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ARBITRATION

WAIVER OF RIGHT TO ARBITRATE

To Move or Not to Move: Calculating the Risk Of Waiving the Right to Arbitrate in a Shifting Judicial Landscape

BY SANDRA MCCALLION

The U.S. Supreme Court's decision in *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 2011 BL 110648, 79 U.S.L.W. 4279 (U.S. 2011), has been characterized as a ''game changer'' in the arbitration arena. *Concepcion* overturned California's ''*Discover Bank*'' rule, which had held that arbitration provisions that waived the consumer's right to a class-wide arbitration in certain consumer contracts of adhesion were unconscionable.[1] In overruling the California practice, the Supreme Court held that the rule was ''an obstacle to the accomplishment and execution of the full purposes and objections of the Federal Arbitration Act.''[2] Before *Concepcion*, a motion to compel challenging state court precedent would have been summarily denied. After the decision, case law from both state and federal courts suggests that the same motion will likely be granted.[3]

''In short, the judicial landscape remains somewhat unsettled.''

These motions are not simply *pro forma* in the post-*Concepcion* world, however. The FAA's ''savings clause,'' which provides that common law contract defenses may invalidate an arbitration provision, may still permit a party to try its case in court so long as those defenses are not ''applied in a fashion that disfavors arbitration.''[4] Since *Concepcion*, some courts—although few—have cited this language in support of their findings that the arbitration provision at issue is unconscionable.[5]

Still other courts have questioned the scope of *Concepcion*, holding, for example that the policy favoring arbitration is not so broad that it requires arbitration of claims brought by a representative action under a Pri-

[1] *Concepcion,* 131 S. Ct. at 1753.
[2] *Id.*

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[3] *See, e.g., Owen v. Briston Care Inc.*, 702 F.3d 1050 (8th Cir. 2013); *Pendergast v. Sprint Nextel Corp.*, 691 F.3d 1224 (11th Cir. 2012) (81 U.S.L.W. 310); *Torres v. United Healthcare Service Inc.*, No. 12-cv-923, 2013 BL 28690 (E.D.N.Y. Feb. 1, 2013); *Superbag Operating Co. Inc. v. Sanchez*, No. 01-12-00342-cv, 2013 BL 26258 (Tex. App., Jan. 31, 2013).
[4] *Concepcion*, 131 S. Ct. at 1747.
[5] *See, e.g., Gandee v. LDL Freedom Enterprises Inc.,*, No. 87674-6, 2013 BL 33094 (Wash. Feb. 7, 2013); *Natalini v. Import Motors Inc.*, A133236, 2013 BL 30491 (Cal. App. 1 Dist. Jan. 7, 2013); *Smith v. AmeriCredit Financial Services Inc.*, No. 09-cv-1076, 2012 BL 343559 (S.D. Cal. Mar. 12, 2012).

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vate Attorney General Act;[6] claims brought under car purchase agreements;[7] or claims arising from the Bankruptcy Code.[8] In short, the judicial landscape remains somewhat unsettled.

Still another defense that is likely to remain viable until—and if—this area becomes more settled, is that the defendant waived its right to arbitrate because it litigated the case rather than moving to compel. In response, defendants argue that such a motion would have been futile pre-*Concepcion*, so litigating was the only real option. Although the standard is articulated in different ways, the court deciding the motion will look primarily at the extent to which the movant participated in the judicial proceedings; whether the non-movant would be prejudiced; and the reason for any delay.[9]

Eleventh Hour Attempt to Arbitrate Rejected

The success of the waiver challenge has been mixed. For example, in *Garcia v. Wachovia Corp.*,[10] the U.S. Court of Appeals for the Eleventh Circuit found that the defendant had waived its rights in a putative class action alleging that the defendant charged excessive overdraft fees on debit card transactions. The arbitration agreement at issue permitted either party to invoke arbitration, but all arbitrated claims had to be arbitrated on an individual and not a class-wide basis.[11] In other words, the issue adjudicated in *Concepcion*, albeit in Florida and not California.

The facts here are unique but cautionary. Two years before *Concepcion* was decided, the district court in that case had actually invited the defendant—not once but *twice*–to move to compel arbitration, but the defendant chose not to do so. Instead, as the Eleventh Circuit noted, the defendant represented that it did not ''intend to seek arbitration of [its] claims in the future.''[12] The parties then proceeded to prepare for trial, engaging in extensive discovery and litigating several motions before the district court.[13] Two days after *Concepcion* was decided, the defendant shifted course and moved to dismiss in favor of arbitration or, alternatively, to stay the proceedings pending arbitration, taking the position that it had not waived its right to compel arbitration because, before *Concepcion*, it could not have enforced its arbitration agreements.[14]

Both the district court and the Eleventh Circuit rejected the eleventh hour attempt to arbitrate. The Eleventh Circuit pointed to the fact that the defendant had gone ''so far as to say that it did not intend to seek arbitration in the future of the claims'' and had ''substantially invoke[d] the litigation machinery prior to demanding arbitration.''[15]

The defendant's contention that any motion to compel would have been ''unlikely'' to succeed before *Concepcion* was given short shrift. Significantly, the Eleventh Circuit held that the defendant's motion would *not* have been futile, holding that ''absent controlling Supreme Court or circuit precedent foreclosing a right to arbitrate, a motion to compel arbitration will almost never be futile.''[16] The circuit court then went on to note that the only excuse for failing to move when an arbitration provision is at issue is if it is ''almost certain'' that the motion would be denied.[17]

Defendant Didn't Move Swiftly Enough

California's Second District Court of Appeals similarly found waiver in *Alvarado v. Miller-DM Inc.*[18] In *Alvarado*, the defendant moved to compel arbitration on May 14, 2010—nearly a year before *Concepcion* was decided and so California's *Discover Bank* rule was controlling—which was denied. It then filed a second petition on July 22, 2010, in which the defendant ''expressly agreed not to seek arbitration of plaintiff's class claim under the [California] Consumers Legal Remedies Act'' but sought to arbitrate plaintiff's other claims.[19] Consistent with the *Discover Bank* rule controlling at that time, the defendant stated in its petition that it ''does not suggest that the [arbitration clause] applies to that claim.''[20] On Aug. 2, 2011, nearly four months after *Concepcion* was decided, the defendant then sought to compel arbitration of the class claims in light of the Supreme Court's decision.[21]

The Fourth District held that the ''Defendant expressly waived its right to arbitrate the class action claims'' by stating that it did not intend to arbitrate those claims and then waiting ''almost four months'' after *Concepcion* to file its third petition.[22] Although the *Discover Bank* rule would have made it virtually certain the motion would have been denied before *Concepcion*, this defendant nonetheless waived by litigating and then apparently not moving swiftly enough. Even more fatal, the defendant sought by its motion to arbitrate ''the precise claim defendant had expressly stated previously that it would not seek to arbitrate.''[23]

Some Courts Have Accepted Futility Argument

Some California courts have accepted the futility argument despite the defendants' participation in the litigation process. In *Doty Scott Enterprises Inc. v. Sector 10 Inc.*,[24] for example, although the defendant moved to compel arbitration when the parties had prepared ''memoranda of contentions of fact and law and trial briefs'' and were waiting for a trial date to be set, the court nonetheless found no waiver because the plaintiff had not been prejudiced. The defendant successfully argued that all the materials that had been prepared were

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[6] *Brown v. Ralphs Grocery Co.*, 187 Cal. App. 4th 489 (Cal. App 2 Dist. 2011).
[7] *See, e.g., Natalini.*
[8] *Henderson v. Legal Helpers Debt Resolution LLC (In re Huffman)*, Bankr. No. 12-00177, 2013 BL 31919 (Bankr. S.D. Miss. Feb. 6, 2013).
[9] *See, e.g., Rota-McLarty v. Santander Consumer USA Inc.*, 700 F.3d 690, 701-02 (2012) (applying Maryland arbitration law).
[10] 699 F.3d 1273 (2012).
[11] *Id.* at 1276.
[12] *Garcia,* 699 F.3d at 1276.
[13] *Id.*
[14] *Id.*
[15] *Garcia*, 699 F.3d at 1277 (citations omitted).
[16] *Garcia*, 699 F.3d at 1278.
[17] *Id.* at 1279.
[18] B239918, 2013 BL 15223 (Cal. App. 2 Dist. Jan. 18, 2013).
[19] *Id.* at *1.
[20] *Id.* at *4 (quoting Petition).
[21] *Id.* at *5.
[22] *Id.* at *7.
[23] *Id.* at *1.
[24] No. 3:09-cv-2616 (S.C. Cal. Jan. 24, 2013).

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''entirely consistent with the disclosures required in arbitration'' so ''the case is as ready for arbitration as it was for trial.''[25] Significantly, the court found that there was no ''indication that Defendant used this case to gain information about Plaintiff's case that would otherwise be unavailable in arbitration.''[26]

''The defendant successfully argued that all the materials that had been prepared were 'entirely consistent with the disclosures required in arbitration' so 'the case is as ready for arbitration as it was for trial.' ''

In *Gomez v. Marukai Corp.*,[27] the California Court of Appeal for the Second District reversed the trial court's finding that the defendant waived the right to compel arbitration, holding that there had been no waiver for its failure to move before *Concepcion* was decided. The case involved a class and representative action under the California Labor Code Private Attorneys General Act of 2004 (''PAGA'') filed in March 2010.[28] The parties conducted precertification discovery; held a case management conference; negotiated the text of an opt-out notice; and the plaintiff took depositions of two of the defendant's managers.[29] In early August 2011, nearly four months after *Concepcion* had been decided, the defendant told plaintiff that it would not produce putative class member information because it intended to compel arbitration of the individual claims.[30] The defendant filed its motion on Aug. 16, 2011.

The Second District held that there was no waiver despite waiting four months after *Concepcion* to file because, among other things, ''*Concepcion* did not address or consider whether the FAA preempted'' a California rule established in *Franco v. Athens Disposal Co.*,[31] holding that a PAGA waiver in an arbitration agreement was unconstitutional. According to the Second District, that issue was not decided until it was addressed by the California Court of Appeals for the Fourth District on July 12, 2011.[32] *Brown* held that the trial court could sever the PAGA waiver from the arbitration agreement and send the other claims to arbitration.[33] The Second District determined that, although *Concepcion* had been decided, without the added benefit of the ruling in *Brown*, the defendant in *Gomez* had not ''unreasonably delayed'' by waiting to make its motion.[34] Indeed, the Second District noted that, ''[a]lthough defendant could have moved to compel arbitration . . . we decline to establish a rule that defendant should have done everything possible to compel arbitration, no matter how futile, expensive, or protracted the process.''[35] According to this appellate court, the defendant had no choice but to participate in the litigation process when the governing California law arguably held that the arbitration agreement was unenforceable.[36]

How Should a Defendant Proceed?

What do these cases suggest about how a defendant should proceed if the right to arbitrate is at all unclear? On the one hand, there is the Fed. R. Civ. P. 11 obligation not to burden judicial resources with frivolous motions, and clients are unlikely to want to spend financial resources on motions that are virtually certain to be denied. On the other, in a rapidly developing area of the law such as arbitration, it may be advisable to err on the side of caution and bring the motion despite the limited likelihood of success. The *Garcia* case in the Eleventh Circuit is particularly instructive in this regard. There, the circuit court focused among other things on the fact that the trial court had twice raised the issue of arbitration, the defendant represented that it did not intend to arbitrate plaintiff's claims (although the law did not permit arbitration of those claims at the time), and then actively litigated the case.

Even if the court does not raise the issue of arbitration on its own, it would behoove the defendant to do so itself, going on record that it views such a motion as futile, but, should the legal landscape change, it would consider promptly doing so. And then the client and its lawyers must be prepared to move immediately or risk a finding of waiver. As *Concepcion* has shown, arbitration is highly favored; if the client is a signatory to an arbitration provision, arbitration may prove to be an option even where the law today says that forum is foreclosed. Certainly a defendant should think long and hard about expressly disclaiming the right to arbitrate any claims, even if it seems momentarily advantageous.

[25] *Id.*
[26] *Id.*
[27] B236623, 2013 BL 35596 (Cal. App. 2 Dist. Feb. 11, 2013),
[28] *Id.* at *1.
[29] *Id.*
[30] *Id.*
[31] 171 Cal. App. 4th 1277 (2009).
[32] *Brown v. Ralphs Grocery Co.*, 197 Cal. App. 4th 489 (Ca. Ct. App. 4 Dist. 2011).
[33] *Gomez*, 2013 BL 35596, at *2.
[34] *Id.* at *7.
[35] *Id.* at *6.
[36] *Id.* at *8 (citing waiver cases).