fee" and "costs of service" and not to costs generally. As such, the court held that it was appropriate to construe any ambiguity against the defendant/offeror as the draft of the offer.

(d) An Unaccepted Rule 68 Offer that Would Fully Satisfy a Plaintiff's Claim Does not Render that Claim Moot – *Diaz v. First American Home Buyers Protection Corp.*, 732 F.3d 948 (9th Cir., Oct. 4, 2013). See also *Genesis Healthcare Corp. v. Symczyk*, 133 S.Ct. 1523 (2013)

In Diaz, plaintiff brought a class action on behalf of a putative nationwide class consisting of all persons who made a claim under a home warranty plan obtained from defendant after March 2003. The district court denied plaintiff's motion for class certification. Defendant then made a Rule 68 offer of judgment to plaintiff on her remaining claims for misrepresentation, breach of contract, and breach of implied covenant of good faith and fair dealing. Plaintiff did not accept the offer.

Defendant then filed a motion to dismiss for lack of subject matter jurisdiction, arguing that plaintiff's action was moot in light of Plaintiff's refusal to accept a Rule 68 offer for full satisfaction of the amount she could possibly recover at trial. The district court found that the unaccepted offer would have provided Plaintiff complete relief on her remaining claims, and was sufficient to render those claims moot. Plaintiff appealed.

Until *Diaz*, the effects of an unaccepted Rule 68 offer on plaintiff's individual claims was an open question in the Ninth Circuit; other circuits disagree on the question. In *Genesis Healthcare Corporation v. Symczyk*, 133 S.Ct. 1523, 1528-29 (2013), the Supreme Court discussed the issue, but in a 5-4 opinion determined that the issue was not before it and failed to resolve the split. The Court ruled that a case brought by an employee under the Fair Labor Standards Act of 1938 (FLSA), 29 U.S.C. § 201 *et seq.*, to recover damages for violations of that Act on behalf of himself and other "similarly

situated” employees is not justiciable when the individual plaintiff’s claim is moot. In reaching that decision, the Court assumed, without deciding, that petitioner’s Rule 68 offer mooted respondent’s individual claim. In a lively and engaging dissent, Justice Kagan suggested that the premise of the majority opinion – the assumption that the individual claim was moot – was bogus. The dissent emphasized that the language of Rule 68 specifies that “[a]n unaccepted offer is considered withdrawn.” Fed.R.Civ.P. 68(b).

In *Diaz*, the Ninth Circuit followed the approach set in Justice Kagan’s dissent in *Genesis Healthcare* and held that “an unaccepted Rule 68 offer that would have fully satisfied a plaintiff’s claim does not render that claim moot.” The district court’s dismissal order was vacated and the matter remanded for further proceedings.

(e) An Unaccepted Rule 68 Offer for the Full Amount of the Plaintiff’s Individual Claim, Made Before the Named Plaintiff Files a Motion for Class Certification, Does not Moot a Class Action (the “Pitts Rule” Applied) – *Ramirez v. Trans Union LLC*, 2013 WL 1089748 (N.D.Cal., Mar. 15, 2013)

This matter involved a putative class action in which plaintiff complained that Trans Union had violated the Federal Credit Report Act (FCRA) and the California Consumer Credit Reporting Agencies Act (CCRAA) by failing to ensure “maximum possible accuracy” of its credit reports, and failing to provide consumers with property disclosures. Shortly after plaintiff’s lawsuit was filed, defendant sent plaintiff a Rule 68 offer of judgment in the amount of \$5,001, plus court costs and reasonable fees. Plaintiff did not accept the offer. Defendant then moved to dismiss on the ground that the court lacked subject matter jurisdiction because defendant’s offer of judgment was more than plaintiff could recover on his individual claims. In light of the Ninth Circuit’s 2011 decision in *Pitts v. Terrible Herbst, Inc.*, 653 F.3d 1081 (9th Cir. 2011) (considering the effect of a pre-certification Rule 68 offer on a named plaintiff’s standing to pursue his claims), the Court denied defendant’s motion to dismiss and motion for reconsideration.

In *Pitts*, the Ninth Circuit surveyed Supreme Court precedent on the issue of mootness and concluded that allowing a Rule 68 offer to moot a class action by satisfying the class representative’s individual claims would allow a defendant to “pick off” lead plaintiffs and “effectively ensure that claims that are too economically insignificant to be brought on their own would never have their day in court.” 653 F.3d at 1091. The Ninth Circuit therefore held that “an unaccepted Rule 68 offer of judgment

– for the full amount of the named plaintiff’s individual claim and made before the named plaintiff files a motion for class certification – does not moot a class action.” *Id.* at 1091-1092.

(f) Rule 68 Offers of Judgment Apply to Attorney’s Fees Disputes Under the Cost-Shifting Provisions of the Resource Conservation and Recovery Act (“RCRA”) – *Interfaith Community Organization, et al. v. Honeywell Int’l, Inc.*, 726 F.3d 403 (3d Cir., Jul. 22, 2013)

In citizen suits brought under the Resources Conservation and Recovery Act (RCRA), 42 U.S.C. § 6901, *et seq.*, seeking cleanup of a contaminated area, the district court entered judgment against the corporate successor to the owner of the site. The next year, in 2004, the district court awarded plaintiffs their fees and costs for litigating the case, and required defendant to pay plaintiffs’ future fees and costs for monitoring defendant’s cleanup. In 2009, the parties failed to reach agreement on the fees sought for the monitoring work.

Plaintiff filed two separate fee applications, and defendant filed objections to the fee applications on various grounds. Defendant also served offers of judgment pursuant to Rule 68 for the disputed fees. In response, plaintiffs asked the district court to issue a declaratory judgment that defendant’s Rule 68 offers were null and void in the context of RCRA citizen suits. The district court upheld the fee request and ruled that Rule 68 offers of judgment cannot be made in citizens suits under RCRA. The court reasoned that Rule 68 offers made in RCRA citizen suits would violate the Rules Enabling Act, 28 U.S.C. § 2072, by discouraging the citizen suits that Congress intended to encourage.

The Third Circuit disagreed, finding that application of Rule 68 in this context did not violate the Rules Enabling Act. The Court also found that Rule 68 offers apply to attorney fees disputes after liability has been determined, finding that a Rule 68 offer is both consistent with the “extent of liability” language in Rule 68 and with the fee-shifting provisions of RCRA. “It may very well be that a Rule 68 offer of judgment in the context of a RCRA attorney’s fee dispute will require a plaintiff to make a hard choice between accepting what has been offered versus adjudicating the issues that are in dispute in such a case the appropriate hourly rate and the reasonableness of the hours expended. . . . Settlement offers often present difficult choices for a plaintiff, but that fact neither abridges nor modifies the substantive rights at issue.” 726 F.3d at 410.

(g) Defendant Could not Obtain Discovery Through Interrogatories of Information Related to Attorney's Fees for Purposes of Formulating a Rule 68 Settlement Offer – *Branscum v. San Ramon Police Department*, 283 F.R.D. 530 (N.D.Cal., Feb. 24, 2013)

In a civil rights action, the defendant City served a set of special interrogatories on plaintiff, including requests for a monthly breakdown of “statistical information” relating to plaintiff’s attorney fees. Plaintiff responded in part, but objected on the ground that the requests exceeded the proper scope of discovery under Rule 26. The City argued, *inter alia*, that the information would be useful in evaluating a settlement offer under Rule 68.

Rule 26 provides that “[parties may obtain discovery regarding any nonprivileged matter that is relevant to any party’s claim or defense” Fed. R. Civ. P. 26(b)(1). The Court found no authority to suggest that a settlement analysis was a factor to be considered with the parties’ “claims and defenses” under Rule 26.

(h) Mock Trial Expenses and Investigation Fees Related to Witness Location are Not Recoverable as Nontaxable Cost Items – *Beach v. Wal-Mart Stores, Inc.*, 958 F.Supp.2d 1165 (D.Nev., Jul. 23, 2013)

Customer brought a personal injury action against Wal-Mart arising from an alleged slip and fall accident. The action was filed in state court in December 2010 and was removed to federal court in January 2011. In May 2012, Wal-Mart made a Rule 68 offer of judgment in the amount of \$100,001. Plaintiff did not accept the offer and the matter proceeded to trial in October 2012. On November 1, 2012, the jury found in favor of Wal-Mart, who then filed a motion for attorney’s fees and nontaxable costs.

With regard to the nontaxable cost aspects of this case, the law in the Ninth Circuit is that where a statute authorizes an award of reasonable attorney’s fees to the prevailing party, the court has the discretion to award reasonable out-of-pocket litigation expenses as part of the attorney’s fee award “when it is the prevailing practice in a given community for lawyers to bill those costs separate from their hourly rates.” *Grove v. Wells Fargo Fin. Calif., Inc.*, 606 F.3d 577, 579-582 (9th Cir. 2010). In this case, Wal-Mart sought to recover costs of approximately \$9,000 for “mock trial/focus group” expenses and “witness location investigation” fees. This request for nontaxable costs was denied because the court found that neither expense was a reasonable litigation cost that should be compensated.

C. MISCELLANEOUS

(1) Settle with Your Adversary and Sue Your Attorney for Settlement Malpractice – A Possible Trend

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).

Last year, we looked at *Filbin v. Fitzgerald*, 211 Cal. App. 4th 154 (1st Dist., Nov. 12, 2012) as an example of this developing trend of settle with your attorney and then sue your attorney for “negligent” or “inadequate” settlement. Following a bench trial, the trial court in this case entered judgment in plaintiffs’ favor on the malpractice claim. The First District Court of Appeal reversed, explaining 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 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, however, the Court 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.

This year, we have *Roldan v. Callahan & Blaine*, 219 Cal. App. 4th 87 (4th Dist., Sep. 18, 2013). Plaintiffs were among a group of elderly, low-income apartment residents who sued the building owner for damages resulting from toxic mold contamination. Callahan & Blaine associated in as counsel, representing the plaintiffs on a contingent fee basis, which also obligated them to advance the substantial costs associated with preparation for trial. Plaintiffs settled the underlying case reluctantly and only after Callahan & Blaine attempted – unsuccessfully – to have them declared legally incompetent so that a guardian ad litem could be appointed to cooperate with the attorneys’ settlement efforts. Plaintiffs then brought suit against Callahan & Blaine alleging financial elder abuse, conversion and breach of fiduciary duty, among other claims.²² This case is discussed in Section I(E)(2)(f), above, concerning enforcement of the arbitration provision contained in the firm’s retainer agreement. According to the trial court’s docket, the three plaintiff lawsuits are proceeding to arbitration pursuant to a stipulation entered into between the parties and filed with the Court in early January 2014, which provides that “Defendants shall pay all fees and costs associated with the arbitration proceedings, and Plaintiffs shall never be subject to having to pay any costs or fees incurred by Defendants before, during or after the arbitration.” That stipulation was approved and became an order of the Court on January 29, 2014. Thus, the outcome on the merits of plaintiffs’ claims has not yet been determined and may not be a matter of public record unless and until the prevailing party seeks confirmation and/or the losing party seeks vacatur of the arbitration award.²³

²² The three plaintiffs’ actions are pending in the Orange County Superior Court where they are commonly referred to as *Roldan v. Callahan & Blaine*, Case No. 30-2009-00303966, *Chudacoff v. Callahan & Blaine*, Case No. 30-2010-00417796, and *Mendoza v. Callahan & Blaine*, Case No. 30-2010-00417811. Early on in the proceedings, the *Chudacoff* and *Mendoza* actions were consolidated with the *Roldan* action.

²³ According to the electronic file for the *Roldan* action, a post-arbitration review hearing is scheduled for August 26, 2014, so it would appear that the merits hearing is scheduled to occur before that date and that the parties may know that outcome by that date.

IV. PANEL BIOS



Christopher Blank has a solo practice in Newport Beach, CA, concentrating in business litigation, real estate finance and business bankruptcy. Previously, he was a partner with an international firm in its Newport Beach office. Chris serves on the Mediation Panel of the United States Bankruptcy Court for the Central District of California. Chris also serves as a fee arbitrator and mediator for the OCBA, and from 2007 through 2013 he served as Co-Chairperson of the OCBA Mandatory Fee Arbitration Committee. He was appointed to the California State Bar Mandatory Fee Arbitration Committee in 2013. He has two adult sons who he is proud to say are self-supporting. For fun, Chris is a bread baker and a licensed pilot with an instrument rating. Contact Info: clblank@pacbell.net 949-250-4600.



Rebecca Callahan is a 30-year, AV-rated attorney who acts as an independent mediator, arbitrator and ADR consultant. She is on the arbitration and mediation panels of the American Arbitration Association, and regularly teaches ADR courses as a faculty member of the American Arbitration Association University and as an adjunct professor at Pepperdine University School of Law. Rebecca 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. Rebecca received her JD from the University of California at Berkeley and her undergraduate degree from the University of Southern California. In 2007, she earned an LLM in Dispute Resolution from Pepperdine University School of Law. She is the Immediate Past Chair of the ADR Section of the OCBA and a current member of the OCBA Board of Directors.



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. This year, the Southern California Super Lawyers ranked him as one of its Top Ten Lawyers.

Stephen J. Kessler is a full-time mediator associated with QDR Services in Irvine, California. He also serves on the mediation panel of the U.S. District Court for the Central District of California. During the recent banking and financial crisis, he served as the Managing Counsel of the FDIC office in Irvine from its inception in early 2009 until it closed in 2012. Because of his substantial experience with the FDIC, he has particular expertise in dealing with complex commercial litigation, including cases involving banking and lending, bankruptcy, breach of contract, creditor/debtor, and real estate. He also has significant experience with employment, EEO (employment discrimination), and ERISA (employee benefit plan) cases.



Gail Killefer serves as the ADR Program Director for the U.S. District Court, Central District of California. In her work at the district court, Ms. Killefer oversees the administration of the Court's ADR Program and serves as a mediator herself. Before joining the Court in August 2010, Ms. Killefer had a private mediation and law practice in San Francisco and taught mediation at U.C. Hastings College of Law. She served as an Assistant United States Attorney in San Francisco from 1989 to 2001, as Deputy Chief of the Civil Division from 1994 to 1998, and as Chief, Civil Division, from 1998 to 2001. Before joining the U.S. Attorney's Office, she served as a Trial Attorney with the U.S. Department of Justice, Torts Branch, in Washington, D.C., and as a law clerk to the Honorable Barrington D. Parker (D.D.C.).



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. A full-time neutral for more than 20 years, she is on the Large Complex, International, Employment, Franchise, Real Estate and Commercial panels of AAA/ICDR. A full-time mediator and arbitrator since 1992, she has been named a Southern California Super Lawyer (2006-14) and a Best Lawyer in America (2006-14). 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 the incoming President of the College of Commercial Arbitrators, co-editor of the CCA's "Protocols for Expeditious, 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.

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