The Arbitration Newsletter

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The Arbitration Newsletter is published periodically by Whitaker Chalk Swindle & Schwartz PLLC, Fort Worth, Texas to explore the rapidly developing law and practice of commercial arbitration both in the U.S. and other countries.[1]

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FEDERAL ARBITRATION ACT ("FAA") PREEMPTION
FERGUSON et al. v. CORINTHIAN COLLEGES, INC.

The Ninth Circuit Court of Appeals has just issued its decision in *Ferguson v. Corinthian Colleges, Inc.*, 733 F.3d 928 (9th Cir.2013), laying out a bright line test for FAA preemption of three California state laws that authorize "public injunctions."[2] A California federal district court declined to compel arbitration of appellants' claims based on the UCL, FAL, and CLRA statutes, although having granted the schools' motion to compel "most of Plaintiffs' claims and stayed those claims pending arbitration."[3] The trial court refused to compel arbitration under these three California statutes based on California Supreme Court's *Broughton-Cruz* rule.[4] *Broughton* found an "inherent conflict" between CLRA's right of a plaintiff to act as a "private attorney general" to enjoin "future deceptive practices" and the parties' right to pre-dispute, contractual arbitration of a public injunction claim.[5] *Cruz* extended the *Broughton* rule to "requests for public injunctive relief under the UCL and FAL."[6]

Citing 1984, 1995, and 2011 U.S. Supreme Court cases, the Ninth Circuit told the appellants (former students[7] of the appellees) that Congress with the enactment of the FAA "withdrew the

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[1] Nothing in *The Arbitration Newsletter* is presented as or should be relied on as legal advice to clients or prospective clients. The sole purpose of *The Arbitration Newsletter* is to inform generally. The application of the comments in *The Arbitration Newsletter* to specific questions and cases should be discussed with the reader's independent legal counsel.

[2] "At issue in this appeal are Plaintiffs' claims under California's unfair competition law ('UCL'), California Business and Professions Code §17200 *et seq.*; false advertising law ('FAL'), California Business and Professions Code §17500 *et seq.;* and Consumer Legal Remedies Act ('CLRA'), California Civil Code §1750 *et seq.*" 733 F.3d at 931 and 938.

[3] 733 F.3d at 931.

[4] *Broughton v. Cigna Healthplans of California*, 21 Cal.4th 1066, 90 Cal.Rptr.2d 334, 988 P.2d 67 (1999) (California Supreme Court found "inherent conflict" between "the purposes of the CLRA and right to arbitrate such claims using the "inherent conflict" analysis in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S.614, 627-28, 105 S.Ct. 3346, 87 L.Ed.2d 444(1985).); *Cruz v. PacificCare Health Systems, Inc.*, 30 Cal.4th 303, 133 Cal.Rptr.2d 58, 66 P.3d 1157, 1164-65 (2003).

[5] 733 F.3d at 932; *citing Broughton*, 90 Cal.Rptr.2d 334, 988 P.2d at 77, 78.

[6] 733 F.3d at 933; *citing Cruz,* 66 P.3d at 1164-65.

[7] The two plaintiffs/appellants were putative representatives of two separate putative class action groups. Appellant Ferguson's enrollment agreement in addition to a jury trial waiver stated: "I agree that any dispute arising from my enrollment, no matter how described, pleaded or styled, shall be resolved by binding arbitration under the Federal Arbitration Act." Appellant Muniz's enrollment agreement in addition to a jury trial waiver stated: "I … agree that any dispute arising from my enrollment at Heald College … no matter how described, pleaded or styled, shall be resolved by binding arbitration." 733 F.3d at 738.

power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration";[8] that the court is "thus prohibited from applying any state statute that invalidates an arbitration agreement";[9] and that the court cannot "apply any other state law that 'prohibits the arbitration of a particular type of claim'."[10] The court reversed and remanded to the trial court with directions "to grant the motion [to compel] as to all claims, including Plaintiffs' injunctive relief claims, and to stay the lawsuit pending arbitration."[11]

The Ninth Circuit's rationale for its reversal and remand started with citation to *AT&T Mobility LLC v. Concepcion*, --U.S.--, 131 S.Ct. 1740, 179 L.Ed.2d 742 (2011) in which the U.S. Supreme Court had previously struck down California's *Discover Bank* rule based on FAA preemption.[12] The court also cited *Marmet Health Care Center, Inc. v. Brown*, --U.S.--, 132 S.Ct. 1201, 182 L.Ed.2d 42 (2012) (per curiam) for the reiteration of the *Concepcion* holding.[13] Since the *Broughton-Cruz* rule "similarly prohibits outright arbitration of a particular type of claim," under the CLRA, UCL, and FAL, the rule is preempted by the FAA.[14]

The Ninth Circuit also rejected appellants' contention that "an injunction is technically a remedy rather than a cause of action" and, therefore, "insulated [the rule] from the FAA."[15] The court did not so read "recent Supreme Court decisions" to give the FAA such a technical reading of "claim."[16] These recent U.S. Supreme Court decisions "have given broad effect to arbitration agreements."[17] Earlier in 2013, the Ninth Circuit observed, the U.S. Supreme Court "reiterated that 'courts must 'rigorously enforce' arbitration agreements according to their terms."[18] Any attempts to limit what parties can agree regarding an arbitrator's powers, including the power to grant injunctive relief, [19] was settled in *Mastrobuono v. Shearson Lehman Hutton, Inc.*[20] and in *Marmet*.[21]

The Ninth Circuit also rejected appellants' attempts to argue "inherent conflict" between the three state statutes in question and FAA arbitration. The court explained that the "inherent conflict analysis" drawn from *Mitsubishi Motors Corp.*[22] is only for claims brought under federal statutes,

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[8] 733 F.3d at 932, *citing Southland Corp. v. Keating*, 465 U.S. 1, 10, 104 S.Ct.852, 79 L.Ed.2d 1 (1984).
[9] 733 F.3d at 932, *citing Allied-Bruce Terminix Cos., Inc. v. Dobson*, 513 U.S. 265, 272, 115 S.Ct. 834, 130 L.Ed.2d 753 (1995).
[10] 733 F.3d at 932, *citing AT&T Mobility LLC v. Concepcion,* --U.S.--, 131 S.Ct. 1740, 1748, 179 L.Ed.2d 742 (2011).
[11] 733 F.3d at 938.
[12] 733 F.3d 934 (The *Discover Bank* rule "invalidated most class action waivers in adhesion contracts, including arbitration agreements, as unconscionable.").
[13] *Id., citing Marmet*, 132 S.Ct. at 1203 ("As this Court reaffirmed last Term, '[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.' That rule resolves these [three nursing home negligence] cases."; quoting *Concepcion*, 131 S.Ct. at 1747).
[14] 733 F.3d at 934.
[15] *Id.*
[16] *Id.*
[17] 733 F.3d at 934-35.
[18] 733 F.3d at 935; *citing Am. Express Co. v. Italian Colors Rest.,* --U.S.--, 133 S.Ct. 2304, 2309, 186 L.,Ed.2d 417 (2013) (quoting *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 221, 105 S.Ct. 1238, 84 L.Ed.2d 158 (1985).
[19] The court rests the arbitrator's power to grant injunctive relief on "if the arbitration agreement at issue permits it," leaving to the arbitrator to interpret the parties' agreement regarding power to grant injunctive relief. Appellees conceded that approach as correct. 733 F.3d at 937.
[20] 733 F.3d at 935; citing *Mastrobuono*, 514 U.S. 52, 115 S.Ct. 1212, 131 L.Ed.2d 76 (1995).
[21] 733 F.3d at 935; quoting *Marmet*, 132 S.Ct. at 1204 ("FAA pre-empts state law[s] requiring judicial resolution of claims involving punitive damages.").
[22] 733 F.3d at 935-36; *citing Mitsubishi Motors Corp.*, 473 U.S. 614, 627-28, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985).

not state statutes as in this case.[23] The Supremacy Clause's "central premise ... is that federal law is superior to state law."[24] When state law conflicts with the FAA and thereby "frustrates the FAA's purposes and objectives," the FAA preempts the conflicting state laws.[25]

The *Broughton* case also justified its decision not to compel arbitration of public injunctions based "on the institutional advantages of the judicial forum" over the arbitration forum.[26] This argument was thoroughly discussed and rejected in *Concepcion*,[27] according to the Ninth Circuit. State rules that "disfavor arbitration," as explained in *Concepcion*, regardless of how "desirable for unrelated reasons" cannot override or prohibit FAA arbitration.[28]

Although the Ninth Circuit left the power to issue injunctive relief to the arbitrator, it did proceed to decide the scope of the parties' arbitration agreement.[29] The court looked at the express terms of the arbitration agreement, remembering that "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration," and concluded "that Plaintiffs' claims do fall within the scope of their arbitration agreements."[30]

OBSERVATIONS

1. *Ferguson* is another opinion that illustrates how critically important to getting disputes arbitrated is the drafting of the arbitration agreement.

2. The Ninth Circuit, mostly interpreting California arbitration cases, has been liberal with its support of trial court denials of motions to compel arbitration. But in *Ferguson* the court weighed in strongly in favor of FAA preemption of any state law or rule that would frustrate the objectives and purposes of the FAA.

3. Be careful what you ask for! Appellants in *Ferguson* argued "scope" **in the alternative** after the Ninth Circuit had left to the arbitrator to determine the arbitrator's "power" to grant injunctive relief, in return for which the appellants got a finding (as the law of the case) that all the appellants' claims were within the scope of the parties' arbitration agreement.
4. *Ferguson* is an interesting example of broad form arbitration agreements by use of "any dispute arising from my enrollment, no matter how described, pleaded or styled."

5. The former student parties in *Ferguson* also agreed to waive a jury trial in addition to their broad form arbitration clause.

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[23] 733 F.3d at 935-36 ("Both [the effective vindication and inherent conflict] exceptions are reserved for claims brought under federal statutes.").
[24] 733 F.3d at 936.
[25] *Id.*; *citing* Justice Kagan's dissent in *Italian Colors* and *Nitro-Lift Technologies, LLC v. Howard*, --U.S.--, 133 S.Ct. 500, 504, 184 L.Ed.2d 328 (2012).
[26] 733 F.3d at 936; *citing Broughton*, 90 Cal.Rptr.2d 334, 988 P.2d at 77.
[27] 733 F.3d at 936; *citing Concepcion*, 131 S.Ct. at 1747.
[28] 733 F.3d at 936; *citing Concepcion*, 131 S.Ct. at 1747.
[29] Appellants raised the scope question in the alternative. 733 F.3d at 937.
[30] 733 F.3d at 937-38; *citing Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).

6. The parties' arbitration agreements also wisely adopted the FAA as the applicable arbitration law. Who knows what would have happened with the *Broughton-Cruz* rule in *Ferguson* if the parties' arbitration agreement had explicitly adopted the California state arbitration law or had left open what arbitration law applied.[31]

[31] As an example, *Hall Street* limitations on party autonomy to choose expanded judicial review under the FAA do not apply under the Texas General Arbitration Act. *See Nafta Traders, Inc. Inc. v. Quinn*, 339 S.W.3d 84, 101 (Tex. 2011) *cert. denied,* 132 S. Ct. 455, 181 L. Ed. 2d 295 (U.S. 2011).