S174475

IN THE SUPREME COURT OF CALIFORNIA

SONIC-CALABASAS A, INC.,

Plaintiff and Appellant,

v.

FRANK MORENO,

Defendant and Respondent

Following a Decision of the Court of Appeal, Case No. B204902
Second Appellate District, Division Four

Appeal from an order of the Superior Court of California, County of Los Angeles
Case No. BS107161, Hon. Aurelio N. Munoz, Judge

INITIAL BRIEF FOLLOWING REMAND FROM UNITED STATES SUPREME COURT

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I. INTRODUCTION

In this proceeding on remand from the United States Supreme Court, "for further consideration in light of *AT&T Mobility LLC v. Concepcion,* 563 U.S. ____ (2011) [131 S.Ct. 1740]," the only issue for determination is whether, and if so, how, *Concepcion* requires modification of this Court's now vacated decision – a decision which was issued on February 24, 2011, some two months prior to the issuance of *Concepcion.* In its prior decision, this Court held that while binding arbitration is an enforceable alternative to de novo superior court appeal of a "Berman award" (the Labor Commissioner's decision following an administrative hearing on a claim for unpaid wages), a provision in an employment agreement that waives access to the Labor Commissioner's Berman hearing process is unconscionable and a violation of public policy, as a matter of California law. This Court further held, pursuant to savings clause contained in Section 2 of the Federal Arbitration Act ("FAA"), which requires enforcement of arbitration agreements "save upon such grounds s exist at law or in equity for the revocation of any contract," that the FAA does not preempt this state law rule denying enforcement to a pre-dispute contractual provision, whether or not contained in an arbitration agreement, that denies an employee access to the Labor Commissioner's Berman process.

Concepcion does not put into question the standard for determining whether a contractual provision is unconscionable or a violation of public policy under state law. Rather, the import of *Concepcion* goes to whether a particular contractual provision, having been found to be unconscionable or contrary to public policy under state law, may nonetheless be enforceable as a result of FAA preemption of the state law rule denying enforcement to the challenged contractual provision, when that contractual provision is contained within an arbitration agreement.

Concepcion does set out the method to be followed for analyzing the question of whether the FAA preempts a state law rule denying enforcement of a provision in an arbitration agreement. In this brief, we first review the facts and procedural history of this case, carefully following this Court's prior decision, so that the reasoning and rationale for that decision can be considered against the test that has now been set out in *Concepcion.* As we demonstrate below, whatever effect *Concepcion* has had on other state laws or state law rules with respect to other issues related to arbitration, the rule that had been adopted in this case is unaffected by *Concepcion.* Following the preemption analysis set out in *Concepcion* results in the same conclusion that this Court reached over one year ago – the state law rule adopted by this Court, precluding the enforcement of predispute Berman

waivers, is not preempted under *Concepcion.*

II. FACTS OF THE CASE AND PROCEDURAL HISTORY

Respondent Frank Moreno ("Moreno") was employed by Petitioner Sonic-Calabasas A, Inc. ("Sonic") at its automobile dealership. As a condition of employment, Moreno signed an agreement to submit employment disputes to binding arbitration under the Federal Arbitration Act ("FAA"). Subject to exceptions not relevant here, the agreement applied to "all disputes that may arise out of the employment context ... that either [party] may have against the other which would otherwise require or allow resort to any court or other governmental dispute resolution forum...." (*Sonic-Calabasas A v. Moreno* (2011) 51 Cal.4th 659, 669-670.)

After resigning from his position with Sonic, Moreno filed an administrative wage claim with the California Labor Commissioner for unpaid vacation wages and penalties. In February 2007, Sonic filed a petition to compel arbitration of Moreno's claim, contending that by signing the arbitration agreement, Moreno waived his right to a Berman hearing. The Labor Commissioner intervened in the superior court proceedings on Moreno's behalf, arguing, *inter alia*, that resort to a Berman hearing was compatible with the arbitration agreement because the Berman hearing could be followed by de novo arbitration in lieu of a de novo appeal to the

superior court that is provided by Labor Code § 98.2(a); and that enforcement of the arbitration agreement to preclude preliminary access to the Berman hearing process would violate public policy. (*Id.*, at 670.)

The superior court denied the petition to compel arbitration as premature, stating that, as a matter of "basic public policy," an employee must be permitted to proceed with a wage claim before the Labor Commissioner, and that "until there has been the preliminary non-binding hearing and decision by the Labor Commissioner, the arbitration provisions of the employment contract are unenforceable, and any petition to compel arbitration is premature and must be denied." (*Id.*, at 670-671.)

Sonic appealed from the order denying its petition to compel arbitration. During the pendency of the appeal, the United States Supreme Court decided *Preston v. Ferrer* (2008) 552 U.S. 346, which held that the Labor Commissioner's original and exclusive jurisdiction under the Talent Agencies Act (Labor Code §1700, et seq.) was preempted when the parties are subject to an arbitration agreement governed by the FAA. As a threshold matter, the Court of Appeal concluded that *Preston* was not dispositive, reasoning that although *Preston* is not applicable to cases in which the party resisting arbitration brings a discrete challenge to the arbitration clause as unconscionable or contrary to public policy.

Nonetheless, the Court of Appeal reversed the order denying the petition to compel arbitration, holding that by signing the arbitration agreement, Moreno waived his right to pursue his wage claim before the Labor Commissioner, and that this "Berman waiver" was not contrary to public policy. (*Id.,* at 671.)

Moreno petitioned for review, contending that the Court of Appeal decided this question incorrectly. Sonic, in its answer to the petition for review, argued that the Berman waiver was enforceable, and renewed its argument that a court ruling invalidating a Berman waiver contained within an arbitration agreement would be preempted by the FAA, as construed in *Preston*. Review was granted to decide these two questions -- the enforceability of a Berman waiver, and the applicability of *Preston*. (*Id.*)

In the decision that issued one year ago, this Court explained: "the choice is not between a Berman hearing and arbitration, because a person subject to binding arbitration and eligible for a Berman hearing will still be subject to binding arbitration if the employer appeals the Berman hearing award. The choice is rather between arbitration that is or is not preceded by a Berman hearing." (*Id.*, at 680.) The Court then considered the import of the numerous statutory protections that are provided to employees under the Berman hearing and post-hearing process, including significant protections

that come into play if the employer chooses to file a de novo appeal of the Labor Commissioner's decision. For example, the Court noted that only by first proceeding before the Labor Commissioner could an employee avoid the risk of exposure for employer's attorney fees under Labor Code § 218.5, which requires an award of attorneys' fees to the prevailing party "[i]n any action brought for the nonpayment of wages," as any de novo appeal from a Labor Commissioner decision is instead governed by the one-way fee shifting provisions of Labor Code § 98.2(c). Likewise, only by first proceeding before the Labor Commissioner would an employee unable to afford counsel obtain the benefits, stemming from Labor Code § 98.4, of no-cost representation by an attorney provided by the Labor Commissioner to represent the employee in an employer filed de novo appeal. Also, only by first proceeding before the Labor Commissioner would an employee obtain the protection of an employer posted undertaking in the amount of the Labor Commissioner's award, required by Labor Code §98.2(b), as a means of ensuring payment to the employee if the employee ultimately prevails in the de novo proceedings. (*Id.,* at 680.) These statutory protections "are contingent on the Labor Commissioner's findings in a Berman hearing that an employee's claim is meritorious," so any waiver of the right to a hearing before the Labor Commissioner necessarily results in

a waiver of the right to these protections. (*Id.*, at 682.)

The Court reasoned that the above-enumerated protections, along with various others that flow from the Labor Commissioner hearing process, "represent[] a legislative judgment about the special protections and procedural rights that should be afforded to persons with wage claims in order to ensure that such claims be fairly resolved." (*Id.*, at 683.) The Court observed that these protections shared an evident "common purpose," to wit: "Given the dependence of the average worker on prompt payment of wages, the Legislature has devised the Berman hearing and posthearing process as a means ... to reduce the costs and risks of pursuing a wage claim, recognizing that such costs and risks could prevent a theoretical right from becoming a reality." (*Id.*, at 679.)

The Court therefore concluded that a pre-dispute Berman waiver, imposed as a condition of employment, is contrary to public policy. (*Id.*, at 684.) The Court further concluded that the Berman waiver contained in Sonic's arbitration agreement was unconscionable, both procedurally (because it was indisputably a contract of adhesion imposed as a condition of employment) and substantively (because the Berman waiver is unfairly one-sided). (*Id.*, at 685-686.) The conclusion of substantive unconscionability was expressly premised on the Court's finding that

"[r]equiring employees to forego these [Berman] protections as a condition of employment can only benefit the employer at the expense of the employee." (*Id.*) "[B]ecause the Berman hearing statutes accomplish their public policy goal of ensuring prompt payment of wages by according employees special advantages in their effort to obtain such payment, a provision in a contract of adhesion that requires the employee to surrender such advantages as a condition of employment is oppressive and one-sided, and therefore unconscionable." (*Id.*, at 687.)

The Court next considered whether the FAA preempts its holding that a predispute waiver of a Berman hearing, contained in an arbitration agreement, is contrary to public policy and unconscionable. This analysis began with the Court's observation that although federal and California law "favors enforcement of valid arbitration agreements .... such enforcement is limited by certain general contract defenses at law or in equity for the revocation of any contract." (*Id.* [internal citations and quotation marks omitted].) The Court noted that the United States Supreme Court has recognized that the FAA itself explicitly preserves these contract defenses to enforceability: "[U]nder section 2 of the FAA, a state court may refuse to enforce an arbitration agreement based on 'generally applicable contract defenses, such as fraud, duress, or unconscionability.'" (*Id.*, at 687-688,

quoting *Doctor's Associates, Inc. v. Cassarotto* (1996) 517 U.S. 681, 687.)

To be sure, the Court acknowledged that the doctrine of unconscionability cannot be used in a way that discriminates against arbitration agreements: "[S]tate law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. A state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2 [of the FAA]." (*Id.,* at 688, quoting *Perry v. Thomas* (1987) 482 U.S. 483, 492-493, fn. 9.) Thus, "in assessing the rights of litigants to enforce an arbitration agreement," a court may not "construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law. Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable for this would enable the court to effect what . . . the state legislature cannot." (*Id.*)

The Court explained that under *Perry*, there is no preemption of the Court's conclusion that Berman waivers are contrary to public policy and unconscionable, as this conclusion "does not discriminate against arbitration agreements. We neither construe the arbitration agreement in a

manner different from that in which we would construe nonarbitration agreements nor do we rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable." (*Id.,* at 688-689 [internal quotation marks omitted].) Rather, the Court noted, "our conclusion that a Berman waiver is contrary to public policy and unconscionable is equally applicable whether the waiver appears within an arbitration agreement or independent of arbitration." (*Id.,* at 689.)

This Court then considered, and rejected, Sonic's argument that *Preston* compels a finding that a state law rule precluding a waiver of the right to access the Labor Commissioner's Berman process is preempted by the FAA. The Court carefully examined the facts that distinguish *Preston* from this case, identifying two distinct reasons why *Preston* is inapplicable to the instant matter, and does not mandate FAA preemption of a state law rule denying enforcement to Berman waivers on the grounds that such waivers violate public policy and are unconscionable.

First, the Court noted that in *Preston,* the party resisting arbitration based his opposition to arbitration not on a discrete challenge to the arbitration clause of the parties' agreement, but rather, on an attack on the validity of the agreement as a whole, founded upon his claim that the agreement (between a television personality and his attorney) was void

under the Talent Agencies Act ("TAA") in that the attorney, seeking payment of fees allegedly owed under the agreement, had been acting as a talent agent without the license that is required under the TAA. The television personality sought to adjudicate the issue of whether the attorney had acted as a talent agent without a required license (and if so, whether the parties' agreement was void) before the Labor Commissioner, with whom the TAA vests exclusive primary jurisdiction to adjudicate disputes arising under that statute. The attorney sought instead to compel arbitration, pursuant to an arbitration clause in the parties' agreement, arguing that the arbitrator should decide the merits of the challenge to the validity of the entire contract as part of the arbitration over the fee dispute. In its decision, the U.S. Supreme Court held that the TAA's grant of primary jurisdiction to the Labor Commissioner, inasmuch as it thwarted the arbitration agreement, violated Section 2 of the FAA, which requires enforcement of arbitration agreements "save upon such grounds as exist at law or equity for the revocation of any contract." (*Id.*)

In analyzing the reasoning behind the *Preston* decision, this Court observed that *Preston* was simply the latest of a line of U.S. Supreme Court cases holding that "attacks on the validity of an entire contract, as distinct from attacks aimed at the arbitration clause .... are within the province of

the arbitrator to decide." (*Id.,* at 689-690, citing *Preston, supra,* 552 U.S. at 353. See also, *Buckeye Check Cashing, Inc. v. Cardegna* (2006) 546 U.S. 440 [plaintiffs brought court challenge to contracts they signed, which contained arbitration clauses, alleging that contracts *as a whole* were illegal under state law and void *ab initio*; U.S. Supreme Court held that challenge to whole contract, unlike discrete attack on validity of arbitration clause, is subject to arbitration.]) Like *Buckeye, Preston* involved a litigant seeking "invalidation of the contract as a whole.... [making] *no discrete challenge to the arbitration clause*." (*Sonic-Calabsas A, Inc., supra,* 51 Cal.4th at 690, citing *Preston, supra,* 552 U.S. at 354.)

This Court thus distinguished *Preston* from the instant discrete challenge to the Berman waiver contained within an arbitration agreement that is itself contained within an employment agreement: "*Preston* is distinguishable. In this case, unlike in *Buckeye* and *Preston,* the challenge is to a portion of the arbitration agreement – the Berman waiver – as contrary to public policy and unconscionable, rather than to contract as a whole. *Buckeye* therefore does not apply." (*Id.,* at 692.)

Second, the Court distinguished *Preston* "not merely because of the nature of the litigants' challenges, but also because of the fundamental differences between the two statutory regimes at issue. The statute in

Preston, the TAA, merely lodges primary jurisdiction in the Labor Commissioner, and does not come with the same type of statutory protections as are found in the Berman hearing and post hearing procedures." (*Id.*) For that reason, a predispute agreement that provides for arbitration rather than Labor Commissioner resolution of TAA disputes, "cannot be unconscionable or contrary to public policy concerns," unlike a waiver of the right to a Berman hearing. (*Id.*)

Finally, this Court addressed Sonic's contention that any delay to arbitration occasioned by allowing an employee's wage claim to first be heard by the Labor Commissioner prior to de novo arbitration necessarily runs afoul of the FAA. To be sure, *Preston* reasoned that in the context of a controversy under the TAA between parties covered by an arbitration agreement, "[r]equiring initial reference of the parties' dispute to the Labor Commissioner would, at the least, hinder speedy resolution of the controversy." (*Id.*, at 691, quoting *Preston, supra,* 552 U.S. at pp. 357-358.) Such delay, according to *Preston*, would frustrate "[a] prime objective of an agreement to arbitrate," namely "streamlined proceedings and expeditious results." (*Id.*)

This Court urged a narrow reading of *Preston* in this regard: "This statement [in *Preston*] cannot be read, as Sonic urges, to mean that any state

law procedure that delays the commencement of arbitration is preempted by the FAA. Rather, the *Preston* court's statement, read in context, is quite narrow." (*Id.*) It is narrow in the sense that it is merely directed at violations of the *Buckeye* rule – i.e., there can be no justification for delay when, under *Buckeye*, the challenge to the validity of the entire agreement must be decided by the arbitrator. But where, as here, *Buckeye* does not apply – i.e., where there is a discrete challenge to the validity of the arbitration clause, the resulting delay in arbitration does not run afoul of the FAA. (*Id.*)

Summarizing its reasoning, this Court explained that its holding invalidating a waiver of the right to access the Labor Commissioner's Berman process "neither falls within the purview of *Preston* and *Buckeye*, nor relies on rules of contract law that particularly disfavor arbitration, but rather is based on the generally applicable contract defenses of unconscionability and violation of public policy" and therefore, "is not preempted by the FAA." (*Id.*, at 695.) This Court thus concluded that arbitration would be premature until the Berman hearing is held and the Labor Commissioner issues a decision on the wage claim. (*Id.*)

The issuance of the Berman decision, if it is in favor of the wage claimant, provides the claimant with special protections for enforcing his or

her right to payment of wages, including one way fee shifting in any employer-filed de novo appeal, the requirement that the employer file an undertaking in the amount of the Labor Commissioner's award, and free legal counsel provided by the Labor Commissioner to represent the claimant in such de novo proceedings if the Commissioner determines the claimant is unable to afford private counsel. With these protections thus made available upon issuance of the Labor Commissioner's decision finding the claim to have merit, the employer may then file its appeal and compel arbitration of the de novo proceedings. (*Id.*, at 676.)

III. ARGUMENT

A. *CONCEPCION* HAS NO EFFECT ON THIS COURT'S DETERMINATION THAT A PREDISPUTE BERMAN WAIVER, IMPOSED AS A CONDITION OF EMPLOYMENT, IS UNCONSCIONABLE AND CONTRARY TO PUBLIC POLICY UNDER CALIFORNIA LAW

The issue that was considered and decided by the United States Supreme Court in *Concepcion* was "whether the FAA prohibits States from conditioning the enforceability of certain arbitration agreements on the availability of classwide arbitration procedures." (*AT&T Mobility LLC v. Concepcion, supra,* 131 S.Ct. at 1744.) The state law rule at issue, regarding the enforceability of class action waivers, had been set out in *Discover Bank v. Superior Court* (2005) 36 Cal.4th 148, 162: "When the

waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably involve small amounts of damages, and when it is alleged that the party with the superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money, then .... the waivers are unconscionable under California law," and for that reason, should not be enforced. (*Concepcion, supra,* 131 S.Ct. at 1746, citing *Discover Bank, supra,* 36 Cal.4th at 162.)

The U.S. Supreme Court, in its decision, never once questioned this Court's holding that such class action waivers are unconscionable under California law. Not one iota of analysis in *Concepcion* focused on the test for unconscionability, or the determination of public policy, under California law. Rather, *Concepcion* and any analysis of potential FAA preemption pursuant to *Concepcion* starts from the premise that State legislatures and State courts are the ultimate authorities on what constitutes an unconscionable agreement, or what constitutes a violation of public policy, under the law of that State. Potential FAA preemption comes into play only in the subsequent analysis of whether the State's determination that an arbitration agreement is unenforceable (whether due to unconscionabilty, violation of public policy, or any other doctrine of state

contract law) conflicts with the FAA or stands as an obstacle to the accomplishment of the FAA's objectives. (*Concepcion, supra,* 131 S.Ct. at 1746-1748.)

B. *CONCEPCION* HAS NO EFFECT ON THIS COURT'S DETERMINATION THAT THE FEDERAL ARBITRATION ACT DOES NOT PREEMPT THE STATE LAW RULE DENYING ENFORCEMENT TO PREDISPUTE BERMAN WAIVERS

The U.S. Supreme Court began its analysis by acknowledging that despite the federal policy favoring arbitration, "[t]he final phrase of § 2 [of the FAA] ... permits arbitration agreements to be declared unenforceable 'upon such grounds as exist at law or in equity for the revocation of any contract.' This saving clause permits agreements to arbitrate to be invalidated by 'generally applicable contract defenses, such as fraud, duress, or unconscionability,' but not by defenses that apply only to arbitration or that derive their meaning from the fact that an agreement to arbitrate is at issue." (*Concepcion, supra,* 131 S.Ct. at 1746, citing *Doctor's Associates, Inc., supra,* 517 U.S. at 687.)

With that as a backdrop, the Court then set out a two part test for determining whether a state law rule denying enforcement of an arbitration agreement is preempted by the FAA. First, "[w]hen state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA."

(*Concepcion, supra,* 131 S.Ct. at 1747.)

A second, more complex inquiry is required "when a doctrine normally thought to be generally applicable, such as duress or, as relevant here, unconscionability, is alleged to have been applied in a fashion that disfavors arbitration." (*Id.*) In that case, it is necessary to determine whether the state law rule "stand[s] as an obstacle to the accomplishment of the FAA's objectives," which are principally to "ensure that private arbitration agreements are enforced according to their terms." (*Id.,* at 1748; see also *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.* (2010) 130 S.Ct. 1758, 1763.) The U.S. Supreme Court explained that "this purpose is readily apparent from the FAA's text. Section 2 makes arbitration agreements 'valid, irrevocable, and enforceable' as written (**subject, of course, to the saving clause**)." (*Concepcion, supra,* 131 S.Ct. at 1748, emphasis added.) Thus, the second inquiry under *Concepcion* looks to whether the state law rule "interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA." (*Id.*) If it does, the state law rule is preempted by the FAA; if it does not, it is not preempted.

We have no quarrel with this central teaching of *Concepcion*: "States cannot require a procedure that is inconsistent with the FAA, even if it is

desirable for other reasons." (*Id.*, at 1753.) Although we start from the premise that it is the public policy of California to allow wage claimants access to the Labor Commissioner's Berman process, and that as a matter of state law, Berman waivers are unconscionable and contrary to public policy, we acknowledge that this premise does not provide an answer to the question of whether this state law rule is preempted by the FAA. The question of preemption must be answered by application of *Concepcion's* two part test. In applying that test, *infra*, we reach the same conclusion previously reached by this Court in its prior decision in the instant matter – the FAA does not preempt the state law rule denying enforcement of a predispute Berman waiver.

1. THE STATE LAW RULE DENYING ENFORCEMENT TO PREDISPUTE BERMAN WAIVERS DOES NOT PROHIBIT OUTRIGHT THE ARBITRATION OF A PARTICULAR TYPE OF CLAIM, SO IT IS NOT SUBJECT TO CATEGORICAL PREEMPTION

The state law rule adopted by this Court in its prior decision in this matter, denying enforcement to a predispute Berman waiver on the ground that such waiver is unconscionable and contrary to public policy, was correctly found to "not discriminate against arbitration agreements. We neither construe the arbitration agreement in a manner different from that in which we would construe nonarbitration agreements nor do we rely on the

uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable." (*Sonic-Calabasas A, Inc., supra,* 688-689 [internal quotation marks omitted].) Rather, "our conclusion that a Berman waiver is contrary to public policy and unconscionable is equally applicable whether the waiver appears within an arbitration agreement or independent of arbitration." (*Id.,* at 689.)

Moreover, this Court's prior decision makes abundantly clear that the reason for not enforcing the particular arbitration agreement at issue herein is not because it is an arbitration agreement, but rather, because it deprives the employee of the special protections that flow from the Berman process. The Court expressly acknowledged the possibility that an arbitration agreement could be devised that provides wage claimants with those protections, and that such an agreement would be enforced: "It may be possible for an arbitration system to be designed so that it provides an employee all the advantages of the Berman hearing and posthearing protections. But there is no indication that the present arbitration system is so designed." (*Sonic-Calabasas A, Inc., supra,* 51 Cal.4th at 681, fn. 4.) As such, this Court's prior decision cannot be characterized as one that "prohibits outright" arbitration.

The classic example of a state law preempted by the FAA because

the state law discriminated against arbitration agreements is provided in *Perry v. Thomas, supra*, 482 U.S. 483, which held Labor Code § 229 preempted by the FAA. Section 229 states: "Actions to enforce the provisions of this article for the collection of due and unpaid wages claimed by an individual may be maintained without regard to the existence of any private agreement to arbitrate." As the Supreme Court observed in *Concepcion,* this prong of the FAA preemption analysis applies not just to legislative enactments, but also, to rules of law adopted by courts: "[A] court may not rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what ... the state legislature cannot." (*Concepcion, supra,* 131 S.Ct. at 1747, quoting *Perry v. Thomas*, 482 U.S. at 493, fn. 9.)

Labor Code § 229 is preempted under the "prohibits outright" prong in *Concepcion* precisely because it precludes arbitration of wage claims without regard to whether the arbitration provisions implicate any unconscionability or independent public policy concerns that would come within the savings clause of FAA § 2. The only public policy articulated by Section 229 is a preference for litigation rather than arbitration of wage claims. Section 229 provides no grounds recognized by FAA § 2 to deny

enforcement to an arbitration agreement. It thus runs plainly afoul of the FAA.

Arguably, *Preston* also can be considered as an example of a case decided, at least in part, under the "prohibits outright" prong, as it concerned application of the provision within the TAA, Labor Code § 1700.44(a), giving the Labor Commissioner exclusive primary jurisdiction over disputes between artists and persons alleged to be acting as "talent agents" within the meaning of the Act. *Preston* does not provide a perfect fit for this prong of preemption analysis, in that the TAA does not purport to forever prohibit an arbitration of the dispute, but merely requires that the parties first have their dispute heard and decided by the Labor Commissioner, with the decision then subject to de novo review. But like *Perry v. Thomas,* the challenge to arbitration in *Preston* was not founded upon any generally applicable state law grounds recognized by the FAA's savings clause. And it is this, more than anything else, that makes *Preston* utterly inapplicable to the question of whether a state law rule prohibiting *Berman* waivers is similarly subject to FAA preemption. This could not have been expressed any more clearly by the United States Supreme Court: "[I]t bears repeating that Preston's petition [to compel arbitration] presents precisely and only a question concerning the forum in which the parties'

dispute will be heard.... Ferrer relinquishes no substantive rights the TAA or other California law may accord him." (*Preston v. Ferrer, supra,* 558 U.S. at 359.) Thus, under the FAA "he cannot escape resolution of those rights in an arbitral forum." (*Id.*)

The contrast between a Berman waiver and a waiver of the right to have a TAA controversy heard by the Labor Commissioner could not be more stark. What is missing from *Preston* is any claim that the agreement was procured by fraud or duress, or any contention that waiver of the Labor Commissioner's jurisdiction over disputes arising under the Talent Agencies Act brings about any harm that implicates unconscionability or public policy concerns. The absence of such claim is not surprising, as the role of the Labor Commissioner, in a proceeding under the Talent Agencies Act, is purely adjudicatory – i.e., the parties get nothing more out of the proceeding than an non-binding adjudication of their dispute. (Labor Code § 1700.44; *Preston, supra,* 552 U.S. at 359.) In contrast, the Labor Commissioner's Berman procedures are structured in a way that the Commissioner is more than a mere adjudicator of a private dispute. In a wage claim adjudication, a Labor Commissioner decision in favor of the employee triggers critical employee rights that would otherwise not be available to the employee, including one way fee shifting (and thus, no

exposure for the employer's attorneys' fees) in any subsequent employer-filed *de novo* arbitration or court proceeding, and no-cost representation by the Commissioner's attorneys for employees unable to afford private counsel in any such proceeding. (Labor Code §§ 98.2, 98.4.) There are no equivalent rights for parties under the Talent Agencies Act, under which Labor Commissioner adjudications have no effect on exposure to attorneys' fees, if any, in subsequent de novo proceedings, and there is representation provided by counsel for the Labor Commissioner to any party that prevails in a Labor Commissioner proceeding under the TAA. Thus, *Preston* could not, and did not, involve a discrete challenge to the arbitration agreement under the § 2 savings clause. Since the challenge to arbitration in *Preston*, based on a challenge to the validity of the contract as a whole, was not insulated from preemption under the savings clause, it necessarily came into conflict with the FAA.

Post-Concepcion, the U.S. Supreme Court has already made clear that even when a state law rule is subject to preemption because it "prohibits outright" the arbitration of a particular type of claim, enforcement of arbitration may be denied under the independent, generally applicable grounds set out in the FAA's savings clause. In a per curiam decision, the Court held that West Virginia's prohibition against predispute

agreements to arbitrate personal injury or wrongful death claims against nursing homes was "a categorical rule prohibiting arbitration of a particular type of claim," that is preempted under the "prohibits outright" prong of *Concepcion.* (*Marmet Health Care Center v. Brown* (2/21/2012) __U.S. __, ___ S.Ct. __, 2012 WL 538286 * 2.) However, in noting that the West Virginia court proposed an alternative holding that the particular arbitration provisions were unconscionable, the Supreme Court remanded the cases for consideration whether the arbitration clauses ... are unenforceable under state common law principles that are not specific to arbitration and preempted by the FAA." (*Id.*)

Finally, within the past week the Ninth Circuit issued a decision holding that the state law rule set out in *Broughton v. Cigna Healthplans of California* (1999) 21 Cal.4th 1066, and *Cruz v. Pacificare Health Systems, Inc.* (2003) 30 Cal.4th 303, "does not survive *Concepcion* because the rule 'prohibits outright the arbitration of a particular type of claim' – claims for broad public injunctive relief." (*Kilgore v. KeyBank National Association* (9th Cir. 3/7/2012) ___ F.3d ___, 2012 WL 718344 * 10, quoting *Concepcion,* 131 S.Ct. at 1747.) It is worth noting that in this decision, the Ninth Circuit then went on to consider whether enforcement should be denied to the arbitration provision at issue on the ground of

unconscionabiltiy – i.e., on independent grounds recognized by Section 2 of the FAA. The Ninth Circuit explained: "*Concepcion* did not overthrow the common law contract defense of unconscionabilty whenever an arbitration clause is involved. Rather, the Court reaffirmed that the savings clause preserves generally applicable contract defenses such as unconscionability, so long as those doctrines are not applied in a fashion that disfavors arbitration." (*Kilgore, supra,* 2012 WL 718344 *13, citing *Concepcion,* 131 S.Ct. at 1747.)

2. THE STATE LAW RULE DENYING ENFORCEMENT TO PREDISPUTE BERMAN WAIVERS DOES NOT STAND AS AN OBSTACLE TO THE ACCOMPLISHMENT OF THE PURPOSES OF THE FEDERAL ARBITRATION ACT IN THAT IT DOES NOT INTERFERE WITH THE FUNDAMENTAL ATTRIBUTES OF ARBITRATION

An analysis of the reasons set out by the U.S. Supreme Court for its holding, in *Concepcion,* that a state requirement for classwide arbitration procedures for a broad range of consumer disputes is inconsistent with the FAA points to only one conclusion with respect to the state law rule considered herein – that the state law rule that had been adopted by this Court, denying enforcement of a waiver of an employee's right to access the Labor Commissioner's Berman process is *not* inconsistent with the FAA; and hence, not preempted.

In explaining the reasons for its central holding that "[r]equiring the

availability of classwide arbitration interferes with *fundamental attributes of arbitration* and thus creates a scheme inconsistent with the FAA" (*Concepcion, supra*, 131 S.Ct. at 1748, emphasis added), the U.S. Supreme Court noted: "First, the switch from bilateral to class arbitration sacrifices the principal advantage of arbitration – its informality – and makes the process slower, more costly, and more likely to generate procedural morass than final judgment. . . . [B]efore an arbitrator may decide the merits of a claim in classwide procedures, he must first decide, for example, whether the class itself may be certified, whether the named parties are sufficiently representative and typical, and how discovery for the class should be conducted." (*Id.*, at 1751.) "Second, class arbitration *requires* procedural formality. . . . If procedures are too informal, absent class members would not be bound by the arbitration." (*Id.*) "Third, class arbitration greatly increases risks to defendants. . . . Defendants are willing to accept the costs of [uncorrected] errors in arbitration, since their impact is limited to the size of individual disputes, and presumably outweighed by savings from avoiding the courts. But when damages allegedly owed to tens of thousands of potential claimants are aggregated and decided at once, the risk of an error will often become unacceptable. Faced with even a small chance of a devastating loss, defendants will be pressured into settling questionable

claims." (*Id.*, at 1752.) In short, "[a]rbitration is poorly suited to the higher stakes of class litigation." (*Id.*)

None of the considerations and concerns articulated by this Court in *Concepcion* are applicable, even remotely, to the state law rule that had been adopted in this case. The state rule at issue herein does not alter or modify the structure of arbitration in any way; it does not rob arbitration of its informality; it does not superimpose formal procedural rules on arbitration; and it does not plunge arbitration into a high stakes setting that poses unreasonable risks to defendants. This Court's prior decision left the arbitration process completely intact, so that once the Berman process is concluded, arbitration may proceed precisely in the manner envisioned by the FAA. In short, this state law rule does not interfere with any of the "fundamental attributes of arbitration."

The Court's analysis in *Concepcion* necessarily distinguishes between those generally applicable contract defenses that lose their FAA § 2 insulation from preemption, and those that do not. Defenses cognizable under the § 2 savings clause implement policies that are designed to ensure that enforcement of the arbitration agreement will not be unfair. What *Concepcion* makes clear is that the source of the unfairness being addressed by the generally applicable contract defense cannot be some perceived

deficiency in the core fabric of arbitration as conceived by the FAA. Such an impermissible focus on the inadequacy of the basic and unique features of arbitration targets and disfavors arbitration and causes the generally applicable rule to run afoul of the FAA. By contrast, generally applicable contract rules that address a source of unfairness external to the arbitration process itself are preserved from FAA preemption by the § 2 savings clause.

The state law rule at issue in this case plainly falls into this latter category. It is not focused on any deficiency in arbitration. Rather, it is designed to ensure that employees are not denied access to a non-binding, pre-arbitration or pre-court litigation administrative process before the State Labor Commissioner, through which certain rights are made available to those employees who, in the determination of the Commissioner have meritorious wage claims, so as to assist those employees in subsequently vindicating their wage claims in the arbitral or judicial forum. None of these rights – one way fee shifting and the resulting immunization from liability for the employer's attorneys' fees in *de novo* proceedings initiated by an employer's appeal from a Labor Commissioner decision, the employee's right to no-cost representation by an attorney provided by the Commissioner, and the employer's obligation to post a bond or undertaking with a superior court in the amount of the Commissioner's award in order to

proceed with a *de novo* appeal – require the restructuring of any agreed upon arbitration hearing procedure or interfere in any manner with the "fundamental attributes of arbitration."

Under the rule adopted by this Court's prior decision, arbitration must be temporarily postponed while the employee accesses the Labor Commissioner's Berman process. Sonic has contended, and will no doubt continue to contend, that because the rule requires a delay in the commencement of arbitration, the rule is preempted.

Regarding this delay, it is noteworthy that this Court has already concluded that the time between filing a complaint with the Labor Commissioner and a Berman hearing date is usually between four and six months. (*Sonic-Calabasas A, Inc., supra,* 51 Cal.4th at 681, citing *Cuadra v. Millan* (1998) 17 Cal.4th 855, 860-862 & fn. 7.) To this we may add another 15 days, the statutory deadline for the Labor Commissioner's issuance of a decision following the Berman hearing. (Labor Code § 98.1) Boiled down to its essence, Sonic argues that this delay, or presumably, *any* delay (no matter how insignificant) caused by *any* state law rule of general application (no matter the reason for the rule) "interferes with the fundamental attributes of arbitration" so as to mandate FAA preemption of the state law rule. This argument is deeply flawed.

While the facilitation of streamlined proceedings is an important purpose of the FAA, it is unequivocally clear that requiring arbitration proceedings to go forward at once, without any postponement or delay, regardless of the existence of generally applicable state contract law grounds supporting a discrete challenge to the enforceability of an arbitration agreement, is not a "fundamental attribute" of arbitration. Thus, a defense of fraud, duress or unconscionability as to some specific provision of the arbitration agreement will require the postponement of arbitration while the validity of the defense is adjudicated. "If a party challenges the validity under §2 of the precise agreement to arbitrate at issue, the federal court must consider the challenge before ordering compliance with that agreement under § 4." (*Rent-A-Center West, Inc. v. Jackson*, 561 U.S. ___, 130 S.Ct. 2772, 2778 (2010).) Thus, the policy of promoting streamlined arbitration proceedings must yield to the assertion of a ground for revocation of a contract under the § 2 savings clause. This is necessary because the § 2 savings clause recognizes that implementation of a state policy aimed at preventing the unfairness of enforcing an arbitration agreement procured by fraud or duress, or a provision within the agreement that is unconscionable or that violates public policy, trumps the purpose of facilitating streamlined arbitration proceedings.

As *Concepcion* makes clear, the "fundamental attributes of arbitration" are by definition impermeable – they do not yield to countervailing considerations – and that is why those "fundamental attributes" override § 2 defenses that might otherwise be saved from FAA preemption. By contrast, the policies of the FAA related to avoiding the postponement and delay of arbitration are not impermeable and do yield to countervailing considerations asserted pursuant to defenses under § 2; and consequently, such policies are not fundamental attributes of arbitration.

Because the Labor Commissioner's exclusive primary jurisdiction under the TAA does not implicate Section 2 defenses under the FAA, any resulting delay of arbitration could not be justified under the FAA. Neither *Preston* nor *Concepcion* supports Sonic's contention that a generally applicable contract defense under § 2 can be preempted merely on the basis that its implementation will result in a postponement or some delay of arbitration. Indeed, that precise issue was not before the Court in either case. *Preston* stands only for the proposition that where a delay in arbitration is caused by a state law rule that is not based on a generally applicable ground arising under the § 2 savings clause, the rule will be preempted as in conflict with the FAA. There is nothing in *Concepcion* that would support extending this proposition in *Preston* to apply to a

discrete § 2 challenge to the enforceability of an arbitration provision where the challenge, if successful, as here, does not interfere with any of the fundamental attributes of arbitration.

Preston, therefore, has absolutely no bearing on defenses asserted under the § 2 savings clause. It is only to the extent that any such defense may interfere with the "fundamental attributes" of arbitration that *Concepcion* requires preemption, and *Concepcion* cannot possibly be read to mean that the delays occasioned by discrete challenges to the enforceability of an arbitration agreement under the § 2 savings clause poses a threat to a fundamental attribute of arbitration. Indeed, such a reading of *Concepcion* would essentially nullify the savings clause.

IV. CONCLUSION

Application of the test for FAA preemption set out in *Concepcion* compels the conclusion that the state law rule that had been adopted by this Court, barring the enforcement of a predispute waiver of an individual employee's right to access the Labor Commissioner's Berman process, neither "prohibits outright" the arbitration of wage claims, nor discriminates against arbitration agreements, nor stands as an obstacle to the accomplishment of the purposes of the Federal Arbitration Act, nor interferes with the "fundamental attributes of arbitration." Under every

formulation of every test announced in *Concepcion,* this state law rule is not preempted by the FAA. As such, we respectfully request that this Court reaffirm its prior decision in this matter, and hold that *Concepcion* does not warrant any change in the conclusions reached by this Court in its prior decision.

Dated: March 12, 2012

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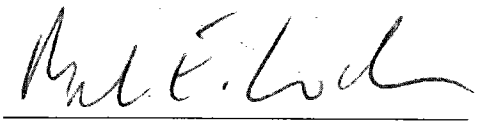
CERTIFICATION OF WORD COUNT
(Cal. Rules of Court, Rule 8.204)

The text of this Initial Brief Following Remand from the U.S. Supreme Court consists of 7,224 words as counted by the Corel Word Perfect X4 word processing program used to generate this document.

Dated: March 12, 2012

By: 

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PROOF OF SERVICE

(CCP Section 1013a(2))

I, Miles E. Locker, hereby certify that I am an active member of the State Bar of California, and I am not a party to the within action. My business address is Locker Folberg LLP, 235 Montgomery Street, Suite 835, San Francisco, CA 94104.

2. On the date hereof, I caused to be served the following document:

INITIAL BRIEF FOLLOWING REMAND FROM U.S. SUPREME COURT

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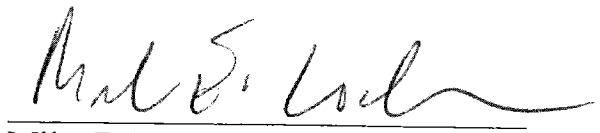
I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed at San Francisco, California, on Monday, March 12, 2012.



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