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# The California Court Of Appeal Disagrees With The U.S. Supreme Court On The Enforceability Of Arbitration Agreements

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*In Sanchez v. Valencia Holding Company, LLC*, --- Cal.Rptr.3d ----, 2011 WL 5027488 (Cal.App. 2 Dist. Oct. 24, 2011), the California Court of Appeal attempts an end run around the U.S. Supreme Court's recent decision in *AT&T Mobility LLC v. Concepcion*, 131 S.Ct. 1740 (2011). In *Concepcion*, the Supreme Court found that the Federal Arbitration Act (the "FAA") preempts state efforts to invalidate or re-write arbitration agreements by applying rules that would not result in the invalidation of other contracts. "The principal purpose of the FAA is to ensure that private arbitration agreements are enforced according to their terms." *Id.* at 1748. Specifically, the U.S. Supreme Court held that the FAA preempts state law restrictions on class action waivers in consumer arbitration agreements.

*Sanchez* also involves an arbitration agreement containing a class action waiver. In it, a consumer filed a putative class action against an automotive dealership, alleging disclosure violations in the purchase of his vehicle. The dealership moved to compel arbitration and enforce the class action waiver contained in a form contract widely used by dealerships throughout California. Before *Concepcion*, the trial court denied the motion on the ground the class action waiver was unconscionable under California law. The dealership appealed, and while that appeal was pending *Concepcion* was decided.

Side-stepping the class action waiver, the Court of Appeal in *Sanchez* affirmed the denial of the motion to compel arbitration on other grounds. It began by finding procedural unconscionability in part because the contract was a take-it-or-leave-it contract not open to negotiation. *Sanchez*, 2011 WL 5027488 at *9. The Supreme Court in *Concepcion* gave short shrift to such concerns, observing that the "times in which consumer contracts were anything but adhesive are long past." *Concepcion*, 131 S.Ct. at 1750.

The *Sanchez* court then went on to find the arbitration agreement substantively unconscionable because of the following four terms--1) a party who loses at arbitration can appeal to a panel of three arbitrators only if the award is $0 or exceeds $100,000; 2) a party can appeal any award of injunctive relief; 3) an appealing party must advance the arbitration costs of appeal subject to a final determination by the arbitrator; and 4) self-help remedies, including the right to repossession, are

excluded from arbitration. The *Sanchez* court concluded these provisions, though neutral on their face, are in practice one-sided in favor of the dealership. Citing *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal.4th 83 (2000), the *Sanchez* court held these arbitration terms to be unconscionable.

The FAA, however, plainly preempts such an approach. In *Concepcion*, the Court upheld class action waivers, even though they favor defendants. The Court was also untroubled by the fact that AT&T, the defendant in that case, had the unilateral right to amend the wireless service agreement at issue in that dispute. *Id.* at 1744. Indeed, AT&T exercised that right, unilaterally making "significant changes" to the arbitration agreement after the plaintiff entered into his contract. The Court also found that the FAA preempts state invalidation of arbitration agreements restricting discovery, even though a "court might reason that no consumer would knowingly waive his right to full discovery, as this would enable companies to hide their wrongdoing." *Id.* The FAA also preempts state invalidation of arbitration agreements allowing procedures that fail to abide by the Federal Rules of Evidence. *Id.* Indeed, the Court correctly noted that the FAA, and federal law generally, favors arbitration, even though arbitration necessarily waives the right to a jury trial. *Id.*

Instead, the Court in *Concepcion* was more concerned about the freedom of contract and federal law favoring arbitration, concluding that arbitration agreements must be enforced "according to their terms." *Id.* at 1745. Noting the long history of "judicial hostility" to arbitration agreements, especially in California, the Court held that state courts "may not rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable." *Id.* at 1747. Unconscionability cannot be based on "defenses that apply only to arbitration or that derive their meaning from the fact that an agreement to arbitrate is at issue." *Id.* at 1746. State law that has a "disproportionate impact on arbitration agreements" is suspect if not outright preempted. *Id.* at 1747. "Contract defenses unrelated to the making of the agreement--such as public policy--could not be the basis for declining to enforce an arbitration clause." *Id.* at 1755 (J. Thomas concurring). Thus, arbitration terms are enforceable even if arguably one-sided.

The four terms identified by the Court in *Sanchez* fall far short of shocking the conscience. They are bilateral on their face. Three of the four terms appropriately and reasonably define and limit the rights of appeal. As for the right to repossession, such a right exists regardless of an arbitration agreement. In other words, the consumer would not be better off without an arbitration agreement. Further, a consumer may challenge a repossession in arbitration, in the same way he or she could do in court. These four terms are certainly less one-sided than arbitration terms that waive rights to a jury, a class action, discovery, or the rules of evidence--all of which states cannot restrict because of FAA preemption. And they are far less one-sided than the unilateral right to change contract terms, including the terms of arbitration, after a contract is entered into.

According to the U.S. Supreme Court, "California courts have been more likely to hold contracts to arbitrate unconscionable than other contracts." *Id.* at 1747. *Sanchez* is but the latest example of this "judicial hostility to arbitration agreements." *Id.* at 1745. Such hostility is further evidenced by the fact that the Court in *Sanchez* refused to sever the offending terms, and otherwise enforce the arbitration agreement. Instead, it concluded that the arbitration terms were "permeated" with unconscionability. Thus, the entire arbitration agreement, including the class action waiver, was invalid. In this way, a California court has once again found that state public policy concerns about arbitration agreements trump freedom of contract and federal law favoring arbitration under the FAA. Such maneuvering flies in the face of the U.S. Supreme Court's decision in *Concepcion*.

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