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Appellate courts sharply disagree over continuing impact of*Concepcion*

By John Querio and Felix Shafir

AT&T Mobility LLC v. Concepcion, 131 S.Ct. 1740 (2011), imposed significant restrictions on state laws limiting the enforceability of arbitration agreements governed by the Federal Arbitration Act. This past year saw appellate courts disagree sharply over the continuing impact of *Concepcion*'s FAA preemption standards on state arbitration law. Here are some of the most important developments in the wake of *Concepcion*:

Does the FAA preempt state unconscionability standards that target arbitration procedure?

Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal. 4th 83 (2000), allows state courts to find arbitration agreements unconscionable where arbitration procedures are insufficiently bilateral. Several courts have expressed doubts about whether *Armendariz*'s unconscionability standard survives *Concepcion*, and courts are divided over its continuing viability. *Lucas v. Hertz Corp.*, 2012 WL 3638568 (N.D.Cal. Aug. 22, 2012);*Antonelli v. Finish Line, Inc.*, 2012 WL 2499930 (N.D.Cal. June 27, 2012).

The state Supreme Court will have its first opportunity to address *Concepcion*'s impact on *Armendariz*'s unconscionability standard in two pending cases, *Sonic-Calabasas A, Inc. v. Moreno* (S174475) and *Sanchez v. Valencia Holding Co.* (S199119).

The first time it considered *Sonic-Calabasas*, the state Supreme Court found unconscionable an agreement to arbitrate statutory wage and hour claims because the agreement waived certain procedural protections available to employees. The U.S. Supreme Court vacated and remanded for reconsideration in light of *Concepcion*. This year, the state Supreme Court directed the parties to brief *Concepcion*'s impact, and the case is now ready for argument and decision.

These ongoing developments ... are likely to come to a head over the next few years, as the U.S. Supreme Court, 9th Circuit and state Supreme Court confront the splits of authority over Concepcion's impact.

In *Sanchez*, the Court of Appeal found unconscionable an arbitration clause that allowed parties a limited right to challenge arbitration awards before a panel of three arbitrators, and that preserved certain self-help remedies outside of arbitration. The court rejected the argument that the FAA preempted this application of *Armendariz*'s unconscionability standard under *Concepcion*, but the state Supreme Court granted review earlier this year to address that issue.

Can state public policy limit the enforceability of arbitration agreements?

Armendariz also held that public policy prohibits courts from enforcing agreements to arbitrate unwaivable statutory claims unless the arbitration procedures satisfy certain procedural requirements. But, as with*Armendariz*'s unconscionability standard, courts have questioned whether these public policy requirements remain good law after *Concepcion*. *Hwang v. J.P. Morgan Chase Bank, N.A.*, 2012 WL 3862338 (C.D.Cal. Aug. 16, 2012).

These doubts may grow in light of the U.S. Supreme Court's decisions in *Marmet Health Care Center, Inc. v. Brown*, 132 S.Ct. 1201 (2012), and *Nitro-Lift Technologies, L.L.C. v. Howard*, 133 S.Ct. 500 (2012), which followed *Concepcion* to hold that the FAA preempted state judicial precedents that relied on public policy to avoid arbitration of certain state-law claims.

In its first opinion in *Sonic-Calabasas*, the state Supreme Court - applying *Armendariz*'s public policy test - refused to enforce as written an employment agreement to arbitrate statutory claims. Now that the U.S. Supreme Court has remanded *Sonic-Calabasas* for reconsideration in light of *Concepcion*, the case presents California's highest court with the opportunity to resolve whether *Armendariz*'s public policy requirements survive*Concepcion*.

May courts refuse to enforce employment arbitration agreements that include class action waivers?

In *Gentry v. Superior Court*, 42 Cal. 4th 443 (2007), the state Supreme Court held that class action waivers in employment agreements to arbitrate statutory wage and hour claims could be invalidated based on *Armendariz*'s public policy test, notwithstanding FAA preemption.

Courts have disagreed sharply over whether the FAA preempts *Gentry* after *Concepcion*. One state court and several federal courts have held that *Gentry* does not survive *Concepcion*. *Iskanian v. CLS Transportation Los Angeles*, LLC, 206 Cal. App. 4th 949 (2012). Another state court concluded that *Gentry* does survive*Concepcion*. *Franco v. Arakelian Enterprises, Inc.*, 2012 WL 5898063 (Nov. 26, 2012). Yet other state courts have, to varying degrees, questioned *Gentry*'s continuing viability after *Concepcion*. *Reyes v. Liberman Broadcasting, Inc.*, 208 Cal. App. 4th 1537 (2012); *Truly Nolen of America v. Superior Court*, 208 Cal. App. 4th 487 (2012); *Nelsen v. Legacy Partners Residential, Inc.*, 207 Cal. App. 4th 1115 (2012); *Kinecta Alternative Financial Solutions, Inc. v. Superior Court*, 205 Cal. App. 4th 506 (2012). Having granted review in *Iskanian*(S204032), the state Supreme Court is poised to resolve this conflict.

Iskanian also presents the related issue of whether, as the National Labor Relations Board has found, class waivers in employment arbitration agreements impermissibly deny employees' right to engage in concerted action under federal labor law. *D.R. Horton, Inc.*, 357 N.L.R.B. No. 184 (Jan. 3, 2012). *Iskanian* disagreed with the NLRB decision, and the employer has appealed the NLRB ruling to the 5th US. Circuit Court of Appeals, where the case awaits oral argument and decision.

Can courts refuse to enforce arbitration agreements if arbitration would not vindicate state statutory rights?

The U.S. Supreme Court has indicated that, despite Congress' protection of arbitration through the FAA, courts have authority to invalidate arbitration agreements that may fail to vindicate *federal* statutory rights, i.e., rights granted by Congress. The state Supreme Court has extended this vindication principle to hold that, as a matter of state public policy, courts may refuse to enforce arbitration agreements where arbitration would not vindicate unwaivable *state* statutory rights. *Armendariz*'s procedural prerequisites for enforcing arbitration agreements and*Gentry*'s prohibition on class waivers in such agreements rested on this principle.

But the U.S. Supreme Court subsequently held in *Concepcion*, *Marmet* and *Nitro-Lift* that the FAA preempts state anti-arbitration judicial precedent predicated on public policy. And earlier

this year the U.S. Supreme Court held that the FAA mandates arbitration even of federal statutory claims "unless the FAA's mandate has been 'overridden by a contrary congressional command.'" *CompuCredit Corp. v. Greenwood*, 132 S.Ct. 665 (2012).

Accordingly, some state and federal appellate courts have held the vindication principle applies to fend off arbitration only of certain federal claims. *Coneff v. AT&T Corp.*, 673 F.3d 1155 (9th Cir. 2012); *Iskanian*, 206 Cal. App. 4th at 380-81. But not all courts agree; in *Franco*, a state court recently held this principle applies to state-law claims, too.

The state Supreme Court may soon examine the vindication principle's scope in *Sonic-Calabasas* and *Iskanian*, since *Armendariz* and *Gentry* were based on that principle and their continuing viability is at issue in those cases.

The 9th Circuit may also address this subject. A three-judge panel recently held the vindication principle "applies only to f*ederal*, not state, statutes." *Kilgore v. KeyBank, Nat'l Assocs.*, 673 F.3d 947 (9th Cir. 2012). But the 9th Circuit granted rehearing en banc, with oral argument occurring this month.

Additionally, the U.S. Supreme Court is set to weigh in on the vindication principle next year following the grant of certiorari from a 2nd Circuit decision refusing to enforce an arbitration agreement containing a class waiver. The 2nd Circuit held the waiver effectively precluded plaintiffs from bringing federal antitrust claims that could not economically be pursued individually. *In re American Express Merchants' Litigation*, 667 F.3d 204 (2d Cir. 2012), *cert. granted sub. nom. American Express Company v. Italian Colors Restaurant*, 133 S.Ct. 594 (2012).

Can courts compel parties to arbitrate statutory claims for public injunctive relief and penalties?

Before *Concepcion*, the state Supreme Court barred enforcement of agreements to arbitrate claims for public injunctive relief under certain state consumer protection statutes. *Cruz v. PacifiCare Health Systems, Inc.*, 30 Cal. 4th 303 (2003); *Broughton v. Cigna Healthplans*, 21 Cal. 4th 1066 (1999). Creating what is known as the "*Broughton-Cruz*" rule, the court held the FAA did not preempt this state-law limitation on parties' ability to arbitrate.

One state court has since extended the *Broughton-Cruz* rule to hold that, notwithstanding *Concepcion*, plaintiffs cannot be compelled to individually arbitrate representative claims for penalties under the Private Attorneys General Act, or PAGA. *Brown v. Ralphs Grocery Co.*, 197 Cal. App. 4th 489 (2011). But more recently, a state court (in *Nelsen*) and the 9th Circuit (in *Kilgore*) concluded that the FAA preempts the *Broughton-Cruz* rule after*Concepcion*. Moreover, another state court (in *Iskanian*) disagreed with *Brown*, holding that the FAA preempts state law prohibiting individual arbitration of PAGA claims.

As noted above, the 9th Circuit will soon rehear *Kilgore* en banc, and in *Sanchez* and *Iskanian*, the state Supreme Court may also examine FAA preemption of the *Broughton-Cruz* rule.

These ongoing developments in arbitration law are likely to come to a head over the next few years, as the U.S. Supreme Court, 9th Circuit and state Supreme Court confront the splits of authority over *Concepcion*'s impact described in this article. Stay tuned.

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