No. S199119

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

GIL SANCHEZ, Plaintiff and Respondent vs. VALENCIA HOLDING COMPANY, LLC, Defendants and Appellant.	B228027 (Los Angeles County Super. Ct. No. BC433634)

OPENING BRIEF ON THE MERITS

California Court of Appeal, Second District, Division One
Case No. B228027
Los Angeles Superior Court Case No. BC433634
Honorable Rex Heeseman

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INTRODUCTION

In *AT&T Mobility v. Concepcion* (2011) 563 U.S. ___ [131 S.Ct. 1740] (*Concepcion*), the United States Supreme Court struck down this Court's refusal to enforce as substantively unconscionable certain arbitration provisions excluding class action claims. It held that even if a class action waiver would be unconscionable under state law, the Federal Arbitration Act (the "FAA") preempts and requires the arbitration agreement to be enforced according to its terms. But *Concepcion* did more than just preempt one particular state-court unconscionability rule regarding class action waivers; rather, it generally limited the use of unconscionability to attack the parties' selected arbitration procedures. It held that the FAA bars states, under the guise of unconscionability, from negating the "parties[']discretion in designing arbitration processes . . . to allow for efficient, streamlined procedures tailored to the type of dispute." (131 S.Ct. at p. 1749.)

Thus, states cannot refuse to enforce a particular arbitration process based on a policy determination that the process is "unfair" or "harsh." *Concepcion* makes clear that states (whether by statute or judicial decision and regardless of their concerns for procedural safeguards) cannot second-guess the *process* that the parties have contractually designed for arbitration, so long as that process is rationally tailored to likely disputes.

Here, the automobile purchase contract's arbitration provision reflects the parties' contractual agreement as to the process they will employ to resolve their disputes. It is even-handed. It applies to both buyer

and dealer claims. It has a second-look mechanism with a three-member arbitration panel to review *outlier* results, for and against *both* buyers and the dealer – injunctive relief (favoring either side), $0 and over $100,000 awards. Typical results in car purchase disputes are going to fall within the $0 to $100,000 range, and thus outside the second-look clause, making the process a context-tailored one. Only by second-guessing the parties' discretion in designing the arbitral process – which *Concepcion* prohibits – can enforcement of arbitration be refused.

Nor can the arbitration provision here be deemed unconscionable even under California's standard unconscionability principles. Unconscionability must be tethered to objective criteria, not amorphous, subjective judge-by-judge reactions to what might be overly one-sided or unduly harsh. An unconscionability determination must be based on the arbitration provision *as a whole*, not on dissecting the provision, reviewing individual clauses in isolation and only focusing on how a term might disadvantage a party in a particular situation. For there to be unconscionability, the overall balance must reflect a complete lack of *any* plausible business justification.

So examined, the provision here falls well within the ballpark of reasonable give-and-take. It is even-handed. It is well justified by the business realities of the buyer-dealer relationship and the threats posed by outlier results. That's not substantively unconscionable. Unless the rule is that consumer arbitration must be full, one-shot, arbitration of all possible issues at no expense to the consumer – a rule that *Concepcion* undoubtedly

rejects as a basis for not enforcing arbitration – then *this* arbitration provision's process must be valid. It involves *mutual* tradeoffs and a rational relationship to the nature of automobile purchases in general and to the specific transaction at issue – the purchase of a $50,000 pre-owned luxury automobile from a family-owned dealership.

The judgment of the trial court and the Court of Appeal should be reversed with directions to compel arbitration.

But if the arbitration provision's plain language and the undisputed facts about the transaction's nature do not compel that result, then the judgment of the trial court and the Court of Appeal still must be reversed, and the matter remanded to the trial court so it can exercise – for the first time – its fact-finding and discretionary powers regarding unconscionability and severance.

ISSUES FOR REVIEW[1]

1. Does *AT&T Mobility v. Concepcion* (2011) 563 U.S. ___ [131 S.Ct. 1740], constrain California courts outside of the class action waiver context in passing, under the guise of substantive unconscionability, on the procedures and processes that the parties have chosen in tailoring an arbitration provision to particular types of disputes? Must such arbitration procedures afford exact equality of procedural advantage to all parties in all cases?

2. Has *AT&T Mobility v. Concepcion* (2011) 563 U.S. ___ [131 S.Ct. 1740], displaced the bar to arbitration of statutory injunctive claims in *Broughton v. Cigna Healthplans of Cal.* (1999) 21 Cal.4th 1066, and *Cruz v. PacifiCare Health Systems, Inc.* (2003) 30 Cal.4th 303, as several federal district courts have held, or does the *Broughton-Cruz* bar to statutory injunctive relief arbitration retain vitality after *Concepcion*, as the Court of Appeal here appears to have assumed and two federal district courts have held?

3. Is the arbitration provision in the standard auto sales contract unconscionable, as a matter of law, (A) whenever a plaintiff claims to have not read it even though the contract, on its face, just above a signature line in all capital letters references an arbitration provision set out in a large box

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[1] These issues – other than issue 5, see footnote 2 below – are taken verbatim from the Petition for Review. (California Rules of Court, rule 8.520(b)(2)(B).)

on the back of the one-page document and (B) because (1) it allows for an internal arbitral appeal process for extreme, outlier bilateral results ($0, >$100,000, injunctive relief), (2) requires the losing party to advance the costs of an internal arbitral appeal, and (3) excludes from arbitral issues self-help relief that, by definition, is not part of any court process?

4. Where the trial court has never passed on unconscionability or severability, can the appellate court determine those issues in the first instance (as in this case) or is remand to the trial court required for it to find facts and exercise its discretion in the first instance as held in *Brown v. Ralphs Grocery Co.* (2011) 197 Cal.App.4th 489, 504?

5. Whether *Fisher v. DCH Temecula Imports LLC* (2010) 187 Cal.App.4th 601, relied upon by the trial court, survives *AT&T Mobility v. Concepcion* (2011) 563 U.S. ___ [131 S.Ct. 1740]?[2]

[2] Fairly read, this is the issue raised, though not precisely formulated, in the Answer to Petition for Review, Answer at 22-23.

STATEMENT OF THE CASE

A. The Complaint.

Plaintiff Gil Sanchez alleges that he bought a "certified" used Mercedes Benz for roughly $50,000. (AA 15, 274-275; Opn. at 3-4.)[3] He alleges various problems with the transaction, from representations made to fees charged to the vehicle's condition. (*Ibid.*) He filed suit alleging a class-action. (AA 1; Opn. at 5-6.) His class action claims sought redress for asserted violations in (1) failing to advise buyers that part of a down payment was being deferred, without interest, (2) failing to separately list license and registration/transfer/titling fees, (3) automatically charging a $28 DMV electronic filing fee, and (4) charging a $1.25 per tire new tire fee for tires that might be used tires.[4] (AA 6-7.)

B. The Sale Contract.

In purchasing the vehicle, Sanchez executed a standard, preprinted Retail Installment Sale Contract. (AA 271-279; Opn. at 3-4.) The contract form was produced by an industry source, not the individual dealership. (Opn. at 4, fn. 2; see AA 276.) The contract is 26 inches long by a standard 8½ inches wide, printed on both sides of one piece of paper. (Opn. at 8; see

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[3] References are to the Appellant's Appendix in the Court of Appeal and to the Court of Appeal's modified opinion.

[4] As unconscionability is determined at the time of contracting (Civ. Code, § 1670.5), the further specifics of plaintiff's claims are irrelevant at this juncture.

AA 272, Petn. Rev., App. C.)[5] Statutorily required language and font size accounts for 24 inches of that length (back and front). (92 Ops.Cal.Atty.Gen. 97 at *1 (2009); see Civ. Code, § 2982.)

Plaintiff signed the document multiple times on its front side. (AA 276; Opn. at 8.) Above one set of signature lines (for both "buyer" and "co-buyer") is a box notice of "No Cooling-Off Period" and next to it, in all capitals, the following language acknowledging the arbitration provision:

> "YOU AGREE TO THE TERMS OF THIS CONTRACT. YOU CONFIRM THAT BEFORE YOU SIGNED THIS CONTRACT, WE GAVE IT TO YOU, AND YOU WERE FREE TO TAKE IT AND REVIEW IT. YOU ACKNOWLEDGE THAT YOU HAVE READ BOTH SIDES OF THIS CONTRACT, INCLUDING THE ARBITRATION CLAUSE ON THE REVERSE SIDE, BEFORE SIGNING BELOW. YOU CONFIRM THAT YOU RECEIVED A COMPLETELY FILLED-IN COPY WHEN YOU SIGNED IT."

(AA 276; Opn. at 18.)

C. The Arbitration Provision.

The referenced arbitration provision appears on the back of the contract in a large black box. (AA 279; Opn. at 8; Petn. Rev., App. C.) The arbitration provision calls for binding arbitration before a single arbitrator

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[5] A replica copy of the form was submitted to the Court of Appeal at its request on November 16, 2011, and was also attached to the petition for review as Appendix C.

(required to be an attorney or retired judge) under the auspices of two nationally recognized organizations *or* any other organization chosen by the buyer (subject to the dealer's reasonable approval). (AA 279; Opn. at 6-7 & 8, fn. 3.) Self-help remedies and small claims actions are excluded from arbitration. (AA 279; Opn. at 7.) Class-action arbitration is waived. (*Ibid.*) The dealer is to advance up to $2,500 of the buyer's initial arbitration fees. (*Ibid.*)

In the event of an arbitration award of (a) $0, (b) in excess of $100,000, or (c) for injunctive relief, the aggrieved party may obtain a second level of review in a three-person arbitration. (AA 279; Opn. at 7.) The party seeking such review is to initially bear the expense of the new arbitration round (subject to the three-person panel's ultimate allocation). (*Ibid.*)

The arbitration provision makes severable any unenforceable clause, other than the class action waiver: "[I]f any part of this Arbitration Clause, other than waivers of class action rights, is deemed or found to be unenforceable for any reason, the remainder shall remain enforceable." (AA 279.)

D. The Motion To Compel Arbitration.

Defendant Valencia Holding Company, LLC moved to compel arbitration. (AA 238; Opn. at 6.) In opposing arbitration, plaintiff declared that he did not read the contract before signing it, that he was unaware that there was an arbitration provision on the back of the contract, and that no

one at the dealership had pointed out the arbitration provision to him. (AA 357-358; Opn. at 9.)[6] His declaration was at odds with his signed acknowledgment in the contract itself that he had read and had an opportunity to review the contract, including the arbitration provision. (Compare *ibid.* with AA 276; Opn. at 18.)

E. The Trial Court Refuses To Compel Arbitration Because Of The Class-Action Waiver.

The trial court denied the motion to compel arbitration because of the class-action waiver provision, relying on *Fisher v. DCH Temecula Imports LLC* (2010) 187 Cal.App.4th 601, which, in turn, relied on *Discover Bank v. Superior Court* (2005) 36 Cal.4th 148 (*Discover Bank*). (Opn. at 10; AA 529-530.) The trial court did not reach unconscionability or severability. (AA 527-530; Rehearing Petn. at 10-11.)

F. The Court Of Appeal Affirms On A Different Ground: Unconscionability.

In the wake of *Concepcion, supra*, 131 S.Ct. 1740, which overruled *Discover Bank, supra*, 36 Cal.4th 148, the Court of Appeal did not address the trial court's class-action waiver ground. Instead, it affirmed on a different ground: unconscionability. (Opn. at 11.)

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[6] The trial court sustained an objection to plaintiff's declaration that he was told to "just sign here"; it overruled the remaining evidentiary objections. (See AA 454-462, 528.)

Concepcion. The Court of Appeal read *Concepcion* as limited to the application of the unconscionability doctrine "'to *class-action waivers* in arbitration agreements'" and to states "'[r]equiring the availability of *classwide arbitration* . . . .'" (Opn. at 12, quoting *Concepcion*, 131 S.Ct. at pp. 1746 & 1748, italics added by Court of Appeal.) According to the Court of Appeal, "[w]ith the exception of the *Discover Bank* rule, the court acknowledged in *Concepcion* that the doctrine of unconscionability remains a basis for invalidating arbitration provisions." (Opn. at 12.) Thus, in the Court of Appeal's view, *Concepcion* merely carved out one, narrow exception – class-action waivers – to states' broad unconscionability powers to refuse to enforce arbitration provisions.

The De Novo Appellate Unconscionability Determination. The Court of Appeal proceeded to analyze the arbitration agreement, de novo, for unconscionability. It held that it could "resolve [unconscionability] in the first instance, without remand to the trial court." (Opn. at 10.) It reasoned that "[w]hether an arbitration provision is unconscionable is ultimately a question of law. . . . On appeal, when the extrinsic evidence is undisputed, as it is here, we review the contract de novo to determine unconscionability." (Opn. at 10, internal quotation marks and citations omitted.) The Court of Appeal viewed as undisputed plaintiff's bare assertion that he had not read the contract or been aware of the arbitration provision, despite the conflicting representation in the contract itself that immediately preceded his signature. (See Rehearing Petn. at 11.)

Procedural Unconscionability. The Court of Appeal majority found procedural unconscionability *as a matter of law* premised upon the facts that (1) the contract was long, (2) the plaintiff claimed not to have read the agreement that he signed, and (3) the front-of-the-form, large, all-capital-letters reference to the arbitration provision (in a distinctive box on the back of the form) is to the right of the "no cooling off period" box, immediately over any co-buyer's signature. (Opn. at 15-18.)

Substantive Unconscionability. The Court of Appeal majority found the arbitration provision was overly harsh or one-sided and for that reason substantively unconscionable. Specifically, the majority found fault with clauses (1) allowing either party to request review before a three arbitrator panel if the award exceeded $100,000, was for $0, or included injunctive relief, (2) requiring any party so requesting to advance the initial cost of the second round without a mechanism for waiving such fees, and (3) excluding *self*-help remedies (in particular, repossession) from arbitration. (Opn. at 18-30.) The Court of Appeal further found the provision unconscionable in requiring arbitration of Consumers Legal Remedies Act injunctive relief claims. (Opn. at 28-30.)

Severance. Finally, the Court of Appeal majority held that it could determine de novo that the supposedly offending clauses could not be severed. It recognized that severance is within the trial court's discretion such that the appellate court "typically would remand the case to the trial court, allowing it, as a discretionary matter, to decide whether the doctrine of severability should apply." (Opn. at 32, citing *Armendariz v. Foundation*

Health Psychcare Services, Inc. (2000) 24 Cal.4th 83, 122, 124 (*Armendariz*).) Concluding that "it would be pointless to remand the case when only one outcome is proper" (Opn. at 32), the majority viewed it as impossible to strike the offending clauses in the arbitration provision. It reasoned that, to be valid, any arbitration agreement must "establish a procedure or criteria for determining how much [a consumer] can afford" before admitting even the hypothetical prospect that the consumer may bear arbitration fees. (Opn. at 31.)

The Concurring Opinion. Justice Rothschild concurred. She found procedural unconscionability, more broadly than the majority, based solely on her conclusion that the sale agreement was a contract of adhesion. (Opn., conc. opn. of Rothschild, J. at 1.) On the other hand, she limited the substantive unconscionability bases to her view that "(1) the provision making monetary awards of exactly $0 or more than $100,000 appealable is unfairly one-sided; and (2) the provision requiring the appealing party to advance all costs of the appeal is unfairly one-sided." (*Ibid.*)[7]

This Court granted review.

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[7] The Court of Appeal denied petitioner's rehearing petition but granted rehearing on its own motion, modifying its original opinion in multiple respects not material here.

ARGUMENT

I. *AT&T Mobility v. Concepcion* (2011) 563 U.S. ___ [131 S.Ct. 1740], Limits The Use Of Unconscionability To Bar Enforcement Of Arbitration Provisions.

A. The Federal Arbitration Act Preempts State Law Refusals To Enforce Arbitration Based On Findings That The Parties' Agreed-Upon Arbitral Process Is Inadequate.

In *Concepcion*, *supra*, 131 S.Ct.1740, the United States Supreme Court disapproved judicial vetting, under the guise of unconscionability, of the parties' agreed-upon arbitration procedures. *Concepcion* specifically disapproved *Discover Bank*, *supra*, 36 Cal.4th 148, which had held unenforceably unconscionable an arbitration provision with a class action arbitration waiver. *Concepcion* holds that even if a particular arbitral process agreed upon by the parties and reasonably tailored to the type of dispute would otherwise be unenforceable under state law – either directly by statute or indirectly through doctrines such as unconscionability – the FAA preempts and requires enforcement of the arbitration agreement according to its terms. (131 S.Ct. at pp. 1749, 1753.)

Specifically:

- "[P]arties [have] discretion in designing arbitration processes . . . to allow for efficient, streamlined procedures tailored to the type of dispute." (131 S.Ct. at p. 1749.) Courts cannot use substantive unconscionability as a mechanism to refuse to enforce arbitration provisions based on the process agreed upon by the parties. (See *id.* at p. 1747, citing

Broome, *An Unconscionable Application of the Unconscionability Doctrine: How the California Courts are Circumventing the Federal Arbitration Act* (2006) 3 Hastings Bus. L.J. 39 [arguing that California courts have violated the FAA by historically applying heightened unconscionability review to processes selected in arbitration provisions, including a mutuality requirement not applied in the non-arbitration context].)

- At a minimum, there must be a strong presumption that the particular procedures agreed to by the parties are to be honored. (See 131 S.Ct. at pp. 1748-1749.) "The 'principal purpose' of the FAA is to 'ensur[e] that private arbitration agreements are enforced *according to their terms*.' [Citations.] . . ." (*Ibid.*, emphasis added.)

- Accordingly, "parties may agree to *limit the issues subject to arbitration*, [citation], *to arbitrate according to specific rules*, [citation], and to limit *with whom* a party will arbitrate its disputes, [citation]." (*Ibid.*, emphasis added.)

- In particular, the parties may limit the risks associated with outlier results or "high stakes" arbitral determinations. (*Id.* at p. 1748 [parties may exclude class actions from arbitration because the higher stakes involved are not appropriate for arbitration].) They may account for the fact that "[a]rbitration is poorly suited to the higher stakes . . . litigation." (*Id.* at p. 1752.)

At the same time, *Concepcion* recognized that the FAA's "saving clause permits agreements to arbitrate to be invalidated by 'generally

applicable contract defenses, such as fraud, duress, or unconscionability,' . . ." (*Concepcion*, *supra*, 131 S.Ct. at p. 1746, citations omitted.) And, state courts must apply the *same* unconscionability principles to arbitration provisions that they apply to all other contracts. (*Id.* at pp. 1746-1747.) Even then, though, such "defenses [may not] apply only to arbitration or . . . derive their meaning from the fact that an agreement to arbitrate is at issue." (*Id.* at p. 1746.)

Concepcion, thus, is clear that, absent exceptional circumstances, states – either judicially or legislatively – may not, under the guise of unconscionability, judge the supposed fairness of the parties' agreed arbitration *process*. (See *id.* at p. 1747 [providing examples of arbitration-process "unconscionability" evaluations (ranging from discovery to evidentiary requirements) that the FAA precludes]; see *ibid.* [parties properly should be allowed to tailor arbitration to nature of likely disputes and to alleviate arbitration risks]; *Graham v. Scissor-Tail, Inc.* (1981) 28 Cal.3d 807, 824 (*Graham*) [California's Arbitration Act "expressly recognizes the right of contractual parties to provide for the resolution of contractual disputes *by arbitral machinery of their own design and composition*," emphasis added].)

Nor can courts second-guess the parties' attempts to lessen the impact of outlier results. Parties may exclude "higher stakes" disputes and issues – such as embodied in class actions – from the arbitral universe. (131 S.Ct. at pp. 1748, 1752.)

Concepcion necessarily affirms this Court's view in *Graham*, *supra*, 28 Cal.3d at pp. 824-825, that one party's ability to sometimes obtain tactical advantage from the way an arbitration provision is structured does *not* suffice to find unconscionability. If it were otherwise, *Concepcion*'s outcome would have been different. (See *Concepcion*, *supra*, 131 S.Ct. at p. 1753 [rejecting dissent's reliance on need to balance tactical position of consumers seeking redress of small-dollar claims via class actions as sufficient basis to justify overriding arbitration term excluding such claims].)

After *Concepcion*, the extraordinary circumstances that would allow a state to refuse to enforce contractual arbitration on unconscionability grounds are limited. The standard is a simple one: A provision might be unenforceably unconscionable only if it bears no rational relationship to the anticipated disputes such that no reasonable person would have agreed to it absent coercion. (See *Hume v. United States* (1889) 132 U.S. 406, 406 [defining an unconscionable contract as one "'which no man in his senses, not under delusion, would make, on the one hand, and which no fair and honest man would accept on the other,'" citation omitted].) In such a case, it might be said that the parties did not exercise "discretion in designing arbitration processes . . . tailored to the type of dispute." (131 S.Ct. at p. 1749.) Put another way, the line is where the possibility of a fair adjudication becomes "illusory." (*Graham*, *supra*, 28 Cal.3d at pp. 823-825 [although parties may "designat[e] as arbitrator a person or entity who, by reason of relationship to a party or some similar factor, can be expected to

adopt something other than a 'neutral' stance in determining dispute," provision in required musician union contract designating union as sole arbiter of disputes between union musicians and promoters created an "illusory" process], citing *Matter of Cross & Brown Co.* (1957) 4 A.D.2d 501, 167 N.Y.S.2d 573.)

Such irrationality might be evidenced if the agreed upon arbitration process is wholly disconnected from the nature of expected disputes, i.e., the procedure is *not* a "streamlined procedure[] *tailored to the type of dispute*" reasonably anticipated (*Concepcion, supra*, 131 S.Ct. at p. 1749, emphasis added) or if it affords remedies *not rationally related* to the breach (see *Advanced Micro Devices, Inc. v. Intel Corp.* (1994) 9 Cal.4th 362). But short of such a threshold, the "fairness" of the arbitration process and procedures set out in an arbitration provision – the subject disputes, which parties will be allowed, how the disputes are to be determined and by whom – are not a basis to refuse enforcement. (*Concepcion, supra*, 131 S.Ct. at pp. 1747-1749; see *Graham, supra*, 28 Cal.3d at pp. 823-825 [to be enforceable arbitral process need not be scrupulously evenhanded].)

Arbitration is an *alternative* to litigation, not a doppelganger for it. This Court recognized that reality long ago. (*Graham, supra*, 28 Cal.3d at pp. 823-825 [arbitrators may have conflicts of interest that would be inappropriate for judicial officers].) Imposing the restrictions, requirements and the process of litigation on the arbitration process would fundamentally alter the latter's nature, something that the FAA precludes. (See *Concepcion, supra*, 131 S.Ct. at p. 1747 [unconscionability defense *cannot*

be premised on the alternative, nonlitigation nature of arbitration].) As an *alternative* to litigation, arbitration provides many benefits to both disputants (e.g., economy, speed, certainty) and to the public (e.g., relieving overburdened and underfunded courts), even if under a more "rough justice" standard. But those advantages disappear the more that states require arbitration to look like litigation.

Concepcion has undoubtedly changed the playing field (or, in California, returned it to the *Graham* standard) regarding unconscionability attacks. Courts cannot refuse to enforce arbitration provisions deemed unconscionable for setting forth a unique process that differs from normal litigation standards, even if that process is perceived to favor one side more than another.

B. *Concepcion* Is Not Limited To Class Action Arbitration Waivers.

The Court of Appeal's answer to *Concepcion* was to ignore it by claiming that *Concepcion* was limited to class action arbitration waivers (and to some undefined "judicially imposed procedure[s] . . . inconsistent with . . . the purposes of the Federal Arbitration Act"). (Opn. at 14.) It read *Concepcion* as not affecting arbitral substantive unconscionability analysis generally, even when that analysis is premised on the challenged provision's characteristics as an agreed-upon arbitration process. (Opn. at 13-14.)

That reading is unsupportable. Nothing in *Concepcion* limits its holding to a particular type of arbitration clause. Nothing in its rationale is specific to class action waivers. Rather, its language (quoted in section A. above) is general and sweeping.

Not surprisingly, the Ninth Circuit has declined to read *Concepcion* as limited to class action waiver provisions. *Kilgore v. KeyBank, Nat. Assn.* (9th Cir. 2012) 673 F.3d 947, holds that *Concepcion*'s necessary import is that the inclusion of injunctive relief among the issues to be arbitrated, "unconscionable" or not, cannot be a basis to refuse to enforce arbitration. And, *Concepcion* applies to more than just class-action waivers and injunctive relief. (E.g., *James v. Conceptus, Inc.* (S.D. Tex., Mar. 12, 2012, No. H-11-1183) __ F.Supp.2d ___ [2012 WL 845122] at pp. *8, *11-*15 [*Concepcion* limits this Court's decision in *Armendariz, supra*, 24 Cal.4th 83; applying California unconscionability doctrine "post-*Concepcion*" to find enforceable forum-selection provision in arbitration clause, rejecting more restrictive pre-*Concepcion* case law]; *Grabowski v. C.H. Robinson* (S.D. Cal. 2011) 817 F.Supp.2d 1159, 1171, fn. 1 [*Armendariz* and other "pre-*Concepcion* cases applying California unconscionability law must be read in light of *Concepcion*"].)

Indeed, the United States Supreme Court itself has recognized that *Concepcion*'s limitation on unconscionability as a ground to refuse to enforce arbitration is not restricted to class-action waiver provisions. It granted certiorari, vacated and remanded this Court's decision in *Sonic-Calabasas A, Inc. v. Moreno*, a case *not* involving a class action arbitration

waiver, for reconsideration in light of *Concepcion*. (*Sonic-Calabasas A, Inc. v. Moreno* (2011) ___ U.S. ___, 132 S.Ct. 496, vacating *Sonic–Calabasas A, Inc. v. Moreno* (2011) 51 Cal.4th 659; see also *In Re Checking Account Overdraft Litigation* (11th Cir. 2012) 674 F.3d 1252 [remanding for district court "to reconsider its unconscionability determination in light of *Concepcion*"][8].) Likewise, in *Marmet Health Care Center v. Brown* (2012) (*per curiam*) 565 U.S. ___ [132 S.Ct. 1201, 182 L.Ed. 42], a case that also appeared to have *no* class action waiver issue, the Supreme Court remanded the unconscionability issue to the West Virginia Supreme Court to "consider whether . . . the arbitration clauses [at issue] are unenforceable under state common law principles *that are not specific to arbitration* and [thereby] preempted by the FAA." (Emphasis added.)

Concepcion cannot be plausibly limited to exclusions of class actions from arbitration.

C. *Concepcion* Bars State Courts From Prohibiting The Arbitration Of Injunctive Relief Claims.

Citing *Broughton v. Cigna Healthplans of Cal.*, *supra*, 21 Cal.4th 1066, the Court of Appeal majority held the arbitration provision here was substantively unconscionable because "the requirement that the buyer seek

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[8] This was the second remand in *In Re Checking Account Overdraft Litigation*. It came after the district court found unconscionability based on *other than* the arbitral class-action waiver provision. (See Order Denying Renewed Motions to Compel Arbitration, *In re Checking Account Overdraft Litigation* (S.D. Fla., Sep. 1, 2011) Case No. 09-MD-02036-JLK, Dock. 1853.)

injunctive relief from the arbitrator is inconsistent with the [California Legal Remedies Act]." (Opn. at 28; *id.* at 28-30.) But after *Concepcion*, *Broughton* is no longer good law. *Concepcion*, thus, negates one of the central tenets of the Court of Appeal majority's opinion.

Kilgore v. KeyBank, Nat. Ass'n, *supra*, 673 F.3d at pp. 951, 960, directly so holds: "[W]e consider whether, in light of the Supreme Court's recent decision in [*Concepcion*], the Federal Arbitration Act . . . preempts California's state law rule prohibiting the arbitration of claims for broad, public injunctive relief—a rule established in *Broughton v. Cigna Healthplans of California*, 21 Cal.4th 1066 (1999) and *Cruz v. PacifiCare Health Systems, Inc.*, 30 Cal.4th 303 (2003). . . . We hold that the *Broughton–Cruz* rule does not survive *Concepcion* because the rule 'prohibits outright the arbitration of a particular type of claim'—claims for broad public injunctive relief. *Concepcion*, 131 S.Ct. at 1747."

The Court of Appeal majority sought to hedge its bets regarding *Broughton-Cruz*'s continued viability, by suggesting that even if that authority does not survive *Concepcion* (as just demonstrated), it affords a more general public policy basis for finding substantive unconscionability. But the United States Supreme Court has rejected such sleight of hand. *Marmet Health Care Center v. Brown*, *supra*, 565 U.S. ___ [132 S.Ct. 1201, 182 L.Ed.2d 42], held a state cannot transform into a public policy rationale for finding substantive unconscionability an arbitration-specific policy that it cannot directly apply. The West Virginia Supreme Court had found (1) that state law categorically barred predispute arbitration

agreements for nursing home personal injury claims, and alternatively, (2) that "arbitration clauses [were] unconscionable in part because a predispute arbitration agreement that applies to claims of personal injury or wrongful death against nursing homes 'clearly violates public policy.'" (132 S.Ct. at p. 1204.) The United States Supreme Court held that the categorical bar to predispute arbitration agreements violated the FAA. But it went further. It refused to uphold the alternative unconscionability holding because "[i]t [was] unclear . . . to what degree the state court's alternative holding was influenced by the invalid, categorical . . . rule against predispute arbitration agreements." (*Ibid.*) Thus, what a state cannot bar directly in an arbitration provision, it cannot use as a factor to deny arbitration on substantive unconscionability grounds. Yet, that is what the Court of Appeal majority did here.

Under *Concepcion*, the inclusion of injunctive relief within the issues to be arbitrated cannot be a basis, either directly *or indirectly*, to deny enforcement of an arbitration provision. The FAA would bar states from refusing enforcement on unconscionability grounds.

D. Under *Concepcion*, The Arbitration Provision Here Is Enforceable.

The Court of Appeal here, in declining to enforce arbitration, dissected the agreed-upon arbitration procedures to determine if some circumstance might theoretically exist whereby the party opposing arbitration might be at a tactical disadvantage. That is exactly what

Concepcion holds that states (either statutorily or judicially) cannot do.[9] Rather, as discussed above, the inquiry must be limited to whether the agreed upon arbitration process was tailored to the nature of likely disputes or was somehow outside the range of possibilities to which a reasonable person might agree absent undue coercion. Under that standard, the arbitration provision here must be enforced.

The arbitration process cannot be a basis to not enforce. To begin with, the arbitration provision here affects only *the process* – how disputes are to be resolved. It does *not* purport to affect either party's substantive rights (e.g., what damages might be recovered) in *any* way.[10] Even when additional review is provided for outlier results, the process remains an arbitral one, just with three arbitrators instead of a single arbitrator. And the mechanism for additional arbitration review applies to awards for and against both buyers and the dealer.

The agreed-upon process is tailored to typical disputes, with additional review limited to outlier results. The arbitration process is *tailored* to the types of disputes likely to arise. This is a provision in an

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[9] See Petersen & Anderson, *The California Court of Appeal Disagrees With The U.S. Supreme Court On The Enforceability of Arbitration Agreements*, Class Action Defense Strategy Blog (Nov. 2, 2011) <http://documents.jdsupra.com/5dd8091d-b120-4ef9-a1dd-a64d54572ec9.pdf> (as of May 16, 2012) [criticizing Court of Appeal decision in this case as a return to the micro-management process that *Concepcion* rejects].)

[10] That is not to say that a contractual arbitration clause may never restrict available remedies. It can sometimes. (See *Htay Htay Chin v. Advanced Fresh Concepts Franchise Corp.* (2011) 194 Cal.App.4th 704, 712 (*Htay Htay Chin*).) But that issue is not present here.

automobile sales contract. Arbitration awards between $0 and $100,000 are final and fully enforceable after a single arbiter's award. In automobile purchase disputes that is the vast majority of cases, as the average new car purchase price is under $30,000.[11] Additional *arbitral* review by a three-person panel is provided for specific outlier results – those awarding nothing, more than $100,000, or injunctive relief (e.g., directing the buyer to surrender the vehicle if there has been no repossession, directing the dealer to change its operational methods). The $0, $100,000 and injunctive relief triggers define *outlier* results, not typical ones.

The agreed-upon mechanism is, thus, a "streamlined procedure[] *tailored to the type of dispute*" and to the risks to the parties of outlier results. (See *Concepcion*, 131 S.Ct. at pp. 1749 [parties can tailor process to type of dispute], 1752 [parties can recognize and adjust for the fact that arbitration is not particularly well suited for high stakes determinations].)

The process is tailored to the business realities of the contracting parties. Buyers who take a case all the way through arbitration and receive an award of $0 would likely consider that an outlier and would desire a second level of review. Likewise, buyers who are subject to injunctions – requiring them to return a car, for example, or refrain from certain activities – would also desire a second level of review. On the other end of the spectrum, awards exceeding $100,000 – far outside the price of most new cars – or for injunctive relief requiring dealer operational changes

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[11] Snavely, *Prices of Cars Sold Up, Average $29,217; Detroit Cuts Incentives* (July 12, 2010) USA Today <http://www.usatoday.com/money/autos/2010-07-12-carprices12_ST_N.htm> (as of May 16, 2012)

potentially affect the dealer's entire business, going far beyond a particular transaction. Nationally, over the past several years average dealership profits have ranged from roughly $277,000 to $642,000 and net worths have ranged between $2.2 million and $2.6 million.[12] Awards exceeding $100,000 are material, and even life-threatening, to businesses of that size.

Under *Concepcion*, parties are free to exclude problematic types of claims from arbitration. An arbitration provision must be enforced even though tailoring the arbitration process means that parties can exclude certain types of claims from arbitration altogether. In *Concepcion*, it was class-wide claims that were excluded. Here, it is self-help remedies and small claims court amounts. Just as excluding class actions made sense in *Concepcion* due to the high stakes nature of such claims, excluding self-help and small claims court issues made sense here. The first do not use a judicial process, so there is no reason to include them in the arbitration alternative; and the second have their own, already low-cost, streamlined process. The ability to limit the types of claims to be arbitrated is the heart of *Concepcion*'s holding.

A reasonable person might well agree to the balanced arbitration provision. The arbitration process *as a whole* is something to which a reasonable person might agree. There is a balance of clauses. There is an opportunity for further arbitral scrutiny for outlier results. But given the

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[12] See *NADADATA 2011 State of the Industry Report*, at p. 3, NADA (2011) <http://www.nada.org/NR/rdonlyres/ 0798BE2A-9291-44BF-A126-0D372FC89B8A/0/ NADA_DATA_ 08222011.pdf> (as of May 16, 2012).

nature of the disputes, that will be the exception, not the rule. And, further review works both ways; both buyers and dealers can seek review of outlier awards. *Self*-help remedies, such as repossession, that would be more often invoked by the dealer are excluded, but they are by definition outside even the litigation process; and comparable small-claims remedies more likely invoked by the customer are also excluded.

Finally, the dealer pays the buyer's initial arbitration expenses, up to $2,500. Only if the buyer loses a first round and wants to seek further arbitral review does the buyer have to advance further arbitration expenses (the review arbitrators ultimately allocate expenses). That's reasonable: That the party (buyer *or* dealer) losing the first round has to bear the expense of the finality round is common sense and furthers the interests of formality. Indeed, that's how the judicial system handles appeals – the appellant pays for the record on appeal and pays a higher fee than the respondent.[13]

And, in return, individuals get a speedy, cheaper, surer mechanism for resolving disputes.

Under United States Supreme Court precedent, speculation about an ability to pay for a second-round arbitration cannot be a basis to refuse enforcement. That leaves the Court of Appeal's speculative complaint that in some – unidentified – instance a car buyer (here of a $50,000 luxury automobile) *might* be unable to afford second-round arbitral

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[13] Until recent budgetary constraints forced a search for additional court-system revenue, the appellant bore *all* of the appeal filing fees.

review. The United States Supreme Court has decisively rejected just such reasoning as a basis to excuse enforcing arbitration. In *Green Tree Financial Corp.-Alabama v. Randolph* (2000) 531 U.S. 79, 91, the Court addressed the hypothetical claim that some party sometime might not be able to afford arbitration costs (there the costs of an *initial*, first round): "The 'risk' that [the party] will be saddled with prohibitive costs is too speculative to justify the invalidation of an arbitration agreement." Absent an evidentiary showing (*not* made here) that *this* party will suffer prohibitive costs, speculation about such costs cannot justify refusing to enforce a federally protected arbitration provision. Nor can such a showing even be imagined where the issue is not the costs of the original arbitration – an arbitration that is going to finally and conclusively resolve most disputes – but only those of a second round review in the event that the party in question loses the first round.

* * *

Concepcion requires enforcing all the clauses with which the Court of Appeal majority found fault – (1) the potential for a party aggrieved by a $100,000 single arbitrator award (as well as by a $0 such award) to seek a three arbitrator panel review, (2) the potential for a party aggrieved by a single arbitrator injunctive award to similarly obtain such review, (3) the party seeking second-round arbitral review having to advance the additional arbitration expenses, at least without a mechanism for waiving such expenses, and (4) the exclusion of self-help remedies from arbitration (Opn. at 18-19). As conclusively construed by *Concepcion*, the FAA precludes

refusing to enforce the arbitration provision here on unconscionability grounds.[14]

II. In Any Event, The Arbitration Provision Here Is Properly Enforceable Under Standard California Unconscionability Principles.

Even without FAA preemption, the arbitration provision is fully enforceable under California law. As a defense to an indisputably executed arbitration agreement, plaintiff bore the unconscionability burden of proof. (*Htay Htay Chin*, *supra*, 194 Cal.App.4th at p. 708; *Szetela v. Discover Bank* (2002) 97 Cal.App.4th 1094, 1099.)

In California, a finding of unconscionability requires both substantive *and* procedural unconscionability elements. (*Armendariz*, *supra*, 24 Cal.4th at p. 114.) Neither is present here, and certainly not in a sufficient quantum to justify nonenforcement.

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[14] Necessarily, *Concepcion* equally defeats concurring Justice Rothschild's view that arbitration could be refused based on unconscionability solely as to clauses (1) and (4).

A. Substantive Unconscionability Must And Does Require More Than Amorphous, Subjective Fairness Reactions; It Requires An Objective Complete Lack Of Business Justification.

1. California law and public policy require an objective unconscionability standard.

The Court of Appeal found the arbitration provision here was substantively unconscionable because, upon dissection, the majority viewed isolated clauses to be "harsh terms that are one-sided in favor of the car dealer to the detriment of the buyer." (Opn. at 11; see also Opn. at 14.) Relying on *Armendariz, supra*, 24 Cal.4th at p. 114, the majority formulated the unconscionability test simply as a judicial determination of potentially "'overly harsh' or 'one sided' results." (Opn. at 12.) The majority applied these terms as a subjective test – any provision that the court views as unfair in some sense could be deemed unconscionable. The subjective nature of the test as applied is further demonstrated by the concurring opinion, which agreed as to general unfairness of some terms, but not others.

But what is required (and as discussed in section A.2., below, what this Court's precedent mandates) is an *objective* standard. Indeed, it can only be such as the substantive unconscionability question ultimately is one of law, not individual judicial discretion. (Civ. Code, § 1670.5; *Parada v. Superior Court* (2009) 176 Cal.App.4th 1554, 1567-1568.) That is consistent with the rule that objective, not subjective, standards govern contracts. (E.g., *Patel v. Liebermensch* (2008) 45 Cal.4th 344, 352 ["The

terms of the contract are determinable by an external, not by an internal standard—or by what has been termed the objective rather than the subjective test," citation omitted].)

California public policy likewise requires an objective test. Judicial officers "'may not simply impose their own notions of the day as to what is fair or unfair.'" (*Morris v. Redwood Empire Bancorp* (2005) 128 Cal.App.4th 1305, 1316 (*Morris*) [unconscionability determination] quoting and analogizing to *Cel-Tech Communications, Inc. v. L.A. Cellular Telephone Co.* (1999) 20 Cal.4th 163, 182 (*Cel-Tech*) [unfair competition determination].) "'An undefined standard of what is 'unfair' fails to give business adequate guidelines as to what conduct may be challenged and thus enjoined and may sanction arbitrary or unpredictable decisions about what is fair or unfair.'" (*Morris*, *supra*, at pp. 1316-1317, quoting *Cel-Tech*, *supra*, at p. 185.) Rather, "fairness" must be measured by *objective* criteria. (*Cel-Tech*, *supra*, at pp. 185-186 [unfair competition law]; see *Morris*, *supra*, at p. 1316 [*Cel-Tech* involved "an analogous context" to unconscionability].)

The amorphous "fairness" standard that the Court of Appeal applied here violates this norm. It reduces substantive unconscionability to a subjective, shifting standard that varies from judge to judge depending on personal views as to what seems "unfair" or "harsh." It deprives businesses of the reasonable guidelines needed to determine in advance the likely enforceability of arbitration provisions – provisions that are often key to helping businesses reduce and anticipate their litigation costs and to

establish prices. And, it impermissibly "'sanction[s] arbitrary or unpredictable decisions about what is fair or unfair.'" (*Morris*, *supra*, 128 Cal.App.4th at p. 1317, quoting *Cel-Tech*, *supra*, 20 Cal.4th at. p. 185.)

This case exemplifies the problem: The majority and concurring justices reached different conclusions as to what might be unfair or overly harsh. Both conflict with at least one other Court of Appeal that has construed the same provision. (*Arguelles-Romero v. Superior Court* (2010) 184 Cal.App.4th 825, 832, fn. 4, 845, fn. 21.) A subjective fairness standard is no standard at all. Predictability for parties drafting and signing arbitration agreements and consistency of decision amongst cases requires an *objective* standard. Fortunately, as we now discuss, California precedent mandates just such an objective standard – the absence of any legitimate business justification.

2. Properly construed, unconscionability exists only when a provision lacks *any* reasonable business justification.

In stating its amorphous, subjective standard of "harsh terms that are one-sided in favor of the car dealer to the detriment of the buyer" or "'overly harsh' or 'one sided' results" (Opn. at 11, 12, 14), the Court of Appeal relied on *Armendariz*, *supra*, 24 Cal.4th at p. 114 (Opn. at 12). But *Armendariz* does not hold that perceived "one-sidedness," standing alone, renders an arbitration provision substantively unconscionable. It sets forth an *objective* test – lack of *any* commercially reasonable business

justification. It recognizes that "'unconscionability turns not only on a 'one-sided' result, but also on *an absence of 'justification' for it.*'" (*Armendariz, supra*, 24 Cal.4th at pp. 117-118, emphasis added, quoting *A & M Produce Co. v. FMC Corp.* (1982) 135 Cal.App.3d 473, 487 (*A & M Produce*).) "'[A] contract can provide a 'margin of safety' that provides the party with superior bargaining strength a type of extra protection for which it has a legitimate commercial need without being unconscionable.'" (*Armendariz*, at p. 117, quoting with approval, *Stirlen v. Supercuts, Inc.* (1997) 51 Cal.App.4th 1519, 1536.)

Accordingly, the operative question under *Armendariz* is whether the party with the superior bargaining strength "'has a legitimate commercial need'" or "business reality" for any challenged arbitration clause. (*Armendariz, supra*, 24 Cal.4th at pp. 116-117; see also Civ. Code, § 1670.5, Legislative Committee com. 1 [the principle of unconscionability "is one of the prevention of oppression and unfair surprise [citation] and *not of the disturbance of allocation of risks because of superior bargaining power*" (emphasis added)].)

"[A] contract is largely an allocation of risks between the parties." (*A & M Produce, supra*, 135 Cal.App.3d at p. 487, citations omitted, cited with approval in *Armendariz, supra*, 24 Cal.4th at pp. 114, 117-118.) There is a whole range of risk allocations that are, and should be, legally acceptable. They are reached through negotiation, trade-offs (e.g., between price and terms) and, yes, bargaining power. Only when the result is far outside the ballpark of negotiable risk allocations can it be deemed

unconscionable: A contractual provision is substantively unconscionable only if it "'reallocates risks in an *objectively* unreasonable or unexpected manner.'" (*Morris*, *supra*, 128 Cal.App.4th at p. 1317, citation omitted, italics added; see also *A & M Produce*, *supra*, 135 Cal.App.3d at p. 487, cited with approval in *Armendariz*, *supra*, 24 Cal.4th at pp. 114, 117-118.)

Only the absence of *any* business justification – after considering the pertinent commercial background and trade practices – *plus* the weaker party receiving nothing in exchange, can justify a court stepping in and negating the parties' agreed upon deal on the basis that the term in question is nothing more than an unconscionable penalty. (See, e.g., *A & M Produce*, *supra*, 135 Cal.App.3d at p. 493 [holding terms substantively unconscionable because they "result[ed] in allocation of commercial risks in a socially or economically unreasonable manner"]; *Stirlen*, *supra*, 51 Cal.App.4th at p. 1542 [arbitration terms were not justified by "any business reality" and were "'so extreme as to appear unconscionable *according to the mores and business practices of the time and place*'" (emphasis added), quoted with approval in *Armendariz*, *supra*, 24 Cal.4th at p. 117]; see also *id.* at p. 1531 [basic unconscionability test is "whether, *in the light of the general commercial background and the commercial needs of the particular trade or case*, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract," emphasis added].)

And, the standard necessarily goes *beyond* judicial determination of mere unreasonableness, it requires *the absence of any possible justification*:

> "Basing an unconscionability determination on the reasonableness of a contract provision would inject *an inappropriate level of judicial subjectivity into the analysis.* 'With a concept as nebulous as "unconscionability" it is important that courts not be thrust in the paternalistic role of intervening to change contractual terms that the parties have agreed to merely because the court believes the terms are unreasonable . . . .'"

(*Morris*, *supra*, 128 Cal.App.4th at pp. 1322-1323, emphasis added.) To be substantively unconscionable, a provision must be "such an extreme departure from common business practice, and so one-sided as to 'shock the conscience.'" (*Belton v. Comcast Cable Holdings, LLC* (2007) 151 Cal.App.4th 1224, 1247; see also *Young Seok Suh v. Superior Court* (2010) 181 Cal.App.4th 1504, 1515 [substantive unconscionability focuses on whether the agreement's actual terms "create such 'overly harsh' or 'one-sided' results *as to 'shock the conscience*,'" emphasis added, internal quotation marks omitted]; *Morris*, *supra*, 128 Cal.App.4th at p. 1323; *Marin Storage & Trucking, Inc. v. Benco Contracting and Engineering, Inc.* (2001) 89 Cal.App.4th 1042, 1055 [the terms must be "*so* unreasonable, unjustified, or one-sided *as to shock the conscience*," emphasis added].)

And, "the conscience" to be shocked is not a judge's individual, subjective conscience, it is the collective *legal* conscience, i.e., that which

no reasonable person could find justifiable. Unconscionability requires more than just terms that may favor the party with the superior bargaining power: It requires "'a contract which no man in his senses, not under delusion, would make, on the one hand, and which no fair and honest man would accept on the other.'" (*Hume v. United States*, *supra*, 132 U.S. at p. 406.) That is the same standard that this Court effectively applied in *Armendariz* and the standard that should control unconscionability analysis of *any* contract term (arbitration or otherwise) in California.

3. The arbitration provision must be viewed as a whole and needs only demonstrate an *overall* "modicum of bilaterality."

In addition to ignoring the lack-of-any-business-justification standard, the Court of Appeal here distorted the substantive unconscionability test in another important way. It parsed through the arbitration provision picking out clauses that, when viewed *in isolation*, it believed favored the dealer (e.g., further review for awards over $100,000 or injunctive relief, party losing first-round arbitration initially bearing second-round costs, no arbitration of self-help remedies), but impermissibly ignoring the *balance* of provisions, including those favorable to the buyer (e.g., finality of awards of up to $100,000, further review of awards of $0, no arbitration of small-claims, dealer advances initial costs).

Yet contracts must be interpreted as a whole. (See Civ. Code, § 1641 ["The whole of a contract is to be taken together, so as to give effect

to every part, if reasonably practicable, each clause helping to interpret the other"]; *Woodside Homes of Cal., Inc. v. Superior Court* (2003) 107 Cal.App.4th 723, 734-735 [*mutual* waiver of jury trial meant reference provision was not unconscionable, even if inserted because "[b]usinesses prefer to have consumer cases heard by a neutral adjudicator because they expect that, year in and year out, the plaintiffs' recovery will be *less than juries would award*," original emphasis].) The issue must be the arbitration provision as a whole, not individual clauses.

Armendariz is illustrative. It invalidated an employer-drafted arbitration provision that required employees to arbitrate their claims (with onerous discovery and remedial limitations) but allowed the employer to pursue its claims in court. (24 Cal.4th at pp. 121-122.) It found that the provision lacked even a "*modicum* of bilaterality." (*Id.* at p. 117, emphasis added.) *Armendariz* found the provision "*unconscionably* unilateral" because there was no "*reasonable justification* for this lack of mutuality." (*Id.* at pp. 91, 118, emphasis added.) It reasoned that the employer should have been willing to submit its own claims to arbitration if the process was fair, and therefore the arbitration appeared "less as a forum for neutral dispute resolution and more as a means of maximizing employer advantage." (*Id.* at p. 118.)[15] The "unilateral arbitration agreement imposed by the employer *without reasonable justification* reflects the very

[15] As discussed above, at p. 19, there is at least some question whether even this holding survives *Concepcion*.

mistrust of arbitration that has been repudiated by the United States Supreme Court . . . ." (*Id.* at p. 120, emphasis added.)

But even then, *Armendariz* did not invalidate the arbitration agreement because it wasn't equally balanced. Rather, *Armendariz* based its holding on the fact that the agreement failed to meet a lesser threshold: it lacked even a "modicum of bilaterality" in the process *as a whole*. *Armendariz* did not approve a point-by-point dissection of the process searching for clauses that might tactically favor one party over the other. It made clear that bilaterality was not an absolute, but something to be measured as a "modicum" and against "reasonable justification."

Plaintiff and the Court of Appeal have expanded *Armendariz*'s "modicum of bilaterality" into a rule that every clause, every step in an arbitration provision, must benefit each participant equally. But that misreads *Armendariz*. *Armendariz* itself recognizes that a party with superior bargaining power is entitled to obtain "a 'margin of safety'" through "a type of extra protection for which it has a legitimate commercial need without being unconscionable.'" (*Armendariz*, at p. 117, quoting with approval, *Stirlen*, *supra*, 51 Cal.App.4th at p. 1536.)

That's a standard contract principle grounded in common sense. Lien rights or deeds of trust are not per se unconscionable. Yet, such contract provisions only benefit one party – the seller or lender. Paying the purchase price only benefits the seller and conveying title to property only benefits the buyer. But neither is unconscionable for being one-sided.

The same is true of an arbitration provision. There may be some aspects that benefit one party and some that benefit the other unequally. Even the arbitration provision as a whole may favor one particular party, without necessarily being unconscionable. (See *Graham*, *supra*, 28 Cal.3d at pp. 823-825 [contract can "designat[e] as arbitrator a person or entity who, by reason of relationship to a party or some similar factor, can be expected to adopt something other than a 'neutral' stance in determining disputes," without, by that reason alone, being unconscionable].) The arbitration provision is part of the overall deal struck by the parties, a deal which can include price, financing terms, and the like. Only where the arbitration provision, in context, can be viewed as an unjustified penalty in an otherwise wholly one-sided contract might it be thought to lack a modicum of bilaterality.

4. The provision must be viewed in its business context at the time it was entered.

In determining unconscionability, a court must consider a contract's "commercial setting, purpose, and effect." (Civ. Code, § 1670.5.) Here, the relevant setting and purpose are an automobile sales contract and the types of disputes that typically might arise out of such transactions. The provision here is tailored to that context. The parties do not have to plan in the sale agreement for every conceivable contingency or claim that might arise. They can adopt an arbitration process designed to handle the most likely types of disputes without fear that an unusual claim will defeat it.

Statutorily, unconscionability must be determined "at the time [the contract] was made . . . ." (*Ibid.*) Thus, the actually materialized dispute's specifics are *irrelevant.* "The critical juncture for determining whether a contract is unconscionable is the moment when it is entered into by both parties–not whether it is unconscionable in light of subsequent events." (*American Software, Inc. v. Ali* (1996) 46 Cal.App.4th 1386, 1391; accord, *Morris*, *supra*, 128 Cal.App.4th at p. 1324.) What matters is what types of disputes might reasonably be foreseen as most likely at the time the provision was entered. Here, the arbitration provision is tailored to just such foreseeable circumstances.

5. The subjective fairness test and strict mutuality requirement that the Court of Appeal imposed contravene governing unconscionability principles and are out of step with California's non-arbitration unconscionability jurisprudence.

The Court of Appeal distorted the above principles. It created an unconscionability standard premised on after-the-fact subjective fairness judgments, a strict mutuality of benefit requirement for every aspect of the agreed-upon arbitral process and an evaluation of outlier hypotheticals rather than likely disputes. These special rules do not reflect the standard unconscionability test. Rather, they single out arbitration provisions for special review and reflect hostility to arbitration.

The FAA and the "'liberal federal policy favoring arbitration'" that it embodies require that any unconscionability test applied to arbitration agreements be no more stringent than that applied to other contract provisions. (*Concepcion*, *supra*, 131 S.Ct. at pp. 1745-1746.) Any standard that makes substantive unconscionability determinations dependent on after-the-fact, subjective fairness assessments and strict mutuality requirements renders virtually every arbitration provision vulnerable to challenge and is far different from that applied to other contract terms.

Outside the arbitration context, California courts rarely find contract terms to be unconscionable. (See Broome, *An Unconscionable Application of the Unconscionability Doctrine: How the California Courts are Circumventing the Federal Arbitration Act*, *supra*, 3 Hastings Bus. L.J. at p. 54.) In the non-arbitration context, "the basis for a substantive unconscionability finding [in California] is normally limited to contractual terms that are: (1) clearly included in the contract by the superior bargaining party in an attempt *to appropriate from the weaker party something of substantial economic value*; *and* (2) *not justified by any legitimate business interest* of the superior bargaining party." (*Id.* at p. 54, emphasis added; see, e.g., *Carboni v. Arrospide* (1991) 2 Cal.App.4th 76, 80 [no legitimate business interest in 200% interest rate, which was ten times the prevailing rate]; *Ellis v. McKinnon Broadcasting Co.* (1993) 18 Cal.App.4th 1796, 1807 [provision limiting executive's commission on fees received post-termination was "a commercially unreasonable forfeiture clause, exacting a penalty far in excess of any potential detriment suffered by (the

employer)"].) In other words, California courts strike down non-arbitration provisions only when they are unsupported by any reasonable or plausible business justification and a party has effectively used its superior bargaining power to exact, not just a good deal, but a draconian economic penalty on the weaker party without conferring any benefit in return.

But California courts have *not* been applying that same approach to arbitration provisions. Later decisions, ostensibly purporting to follow *Armendariz*, have routinely invalidated arbitration provisions by stretching *Armendariz*'s "modicum of bilaterality" discussion into a strict mutuality requirement based on sweeping fairness considerations, essentially steam-rolling over any reasonable business justification that might exist. (See McGuinness & Karr, *California's "Unique" Approach To Arbitration: Why This Road Less Traveled Will Make All The Difference On The Issue Of Preemption Under The Federal Arbitration Act* (2005) 2005 J. Disp. Resol. 61, 90 ["Whether or not these contractual (arbitration) terms are 'unfair' in some general sense, they are a far cry from the overtly oppressive contracts traditionally policed by court under the doctrine of unconscionability—i.e., they do not 'shock the conscience'"]; *id.* at pp. 81-82 [California courts do not require strict mutuality outside the arbitration context]; Riske, *No Exceptions: How The Legitimate Business Justification For Unconscionability Only Further Demonstrates California Courts' Disdain For Arbitration Agreements* (2008) 2008 J. Disp. Resol. 591, 601-603 [California courts are applying erroneously strict mutuality concepts and disregarding legitimate business justifications]; Broome, *An*

Unconscionable Application of the Unconscionability Doctrine: How the California Courts Are Circumventing the Federal Arbitration Act, *supra*, 3 Hastings Bus. L.J. at pp. 41, 52-58 [same].)

The Court of Appeal's decision here falls into that same trap by effectively requiring strict mutuality among every individual clause. It is therefore wrong under *Armendariz* and violates the FAA's mandate that states apply the same unconscionability standards to arbitration provisions that they traditionally apply to non-arbitration cases.

B. Viewed Under The Correct Legal Standard, The Arbitration Provision Here Is Not Substantively Unconscionable.

1. The arbitration clauses are entirely lawful, viewed as a whole or individually.

Nothing about *this* arbitration provision can be deemed unconscionable when the correct legal standard is applied.

***The provision complies with Armendariz*:** The provision contains the "modicum of bilaterality" that *Armendariz* requires: Dealers and vehicle buyers must both arbitrate *all* their claims in a neutral forum, except for self-help remedies and claims that can be filed in small claims court. Small claims court is – like arbitration – a low-cost, expedited alternative to trial court litigation and generally favors consumers as it prohibits representation by lawyers and deals with the smaller-value claims consumers would be likely to bring. So that bilateral opt-out clause is

eminently reasonable. And *self*-help remedies are just that – *self*-help. They require no neutral arbiter, indeed, no third-party decisionmaker at all.

***There is no economic penalty*:** The arbitration provision does not exact any economic penalty on buyers. It does not shorten buyer's limitations period for filing claims. Nor does it limit the buyer's damages remedies. There are no caps on compensatory damages or punitive damage exclusions, and no restrictions on attorney fee awards.

***The clauses are facially even-handed and bilateral*:** The clauses are even-handed and in aggregate bilateral, particularly when construed collectively. Buyers and dealers *both* retain the right to seek remedies in small claims court and to use self-help remedies. *Both* have the right to seek further arbitration review of outlier, high-stakes results – awards of $0, those exceeding $100,000, or injunctive relief. If a losing party pursues such a new arbitration, *whichever* party lost below – the buyer or the dealer – advances the costs of the second proceeding subject to the arbitrator's final cost allocation. Indeed, the only facially unilateral provision – the dealer's obligation to cover the first $2,500 of the buyer's initial arbitration costs – favors *the buyer.*

***The provisions are bilateral in effect*:** In addition to facially applying to both sides, the arbitration provision also demonstrates bilateralism in its practical effect. Dealers would be more likely to pursue self-help remedies (repossession) outside arbitration, but buyers would be more likely to pursue small claims actions against dealerships where counsel is not allowed. Dealers may be more likely to use the second-level

of review for unusually large awards of more than $100,000 that could threaten their existence, but buyers would be more likely to use the second-level of review for awards of $0. And buyers will be more likely to benefit from the absolute finality of awards they obtain of under $100,000. Buyers may be more likely to file actions seeking injunctive relief against dealers, but both would benefit from a process that allows second-level review when their liberty is constrained by arbitral decisions requiring them to do or refrain from doing certain activities.

The provision is commercially-justified: As previously explained, most dealerships are medium-sized, family-owned businesses that need to prevent runaway litigation expenses. (See pp. 24-25 & fn. 12, above.) The arbitration provision is designed to ensure a neutral decision, while reserving a prompt "second look" by additional neutral arbitrators only for extreme, outlier decisions with business implications beyond the particular dispute. And although a dealer's responsibility for a buyer's initial arbitration costs is capped at $2,500, and a buyer might have to advance the costs of second-round review (subject to the arbitrators' discretion to later apportion fees), such limitations help balance subsidized buyer access to arbitration with discouraging a flood of non-meritorious, coercive claims.

2. Existing precedent rejects the Court of Appeal's rationale.

a. Additional arbitral review of outlier results.

In holding the right to three-arbitrator rearbitration of outlier results substantively unconscionable, the Court of Appeal purported to follow *Saika v. Gold* (1996) 49 Cal.App.4th 1074, and *Little v. Auto Stiegler, Inc.* (2003) 29 Cal.4th 1064 (*Little*). (See Opn. 20-22.) But both cases support *upholding* this arbitration provision.

- ***Saika v. Gold*:** A patient-physician arbitration agreement there authorized either party to request a trial de novo in superior court if an arbitration award exceeded $25,000. Concluding that arbitration awards in malpractice cases typically exceed $25,000, while doctors' claims against patients are typically lower, the court concluded that "the rejection clause meant the arbitration agreement really did not function as an *arbitration* agreement," rather it allowed the doctor to litigate while binding patients to arbitration results. (*Saika v. Gold*, *supra*, 49 Cal.App.4th at pp. 1080-1081, original italics.)

Saika v. Gold, thus, is merely an *Armendariz*-type, one-side-only arbitration agreement. Here, the dealers have no comparable ability to effectively always bypass the arbitration process and litigate in court. The *whole* process, even when there is second-level review, is arbitral.

Saika v. Gold is also inapposite because the court concluded that most malpractice awards will exceed the $25,000 threshold. Here, in contrast, the $100,000 threshold will rarely, if ever, be hit *by anyone*

(particularly since class actions are permissibly barred). The threshold here does not focus on common or likely results – it focuses on extreme, outlier results at both ends of the spectrum.

- ***Little*:** Unlike *Saika*, *Little* involved an appeal to a second arbitrator, not a trial de novo in court. But the arbitral appeal only applied to employer-employee arbitration awards exceeding $50,000, a threshold this Court concluded "inordinately benefits" the employer and for which the employer offered *no* justification whatsoever. (*Little*, *supra*, 29 Cal.4th at p. 1073.)

Here, in contrast, the provision is intended to apply to extreme, outlier results on *both* ends of the spectrum – $0 and over $100,000 – a provision that reasonably can be expected to disadvantage *either* side. (See *Htay Htay Chin*, *supra*, 194 Cal.App.4th at p. 713 [concluding that the franchisor reasonably justified a three-arbitrator threshold for claims exceeding $150,000 "as providing a measure of protection against exaggerated damage claims"].)

Not only did *Little* not prohibit outlier provisions, its analysis strongly suggests that the $50,000 threshold there was only unconscionable because there was no corresponding right to appeal a $0 award: "If the plaintiff and his or her attorney estimate that the potential value of his claim is substantial, and the arbitrator rules that the plaintiff *takes nothing* because of its erroneous understanding of a point of law, then it is rational for the

plaintiff to appeal" yet it has no such right. (*Little*, *supra*, 29 Cal.4th at p. 1073, italics added.) That right exists under the instant provision.[16]

b. Exclusion of self-help and small claims court remedies.

The Court of Appeal's treatment of the self-help and small claims court exclusions directly conflicts with *Arguelles-Romero v. Superior Court*, *supra*, 184 Cal.App.4th 825. Addressing the identical arbitration agreement (*id.* at p. 831, fn. 4), *Arguelles-Romero* held that excluding self-help remedies and small claims court actions was "clearly bilateral, and not unconscionable" (*id.* at p. 845, fn. 21). *Arguelles-Romero* got it right. Nothing about these exclusions shocks the conscience. (See *Htay Htay Chin*, *supra*, 194 Cal.App.4th at p. 712 [as a matter of law, arbitration provision not unconscionable in excluding injunctive and other provisional relief from arbitration].)

The Court of Appeal labeled the exclusion "oppressive" by comparing the exempted self-help repossession remedy (something to which only the dealer would resort) to arbitrable injunctive relief (which it labeled as the buyer's "comparable remedy"). (Opn. at 28.) But that mixes apples and oranges. Injunctive relief is not, nor is it comparable to, a self-

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[16] The arbitration provision in *Little* also provided for an appeal to a second arbitrator, not a de novo arbitration. An appealing employer would bear little risk as an arbitrator acting in appellate capacity would be unlikely to increase the award. (*Little*, *supra*, 29 Cal.4th at p. 1074.) That concern is absent here, because the agreement gives the appealing party "a new arbitration . . . by a three arbitration panel." (App. 279.)

help remedy. It's an important legal remedy imposed by a third party decisionmaker and enforceable using coercive judicial powers. Repossession, in contrast, is not a legal claim or continuing remedy at all – it's a one-shot *non-judicial* contractual right to retrieve a vehicle from a buyer who has failed to make required payments and could damage the dealer's property. Self-help remedies are outside the judicial system and therefore properly outside the arbitral one as well.

c. The losing party advances fees for additional arbitral review.

The agreement's cost provisions likewise are not even remotely unconscionable. The dealer pays for the initial arbitration (up to $2,500 for the buyer); if the dealer seeks a second arbitral review, it bears those costs too. The buyer bears such costs (and then only as an initial matter because the arbitrators can allocate costs) only if he or she loses the first round and wishes a new arbitration. That's hardly earth-shattering. That's how the fees are allocated in the judicial process when a losing party wants to appeal. (See also Code Civ. Proc., § 1284.2 [statutory default is that parties to arbitration each pay their pro rata share of expenses]; *Htay Htay Chin*, *supra*, 194 Cal.App.4th at p. 713 [cost of three arbitrator panel not prohibitive where limited to claims exceeding $150,000].)

The Court of Appeal nonetheless found it was unconscionable to require buyers – if they lost the first round and wanted a second shot before a three-arbitrator panel – to have to advance costs subject to subsequent

reallocation by the arbitrators. Why? Because a *hypothetical* buyer *might* lack the funds to make the advance payment and the arbitration agreement does not specify what should happen in that context. (Opn. at 27-28.)

That approach, as we explained earlier, violates the United States Supreme Court's mandate in *Green Tree Financial Corp.-Alabama Randolph*, *supra*, 531 U.S. at p. 91, that courts cannot invalidate arbitration agreements based on the speculative risk that someone *might* be saddled with prohibitive costs. (See pp. 26-27, above.)

The Court of Appeal ignored *Green Tree*, instead relying on *Gutierrez v. Autowest, Inc.* (2003) 114 Cal.App.4th 77. (Opn. at 26-28.) But that reliance was misplaced. In *Gutierrez*, it was undisputed (from *evidence* submitted to the trial court) that the plaintiffs could not pay the fees necessary to even *initiate* the arbitration proceeding. (114 Cal.App.4th at pp. 90-91 & fn. 13.)

In stark contrast, the plaintiff here – the buyer of a $50,000 automobile – is a presumptively *unlikely* candidate for fee exemption in any adjudicatory system, judicial or arbitral. If plaintiff wanted to claim poverty, he had the burden – as the party claiming unconscionability – to prove below that he would never be able to advance any fees if he ended up seeking rearbitration. And he needed to show that the inability existed at the time he signed the agreement for his expensive car. (Civ. Code, §1670.5 [contract's unconscionability must exist "at the time it was made"].)

Plaintiff cannot avoid arbitration based on what might hypothetically happen to someone else. Yet that's what the Court of Appeal relied on.

* * *

In sum, the provision here is not a dealer-imposed "heads I win, tails you lose" provision that will always favor the dealer. Properly analyzed, there is nothing substantively unconscionable about it.

C. There Is Nothing Procedurally Hidden About The Arbitration Provision Which Is Specifically Referenced Above One Of The Signature Lines On The Agreement's Face.

In addition to showing substantive unconscionability, it was plaintiff's burden to *also* establish procedural unconscionability. (*Armendariz*, *supra*, 24 Cal.4th at p. 114 [unconscionability requires both substantive and procedural elements]; *Htay Htay Chin*, *supra*, 194 Cal.App.4th at p. 708 [party asserting unconscionability bears burden of proof].) Here, there was no finding of any procedural impropriety beyond the face of the signed contract itself. (See section III. A., below.) Because procedural and substantive unconscionability are part of a sliding scale, the *amount* of proven procedural unconscionability is important: "[T]he more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa." (*Armendariz*, *supra*, 23 Cal.4th at p. 114.)

Procedural unconscionability requires that the circumstances of the transaction involve *unfair* surprise and oppression. (*Ibid.*)

Here, plaintiff failed to present substantial evidence that the circumstances of his transaction were so fraught with surprise and oppression as to render the agreement procedurally unconscionable. Plaintiff merely asserts he didn't read it. That evidence is disputed and the trial court never made any such finding. (See section III. A., below.) Nor would plaintiff's excuse suffice.

"Of course the mere fact that a contract term is not read or understood by the non-drafting party or that the drafting party occupies a superior bargaining position will not authorize a court to refuse to enforce the contract." (*A & M Produce*, *supra*, 131 Cal.App.3d at p. 486; see *Concepcion*, 131 S.Ct. at p. 1750 [adhesive nature of consumer contract cannot, standing alone, justify refusing to enforce arbitration provision in it; "the times in which consumer contracts were anything other than adhesive are long past"].) "Parties to commercial contracts fail to read them at their own peril. . . . 'One who signs or accepts a written instrument without reading it with care is likely to be surprised and grieved at its contents later on.'" (*West v. Henderson* (1991) 227 Cal.App.3d 1578, 1587 & fn. 6, quoting 3 Corbin, Contracts (1960) § 607, p. 656.)

"[T]he general rule . . . [is] that 'one who assents to a contract is bound by its provisions and cannot complain of unfamiliarity with the language of the instrument.'" (*Madden v. Kaiser Foundation Hosps.* (1976) 17 Cal.3d 699, 710, citations omitted.) That applies as much to consumer

contracts with arbitration provisions as to any other contract. (*Kilgore v. KeyBank, supra*, 673 F.3d at p. 964.) Here, the arbitration provision was in a large black box in the same font size as the rest of the contract. "The arbitration agreement is not buried within the document; it is conspicuous and appears in its own section . . . ." (*Ibid.*) True, the provision is on the back page of the single page form, but the form's front page – just above one of the sets of signature lines, in all capitals – references the "arbitration clause on the reverse side" and specifies that the buyer has read that clause. (AA 276; Opn. at 17; see *Kilgore v. KeyBank, supra*, 673 F.3d at p. 964 [no procedural unconscionability because, in part, "(i)mmediately above each Plaintiff's signature line is a warning that the student should read the contract carefully before signing, as well as a promise from the student that he would do so 'even if otherwise advised'"].)

The Court of Appeal criticized the form for being long and a single page. But length and complexity cannot be a basis for unconscionability. According to the Attorney General, more than 90 percent of that length and complexity (24 out of 26 linear inches) is statutorily mandated and required to be in a single document. (92 Ops. Cal.Atty.Gen. 97 at pp. *1-3; Civ. Code, § 2982.) Unconscionability requires lack of justification. It cannot be unjustified to comply with statutory mandates. Given the statutory constraints, the arbitration provision is about as prominent and conspicuous as possible.

The Court of Appeal also criticized the form for being a single page, back and front. But until the Attorney General issued his opinion that was

not clear (this contract was signed before the Attorney General's opinion); that's why an opinion from the Attorney General was needed. In any event, it is unclear how having the arbitration provision on page six of a multi-page document would have made it any more conspicuous than having it on the back of a single page document with a specific, all capitalized reference to it on the front above the signature line. The law requires *reasonable*, not perfect, notice.

Plaintiff claims that the dealer did not specifically point out the arbitration provision to him. The Ninth Circuit rejected essentially the same argument in *Kilgore v. KeyBank, supra*, 673 F.3d at p. 964. Under plaintiff's view, a contracting party has to go through a contract line-by-line with the other side to avoid procedural unconscionability because one cannot know in advance which clause may be later disputed. That is not the law. Parties are expected to read what they sign, especially for a major purchase such as a $50,000 luxury automobile.[17]

A reasonable buyer – one who reads what he or she signs, especially when making a $50,000 purchase, even one who just looks at the major, all capitalized provisions in close proximity to the signature lines – would have understood that the sales contract here included an arbitration provision.

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[17] In finding procedural unconscionability, the Court of Appeal relied on *Smith v. Americredit Financial Services, Inc.* (S.D.Cal. 2009) 2009 U.S. Dist. Lexis 115767 (Opn. at 15-16). But the Ninth Circuit vacated that federal district court opinion. (*Smith v. Americredit Financial Services, Inc.* (9th Cir. Dec. 13, 2011, No. 09-57016) 2011 WL 6170545.) It remanded for reconsideration in light of *Concepcion* (and, circularly, the Court of Appeal's opinion here). (*Ibid.*) So the outcome in *Smith* will now likely depend on this case.

Plaintiff – who has the burden of proof – made no showing that he could not negotiate the arbitration provision or that he lacked other alternatives, such as going to another dealer. On this record, there is no support for a finding of procedural unconscionability and certainly no procedural failing sufficient to justify a judicial refusal to enforce a relatively balanced arbitration provision. Even slight procedural unconscionability coupled with slight substantive unconscionability should not suffice to refuse to enforce otherwise valid contract language. (Cf. *Parada v. Superior Court*, *supra*, 176 Cal.App.4th at pp. 1584-1585 [finding provision unenforceable where low to medium procedural unconscionability coupled with high substantive unconscionability].) But *at most* that is all the record here could support.

III. To The Extent That The Arbitration Provision Is Not Per Se Valid, Remand To The Trial Court Would Be Required.

Even if the record could support a finding of unconscionability – it cannot – that still would not support the Court of Appeal's unilateral decision here to order the denial of arbitration. That is because the *trial* court never ruled on unconscionability, and it rests in the trial court's hands, in the first instance, to make the predicate factual determinations that might underlie any unconscionability finding and to exercise *its* discretion regarding severability.

A. The Trial Court Never Passed On The Unconscionability Factual Predicates.

Unconscionability may ultimately be a question of law. (Civ. Code, § 1670.5 [determination "as a matter of law"]; *Parada v. Superior Court*, *supra*, 176 Cal.App.4th at p. 1567.) But that doesn't mean that an appellate court can decide unconscionability without the trial court ever passing on the subject. Unconscionability determinations depend on predicate *trial court factual findings*. (*Murphy v. Check 'N Go of California, Inc.* (2007) 156 Cal.App.4th 138, 144 [when there is conflicting evidence on unconscionability, there is a question of fact]; *A & M Produce*, *supra*, 135 Cal.App.3d at p. 489 [unconscionability is a mixed question of law and fact]; *Baron v. Mare* (1975) 47 Cal.App.3d 304, 312 [questions of surrounding fact must be determined in deciding unconscionability].)

"[N]umerous factual issues may bear on" the unconscionability question. (*Gutierrez v. Autowest, Inc.*, *supra*, 114 Cal.App.4th at p. 89.) Factual determinations properly left to the trial court include "resolution of conflicts in the evidence, or on the factual inferences which may be drawn therefrom." (*Ontiveros v. DHL Express (USA), Inc.* (2008) 164 Cal.App.4th 494, 502.) "When the validity of an arbitration clause turns on a factual determination '[t]he standard on appeal is whether there is substantial evidence to support the trial court's finding.'" (*Stirlen v. Supercuts, Inc.*, *supra*, 51 Cal.App.4th at p. 1527, fn. 2, quoting, *Green v. Mt. Diablo Hosp. Dist.* (1989) 207 Cal.App.3d 63, 69, fn. 2, and citing

Price, *The Conscience of Judge and Jury: Statutory Unconscionability as a Mixed Question of Law and Fact* (1981) 54 Temp. L.Q. 743.)

Here, resolving all inferences favorably to the plaintiff, the arbitration provision would *still* be enforceable for the reasons set forth above, *requiring* arbitration to be completed. But, if not, there was ample basis for the trial court to rule in the dealers' favor – a decision that the Court of Appeal would then review for substantial evidence.

The Court of Appeal concluded on its own that it was "undisputed" (based on the plaintiff's own say so) that the plaintiff did not read the contract and did not know about the arbitration provision. As discussed above, a failure to read, alone, cannot suffice to show unconscionability. But even if it could, the plaintiff's declaration – that in making a $50,000 purchase, he did not even read what he was signing – is not automatically credible.

Nor is it undisputed. In the contract itself, plaintiff acknowledged and represented that he was aware of the arbitration provision and had read it. Documentary evidence is no less persuasive than testimonial evidence. (See *Lara v. Cadag* (1993) 13 Cal.App.4th 1061, 1065, fn. 3 [suggesting that sometimes documentary evidence is more persuasive than other evidence].) A factfinder need not believe a declaration over a contrary writing signed by the same declarant. There is no rule that the word of someone opposing enforcement of arbitration must, as a matter of law, be taken over the plain language of a document that the same person

indisputably executed. Such a rule, in and of itself, would uniquely disadvantage arbitration provisions, thereby violating the FAA.

To the extent the unconscionability determination involves material fact issues, remand to the trial court would be necessary, with directions regarding the standards that *Concepcion* and general unconscionability principles require.

B. An Ample Basis Exists For The Trial Court To Exercise Its Discretion To Sever Any Offending Clause.

The same is true of severance. The arbitration provision here specifically directs that any unenforceable clauses be severed (other than the now clearly enforceable class action waiver): "[I]f any part of this Arbitration Clause, other than waivers of class action rights, is deemed or found to be unenforceable for any reason, the remainder shall remain enforceable." (AA 279.) "[T]he determination of whether to sever an invalid contract provision is committed to the discretion *of the trial court.*" (*Brown v. Ralphs Grocery Co.*, *supra*, 197 Cal.App.4th at p. 503, emphasis added, citing *Armendariz*, *supra*, 24 Cal.4th at pp. 121-122; see Opn. at 32.) The trial court here never had the opportunity to exercise its discretion.

In *Brown*, the trial court (as here) had erroneously found an arbitration class-action waiver unconscionable, but the appellate court found another aspect of the arbitration provision unenforceable. (197 Cal.App.4th at p. 504.) *Brown* held that it must remand the severability

issue to the trial court (*id.* at p. 503) – exactly what the Court of Appeal refused to do here.

The Court of Appeal here asserted that no reasonable trial court could ever sever the offending elements, despite the arbitration provision's express severability clause. It relied primarily on the absence of any clause allowing a waiver of second-round arbitration fees. But there was no showing that *this* plaintiff or any luxury-car-purchasing party might need such a waiver. (*Green Tree Financial Corp.-Alabama v. Randolph*, *supra*, 531 U.S. at pp. 90-91 [speculative risk that party might be saddled with prohibitive costs cannot justify invalidating arbitration provision].)

In any event, there is a simple severability solution: Strike the supposedly offending internal arbitral "appeal" clause. Although the Court of Appeal based its unconscionability analysis heavily on *Little*, *supra*, 29 Cal.4th 1064, it ignored that *Little* held the subject arbitration "appeal" provision there to be *severable as a matter of law*. Severing that provision here would eliminate any issue regarding the losing party having to advance fees for any second arbitration round. But, even if this Court decided not to follow its approach in *Little*, at a minimum, it would have to remand to the trial court for it to exercise discretion as to whether that was possible and warranted.

Likewise, a court could strike the self-help exception clause, leaving the default circumstance – that a party can engage in self-help without the assistance of any court or arbitrator.

* * *

In short, if this Court concludes that some of the provisions might be unconscionable and that an unconscionability finding would not run afoul of *Concepcion* (it shouldn't), then it should remand the matter back to the trial court to make any unconscionability findings and determine all severance issues – at least to the extent this Court decides that any problematic clauses are not as a matter of law severable under *Little*.

IV. The Trial Court's Order Cannot Be Sustained After *Concepcion* On The Ground It Relied On – The Provision's Waiver Of Class-Wide Arbitration.

The trial court did not reach the unconscionability issue, let alone severability. Rather, it found the arbitration provision unenforceable under *Fisher v. DCH Temecula Imports LLC*, *supra*, 187 Cal.App.4th 601, because it failed to allow class action arbitration. (The Court of Appeal did not reach the *Fisher* issue). *Fisher* read the Consumer Legal Remedies Act, Civil Code section 1750, et seq., as requiring such a result, relying on the substantive unconscionability analysis in *Discover Bank*, *supra*, 36 Cal.4th 148.

But *Concepcion* overruled *Discover Bank*'s holding. Under the FAA, a state may not require that arbitration include class action claims. The fact that *Fisher* is premised on a different statutory scheme than *Discover Bank* is irrelevant. Federal Circuit Courts of Appeal recognize that *Concepcion* is not limited to the *Discover Bank* rule and facts; they hold that the FAA preempts *all* state statutes barring class action arbitration

waivers. (*Conneff v. AT&T Corp.* (9th Cir. 2012) 673 F.3d 1155 [*Concepcion* preempts Washington law allowing prohibition of class action arbitration to be substantively unconscionable in particular instances]; *Litman v. Cellco Partnership* (11th Cir. 2011) 655 F.3d 225 [*Concepcion* necessarily means that the FAA preempts New Jersey statute requiring arbitration provisions to include class actions].) *Concepcion*'s necessary implication is to overrule *Fisher* as well. Accordingly, the ground relied upon by the trial court to deny arbitration cannot, in fact, sustain its ruling.

CONCLUSION

Concepcion limits states' ability to refuse to enforce contractual arbitration provisions based on a review of the *process* to which the parties agreed. Absent an irrational process that no reasonable person could have agreed to without improper coercion, states cannot refuse to enforce arbitration provisions on the basis that the process agreed to is unconscionable. But even a standard unconscionability analysis, properly applied, demonstrates that arbitration should have been compelled here.

The Court of Appeal's determination affirming the trial court's refusal to compel arbitration should be reversed. The trial court should be directed to compel arbitration. At a minimum, the matter should be remanded to the trial court to make unconscionability and severance determinations in the first instance.

Dated: May 21, 2012

Respectfully submitted,

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CERTIFICATE OF WORD COUNT

Pursuant to California Rules of Court, Rule 8.204(c), I certify that this **OPENING BRIEF ON THE MERITS** contains **13,947** words, not including the tables of contents and authorities, the caption page, this Certification page and appendices.

Dated: May 21, 2012

Robert A. Olson

PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is 5900 Wilshire Boulevard, 12th Floor, Los Angeles, California 90036.

On May 21, 2012, I served the foregoing document described as: **OPENING BRIEF ON THE MERITS** on the parties in this action by serving:

SEE ATTACHED SERVICE LIST

(X) BY MAIL: As follows: I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. Under that practice, it would be deposited with United States Postal Service on that same day with postage thereon fully prepaid at Los Angeles, California in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date of deposit for mailing in affidavit.

Executed on May 21, 2012, at Los Angeles, California.

(X) (State) I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Anita F. Cole

SANCHEZ
v.
VALENCIA HOLDING COMPANY, LLC
[California Court of Appeal Case No. B228027;
Los Angeles Superior Court Case No. BC433634]

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