AUGUST, 2013

# PARK WATCH ™ LEGAL DEVELOPMENTS NEWSLETTER

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# Supreme Court Stomps Out Consumer Class Actions: Time for Owners to End FTM Risks By Including FAA Arbitration in Residency Documents

*By Kasey C. Phillips, Esq.*

## Upshot

In the ground-breaking precedent of *AT&T Mobility v. Concepcion ("AT&T Mobility")*, the Supreme Court, by the narrow margin of 5-4, embraced arbitration in a set of extreme circumstances which has now become the benchmark for testing the sufficiency and hence enforceability of arbitration clauses. The *trifecta* of *AT&T Mobility* included the right to bar class action treatment of very small claims (even the $30.00 tax at issue there), lowered scrutiny of arbitration clauses (tested like any other contractual clause without application of any special rules applicable only to arbitration) and the trumping of all state laws which would impair the Federal Arbitration Act ("FAA") public policy of favoring arbitration.

In the meantime, *AT&T Mobility* has taken root in several case progeny which re-emphasizes that the FAA is the Supreme law of the land. It has been applied to employment and consumer law of several kinds. State law judges continue to remain hostile to *AT&T Mobility*, seeking to find distinctions to provide breathing space for state procedure (*qua* defenses to arbitration), especially the ability to squelch class actions, and the argument of imbalance of the relative economic strength of the parties. Yet *AT&T Mobility* trundles along unblemished and indeed strengthened and reinforced without foreseeable abatement.

The FAA is a genuine and complete panacea against the *failure to maintain* ("FTM") lawsuit, at virtually no cost to the owner. No state politicians or courts can change that. And no federal authority appears anxious to attenuate arbitration rights and power under the FAA anytime soon.

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*So,* the FAA allows you to wave good-bye to jury trials, and deal with resident claims one by one. *For all the hard work of acquiring, operating, and stressing over your investment, why are you not taking advantage of the single best, available, cost-free protection the federal government will ever provide?*

In this latest, closely-watched case, the Court in *Italian Colors*[1] lends additional support for the freedom of parties to contract as to dispute resolution by reiterating the distinct message that arbitration agreements must be enforced according to their terms. In this case, the Supreme Court held, 5-3, that *contractual waivers* of class action arbitration *must be honored*. This remaining shard of the shattered hopes of plaintiff lawyers is also, like all before, cast aside by the Court.

## Facts

Plaintiff *Italian Colors* and a number of other merchants (collectively "*Italian Colors*") contracted with American Express ("American Express") to accept American Express credit cards as a form of payment. The agreement between the parties stated that all disputes would be resolved through arbitration. Further, the agreement provided that:

> *"[t]here shall be no right or authority for any Claims to be arbitrated on a class action basis" meaning that Italian Colors waived any right to class action arbitration.*

[1] *American Express Co., et al. v. Italian Colors Restaurant, et al.*, No. 12–133. Argued February 27, 2013, Decided June 20, 2013.

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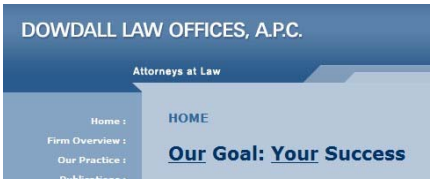


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Nonetheless, *Italian Colors* became upset with American Express, and filed a class action lawsuit for violations of federal antitrust laws, under the *Sherman Anti-Trust* and *Clayton Acts*, for engaging in illegal tying arrangements. *Italian Colors* alleged that American Express was using *monopoly power* in the credit card market to compel merchants to accept American Express cards *"at rates approximately 30% higher than the fees for competing credit cards."*

The Lawsuit: American Express filed a motion to compel *individual arbitration* pursuant to the FAA and the agreement of the parties. In opposition to the motion, *Italian Colors* presented a declaration by an economist who determined that it would cost *"at least several hundred thousand dollars"* to obtain the expert analysis necessary for *Italian Colors* to prove the antitrust claims. The maximum payout for any individual plaintiff would be between $12,850 and $38,549. *Italian Colors* contended that it would not be *economically feasible* to *individually* arbitrate their claims.

The Trial Court: The District Court granted American Express' motion to compel arbitration and dismissed the case. But, the Court of Appeals (the reviewing Court in the Second District) reversed the decision, holding that *Italian Colors* had proven that it would be *cost prohibitive to individually arbitrate* the claims and thus the class action arbitration waiver could not be enforced. The Supreme Court granted *certiorari* and vacated the judgment, remanding for additional consideration in accordance with another then recently decided case. [2]

> . . . just because a plaintiff lacks the means to pursue a claim does not mean the plaintiff is denied the right to pursue it.

The Court of Appeals then took it upon itself to reconsider the case again in light of the Supreme Court ruling in *AT&T Mobility.* The Court found that *AT&T Mobility* did not apply and re-affirmed its reversal of the motion to compel arbitration. The Supreme Court granted review to determine whether under the Federal Arbitration Act courts may:

*"invalidate arbitration agreements on the ground that they do not permit class arbitration of a federal-law claim."*

The Supreme Court: The Supreme Court held that the FAA renders contractual waivers of class arbitration enforceable even when the expense of proving a claim in individual arbitration exceeds *any potential recovery*. This decision reinforces and clarifies some questions left unanswered in the Supreme Court decisions of *Stolt-Nielson and AT&T Mobility*. It bolsters the Court's recent trend of strictly enforcing the terms of arbitration agreements. And, it is very welcome news for park owners.

## Discussion:

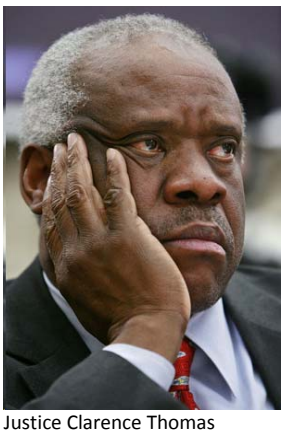
Justice Scalia delivered the opinion of the majority, once again reiterating the FAA requirement that courts "*rigorously enforce*" arbitration agreements in accordance with their terms including provisions regarding participants in arbitration and rules and procedures for arbitration. Scalia stated that this proposition holds true unless the demands of the FAA are "overridden by a contrary congressional command."


Justice Antonin Scalia, at U.S.C. School of Law

The Court found no congressional command requiring a rejection of the class action arbitration waiver. The Court determined that antitrust laws do not reflect intent to preclude a class action waiver nor do they "guarantee an affordable procedural path to the vindication of every claim." The Court was also not persuaded that Congressional approval of Rule 23 created a right to class proceedings for the defense of statutory rights.

The Court then examined the judge-made, "effective vindication" exception to the FAA. *Italian Colors* argued that enforcing the class arbitration waiver "*bars effective vindication ... because they have no economic incentive to pursue their antitrust claims*" in individual arbitration proceedings. Indicating that the origin of the exception was mere dictum in another case,[3] the Court declined to apply it here:

- The exception was designed to prevent "prospective waiver of a party's right to pursue statutory remedies" but was not intended to be invoked when "proving a statutory remedy" became too costly;
- *Just because a plaintiff lacks the means to pursue a claim does not mean the plaintiff is denied the right to pursue it.*


Justice Clarence Thomas

The court explicitly noted that its *"decision in AT&T Mobility all but resolves this case"* because the Court already rejected the argument therein that "class arbitration was necessary to prosecute claims that might otherwise slip through the legal system." Two years later, *AT&T Mobility* is more than alive and well.

The Court, finally, addressed a byzantine labyrinth created by the Court of Appeals, which required parties to exalt needlessly prolix procedure to prove a host of items before the arbitration question was resolved. Essentially, the lower Court sought to try the case before deciding if agreed upon arbitration could be enforced. The Supreme Court determined that such a burdensome hurdle would "undoubtedly destroy the prospect of speedy resolution" for which arbitration was specifically designed and that the FAA did not authorize "such a judicially created superstructure." A well written clause requires the arbiter to resolve all issues including arbitrability of the proffered claim.

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[2] *Stolt-Nielsen S. A. v. Animal Feeds Int'l Corp*., 559 U.S. 662 (2010) ("*Stolt-Nielson*").

[3] *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.,* 473 U.S. 614 (1985).

Justice Thomas Speaks: Justice Thomas concurred, stating in essence that the *Italian Colors* plaintiff, like a disgruntled infant, is just not listening. He stated, simply, that the result was "required by the plain meaning of the Federal Arbitration Act" which requires an arbitration agreement "be enforced unless a party successfully challenges the formation of the arbitration agreement." Justice Thomas concluded that *Italian Colors* "voluntarily entered" into an arbitration agreement and "cannot now escape its obligations merely because the claim it wishes to bring might be economically infeasible."

No Surprise Here: Kagan Dissents: Justice Kagan dissented, joined by Justice Ginsburg and Justice Breyer, giving a harsh summary of the majority opinion:

" . . . the monopolist gets to use its monopoly power to insist on a contract effectively depriving its victims of all legal recourse."

The dissent contended that the cost of individually arbitrating the claims was so prohibitively expensive as to prevent the parties' rights to pursue their statutory remedies. The dissent would apply the "effective vindication" exception.


Justice Elena Kagan

## Comment:

California Courts have *consistently* refused to enforce even valid arbitration clauses in "failure to maintain" actions, ruling that such procedures would result in a duplication of effort, inconsistent rulings, wasted court time, or that such agreements were not enforceable due to the claims excluded or included, costs, or procedural impediments to a fair hearing for the residents. This changed with the holding in *AT&T Mobility* which brought arbitration roaring back to life.

However, *AT&T Mobility* left some perceived questions open, apparently for the ever-hopeful. Regrettably for them, there are some cases best not taken to the high Court. Most lawyers could have predicted that the Court meant what it said in *AT&T Mobility*. *Italian Colors* again represents that proverbial *oncoming light* at the end of the dark tunnel. It is the same light which presaged defeat for the plaintiff's attorneys in *AT&T Mobility.*

## Individual Arbitration Compelled in Failure to Maintain Claims?

*Italian Colors* answers this very question with a resounding YES!

According to the Court, arbitration agreements must be strictly enforced by their terms, even when those terms include a *waiver of class action arbitration.* Thus, individual arbitration may be compelled where tenants have signed an arbitration agreement that includes a waiver of class action arbitration.

The Court in its discussion has certainly narrowed the "effective vindication" exception, but there are circumstances that will still trigger the exception including provisions that explicitly forbid the assertion of a statutory right and where administrative fees for arbitration are so high as to make access to arbitration impracticable.

## Conclusion:

The best solution is to avoid "failure to maintain" claims altogether by generating a positive environment and goodwill among the residents, because generally speaking, residents will not sue owners they like or respect.


The Mentor

However, beyond avoiding "failure to maintain" claims altogether, the ONLY way to effectively stop a "failure to maintain" action, once it is beyond consensual mediation or resolved, is by resorting to arbitration. It is always best to avoid the sparks which ignite a movement for suit against the owner. Preventive actions and monitoring, including sensitivity for resident sentiment from the point of view of your residents, is the most effective tool to avoid the FTM. Incorporating arbitration clauses with class action arbitration waivers into all residency documents provides a means by which to quickly, fairly, and inexpensively resolve unavoidable disputes. As such, it is imperative that you have your arbitration agreements amended to:

(1) refer to the holdings of the Supreme Court arbitration cases including *AT&T Mobility* and now, *Italian Colors*;
(2) specifically include a waiver of class action arbitration; and
(3) avoid provisions that might still trigger the "effective vindication" exception.

The effective tool of arbitration is available by reason of a 5-4 majority on the Supreme Court. It is virtually free for the taking. Arbitration clauses signal the end of jury trials and large FTM actions. Updating all residency documents for FAA arbitration (***not*** state sanctioned arbitration), coupled with updated release and indemnification clauses, should be high on the list for all park owners operating in the repressive business climate in California.

Please feel free to call with any questions or comments.