No. 14-1458

In The Supreme Court of the United States

MHN GOVERNMENT SERVICES, INC., et al.,

Petitioners,

v.

THOMAS ZABOROWSKI, et al.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the Ninth Circuit's unpublished memorandum disposition errs in recognizing that the Federal Arbitration Act does not preempt application of California's general law of contract severability to a contract with five distinct unconscionable provisions.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

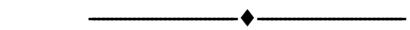
STATUTORY PROVISIONS

TABLE OF AUTHORITIES—Continued

STATUTORY PROVISION INVOLVED

California Civil Code Section 1670.5(a) provides:

> If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.



INTRODUCTION

California contract law authorizes trial courts to decide whether to sever unconscionable provisions from a contract or refuse to enforce the contract as a whole, depending on the degree of unconscionability. This discretion is guided by an equitable standard and applies to all contracts whether or not they involve arbitration. California state and federal courts exercise this discretion regularly. Sometimes they sever any unconscionable provisions and enforce the remainder of a contract; and sometimes, where the unconscionability is pervasive, they decline to sever, deeming the entire contract unenforceable.

Here, the district court exercised this discretion with respect to an arbitration agreement containing five substantively unconscionable provisions. Weighing the interests of justice and its capacity to

cure the agreement, the court decided against severing those provisions and enforcing the remainder. The court of appeals affirmed in an unpublished decision, correctly concluding that the district court had not abused its discretion. At the same time, the Washington Supreme Court held 9-0 that the very same agreement was permeated by unconscionability and unenforceable under California law. *See Brown v. MHN Gov't Servs., Inc.*, 178 Wash. 2d 258, 275-76 (2013). In all, over a dozen judges have refused to enforce Petitioners' agreement, finding that an array of unfair provisions permeate it with unconscionability.

Petitioners (collectively "MHN") do not contest here that their agreement has several unconscionable components. Instead they seek review of the court of appeals' non-precedential application of California's severance doctrine, claiming that it conflicts with precedent from this Court and other courts of appeals, and that it conflicts with the Federal Arbitration Act ("FAA") by discriminating against arbitration.

Petitioners are mistaken. California's severance doctrine derives from statutes that apply to all contracts and from cases dealing with contracts of various sorts—not just arbitration agreements. The doctrine applies to all contracts equally, consistent with the FAA and this Court's precedent. Where there are multiple unconscionable provisions, the doctrine neither requires nor prohibits severance, but instead vests discretion in the trial court. In short,

Petitioners complain about the court of appeals' application of arbitration-neutral statutory and case law that is consistent with the FAA and this Court's interpretation of it.

The court of appeals' decision does not create a conflict with the courts of appeals cited by Petitioners, both because it creates no precedent (being unpublished) and because it is fully consistent with the decisions of those courts. To the extent that they address severability at all, those decisions simply reflect the well-recognized fact that agreements with one or two unconscionable provisions can often be severed and enforced. None of them hold that an agreement as rife with unconscionability as this one must always be enforced. In fact, most of them explicitly acknowledge that agreements can be so unconscionable as to be unenforceable. Given the large number of unconscionable provisions that permeate Petitioners' agreement with unconscionability, there is no reason to think that these courts would have reached a different result in this case.

Petitioners may regret crafting an arbitration contract so tainted by unconscionability. In fact, soon after this case was filed, Petitioners redrafted their arbitration contract in a much fairer way, abandoning seven elements criticized by Respondents in this litigation, and began using this restructured version with new employees. *See* App. 22a-24a. But in this litigation, Petitioners are still responsible for their original choice. They cannot escape the consequences of their initial overreaching by offering to withdraw

unconscionable terms after the fact, as more than a dozen judges have found.

Finally, this case is a poor vehicle for review because the California Supreme Court has recently decided a major case concerning the scope of California's unconscionability doctrine, and many cases involving severability that had been deferred pending that decision are likely to be reconsidered in the near future.

STATEMENT

This petition arises from a conditionally certified collective action under the Fair Labor Standards Act ("FLSA") on behalf of 751 Military and Family Life Consultants who provide financial counseling, child services, and victim advocacy counseling at U.S. Military installations nationwide. Respondents allege that MHN, a behavioral health subcontractor to the Federal Government, misclassified them as independent contractors and as exempt from the overtime pay protections of the FLSA and various state laws. They seek overtime wages and other classwide relief.

Respondents filed this action in October 2012. MHN moved to compel arbitration in November 2012. The district court denied MHN's motion in April 2013. Pet. App. 30a. The court found that under California law, MHN's arbitration agreement was procedurally unconscionable, *id.* at 19a, and five of its provisions were substantively unconscionable. *Id.* at 21a-22a,

24a-26a (truncated statute of limitations, arbitrator selection clause stacked in the drafter's favor, imposition of onerous fees on non-drafting parties, potential liability for attorneys' fees and costs against prevailing party in contravention of federal and state law, and limitation on punitive damages). The district court noted that California law gives trial courts discretion whether to sever (or restrict) unconscionable provisions or refuse to enforce the entire agreement. *Id.* at 28a-29a (citing Cal. Civ. Code § 1670.5(a) and *Armendariz v. Found. Health Psychcare Servs., Inc.*, 24 Cal. 4th 83, 122 (2000)). Following Ninth Circuit precedent applying California law, the court turned its attention to "whether the offending clause or clauses are merely 'collateral' to the main purpose of the arbitration agreement, or whether the [arbitration agreement] is 'permeated' by unconscionability." *Id.* at 29a (alteration in original) (quoting *Davis v. O'Melveny & Myers*, 485 F.3d 1066, 1084 (9th Cir. 2007)). The district court then noted that "[t]he finding of 'multiple unlawful provisions' allows a trial court to conclude that 'the arbitration agreement is permeated by an unlawful purpose.'" *Id.* (quoting *Armendariz*, 24 Cal. 4th at 124). To illustrate its discretion, the district court compared, on the one hand, two cases in which multiple unconscionable provisions were not severed, *id.* (citing *Davis*, 485 F.3d at 1084, and *Graham Oil Co. v. Arco Prods. Co.*, 43 F.3d 1244, 1247 (9th Cir. 1994)), with, on the other hand, two cases in which one and three unconscionable provisions were severed, respectively. *Id.* (citing *Lara v. Onsite Health, Inc.*, 896 F. Supp. 2d 831, 848 (N.D.

Cal. 2012), and *Grabowski v. Robinson*, 817 F. Supp. 2d 1159, 1179 (S.D. Cal. 2011)).

The district court concluded that Petitioners' arbitration agreement was "permeated with unconscionability" because it was "an adhesive contract that contains oppression and surprise," with "substantively unconscionable provisions rang[ing] from the method of selecting the arbitrator, the shortened statute of limitations, and limits on statutory remedies, to the filing fees and the allocation of fees and costs." *Id.* at 30a. Adding that "[t]he Court could not 'attempt to ameliorate the unconscionable aspects' of the Agreement without . . . 'assum[ing] the role of contract author rather than interpreter,'" the district court concluded that the five unconscionable provisions were not severable. *Id.* (quoting *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165, 1180 (9th Cir. 2003)). It therefore denied MHN's motion to compel arbitration.

The court of appeals affirmed in an unpublished memorandum disposition. Pet. App. 1a-2a. It agreed with the district court that MHN's arbitration agreement was procedurally unconscionable and that five of its provisions were substantively unconscionable. *Id.* at 2a-4a. The court of appeals further held that the district court had not abused its discretion by declining to sever the unconscionable provisions and enforce the remainder of the arbitration agreement. *Id.* at 5a. Acknowledging that the FAA "expresses a strong preference for the enforcement of arbitration agreements," the court also noted that "the Act does

not license a party with superior bargaining power 'to stack the deck unconscionably in [its] favor' when drafting the terms of an arbitration agreement." *Id.* (alteration in original) (quoting *Ingle*, 328 F.3d at 1180). The court noted that "[u]nder generally applicable severance principles, California courts refuse to sever when multiple provisions of the contract permeate the entire agreement with unconscionability." *Id.* (citing *Samaniego v. Empire Today LLC*, 205 Cal. App. 4th 1138, 1149 (2012)). Because the district court had found such permeation, and because that finding was not "illogical, implausible, or without support in inferences that may be drawn from the facts in the record," the court of appeals concluded that the district court had acted within its discretion in opting not to sever the five unconscionable provisions. *Id.* (quoting *United States v. Hinkson*, 585 F.3d 1247, 1263 (9th Cir. 2009) (en banc)). Finally, the court of appeals held that its application of the "general principles of California unconscionability law" was balanced—not "impermissibly unfavorable to arbitration." *Id.* at 5a-6a (citing *Chavarria v. Ralph's Grocery Co.*, 733 F.3d 916, 926-27 (9th Cir. 2013)). The court of appeals found the district court's exercise of discretion to be consistent with the FAA's exception for generally applicable state contract laws that apply equally to all contracts, including arbitration agreements. *Id.*

Judge Gould dissented in part, explaining that he would have required severance. Pet. App. 7a-11a. In his view, the California Supreme Court in

Armendariz had reasoned that "multiple unconscionable provisions *will* render an arbitration agreement's purpose unlawful." *Id.* at 8a (emphasis added). Such reasoning, Judge Gould argued, "has 'a disproportionate impact on arbitration agreements' and should have been preempted by the" FAA. *Id.* (quoting *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1747 (2011)). In Judge Gould's view, "*Concepcion* and its progeny should create a presumption in favor of severance when an arbitration agreement contains a relatively small number of unconscionable provisions that can be meaningfully severed and after severing the unconscionable provisions, the arbitration agreement can still be enforced." *Id.* Judge Gould disagreed with the district court's determination that enforcing the remainder of the agreement would require the district court to "assume the role of contract author." *Id.* Although he "recognize[d] that one can imagine an arbitration agreement where the number and content of unconscionable provisions are so pervasive that they rebut the presumption in favor of severance," and that in such a case, "it would then be within a district court's discretion not to sever the unconscionable provisions and not to enforce the arbitration agreement," Judge Gould did "not view the challenged provisions here as being sufficient to rebut a presumption in favor of severance that I urge should arise under *Concepcion* on the facts here." *Id.* at 11a n.1.

MHN petitioned for rehearing en banc in January 2015. Pet. App. 32a. The petition was denied in

February 2015 with no judge on the panel or the court of appeals having requested a vote to rehear the matter en banc. *Id.*

REASONS FOR DENYING THE WRIT

Because the Ninth Circuit's decision is correct and does not conflict with any decision of this Court or another court of appeals, it does not warrant this Court's review.

I. California's Law of Contract Severability Treats All Contracts Equally and Is Therefore Consistent with the FAA.

This Court has made clear that arbitration agreements must be placed "on an equal footing with other contracts." *Concepcion*, 131 S. Ct. at 1745. Contract defenses that apply generally to all contracts may be applied to arbitration agreements in particular, so long as they are not "applied in a fashion that disfavors arbitration." *Id.* at 1746-47.

California, like many states, has a statute directing courts to avoid enforcement of unconscionable terms in contracts. The state legislature has provided that courts have the discretion to (1) refuse to enforce a contract containing unconscionable terms, (2) sever the unconscionable terms and enforce the remainder of the contract, or (3) limit the application of those unconscionable terms to avoid an unconscionable result. State and federal courts routinely exercise this

discretion in deciding whether to enforce arbitration and non-arbitration contracts alike. Sometimes they refuse to enforce the contract; sometimes they sever the offending provisions.

There is no categorical rule. Rather, factfinders must weigh the interests of justice. The standard is equitable and fact-specific, leaving room for reasonable disagreement as to whether severance is appropriate in a given case. California courts apply this standard evenhandedly to contracts of all kinds, including arbitration agreements. The outcomes vary with the specific facts of each case.

In line with this discretion, there are many examples of California courts severing unconscionable provisions to preserve and enforce arbitration agreements. Of course, some agreements are so permeated with unconscionability a trial court is within its discretion to conclude that no surgery can cure it. Petitioners' agreement, which contains *five* distinct unconscionable provisions, is a case in point.

A. California Severance Doctrine Derives from General Contract Law Codified by Statute and Applies in Arbitration and Non-Arbitration Cases Alike.

The California Legislature has given courts discretion to handle unconscionable contract provisions in one of three ways:

> If the court as a matter of law finds the contract or any clause of the contract to have

> been unconscionable at the time it was made [1] the court may refuse to enforce the contract, or [2] it may enforce the remainder of the contract without the unconscionable clause ["severance"], or [3] it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

Cal. Civ. Code § 1670.5(a). This statute applies evenly to all contracts.

Section 1670.5(a) reflects an approach to unconscionability that has been widely adopted across the various States. It employs the exact language of § 2-302 of the Uniform Commercial Code, expanding coverage to noncommercial contracts. *Cf. IMO Dev. Corp. v. Dow Corning Corp.*, 135 Cal. App. 3d 451, 459 (1982) ("Section 1670.5 codifies the judicially developed doctrine of unconscionability and is identical to section 2-302 of the Uniform Commercial Code which has long been adopted by the majority of states."); Restatement (Second) of Contracts § 208 (1981) (also following U.C.C. § 2-302).

The Legislative Comments to § 1670.5 confirm that it gives courts "discretion" to "refuse to enforce the contract as a whole if it is permeated by the unconscionability, or [to] strike any single clause or group of clauses which are so tainted or which are contrary to the essential purpose of the agreement, or [to] simply limit unconscionable clauses so as to avoid unconscionable results." California courts thus have the discretion to refuse to enforce the contract as a whole if it is "permeated" by unconscionability.

The California Supreme Court first had occasion to interpret the permeation standard in *Armendariz*. *See* 24 Cal. 4th at 122 ("We could discover no published cases in California that address directly the question of when a trial court abuses its discretion by refusing to enforce an entire agreement, as the trial court did in this case, nor precisely what it means for an agreement to be 'permeated' by unconscionability."). In deciding how lower courts should exercise their discretion to sever unconscionable terms, the California Supreme Court turned to the statutes and case law governing the severability of *illegal* (as opposed to unconscionable) contract terms.[1] *See id.* (citing Cal. Civ. Code §§ 1598 and 1599). The court examined cases involving contracts of various types, including sales contracts, landlord-tenant contracts, attorney fee agreements, and covenants not to compete. *See id.* at 122-24. Six of the eight cases relied on did not touch on arbitration. *Id.* The court also analogized unconscionable contract provisions to unlawfully broad covenants not to compete, which "courts have tended to invalidate rather than restrict." *Id.* at 124 n.13 (citing Farnsworth on Contracts § 5.8, p. 86, n.23 (2d ed. 1988)). The court reasoned that an overly solicitous severance rule would "encourage[ ] . . . employers . . . to overreach," by "routinely inserting . . . a deliberately illegal clause" into contracts, "know[ing]

[1] Illegal (i.e., "unlawful") terms are those whose very performance would require an illegal act or omission. *See* Cal. Civ. Code §§ 1595, 1599, 1667.

that the worst penalty for such illegality is the severance of the clause after the employee has litigated the matter." *Id.*

From its broad survey of general contract law, the *Armendariz* court identified "basic principles of severability that . . . appear fully applicable to the doctrine of unconscionability": Severance is inappropriate where "the central purpose of the contract is tainted with illegality," but it is appropriate "[i]f the illegality is collateral to the main purpose of the contract, and the illegal provision can be extirpated from the contract by means of severance or restriction." *Id.* at 124. "The overarching inquiry is whether 'the interests of justice . . . would be furthered' by severance. Moreover, courts must have the *capacity* to cure the unlawful contract through severance or restriction of the offending clause, which . . . is not invariably the case." *Id.* at 123-24 (citations omitted).

Eight years later, the California Supreme Court addressed the severability of a non-arbitration contract. *Marathon Entm't, Inc. v. Blasi*, 42 Cal. 4th 974 (2008), *as modified* (Mar. 12, 2008). Maintaining consistency in the law's approach to illegal and unconscionable terms in all contracts, the court reemphasized that trial courts enjoy substantial discretion: "the full voiding of the parties' contract is available, but not mandatory; likewise, severance is available, but not mandatory." *Id.* at 996. To guide trial courts in exercising that discretion, the *Marathon* court went on to reiterate the basic principles distilled in *Armendariz*. *Id.* The court remanded for the trial court to conduct

a fact-specific severability analysis under those principles. *Id.* at 999.

As applied to unconscionable contract provisions, California's general doctrine of severability can thus be summarized as follows. If (1) the unconscionability does not permeate the contract (in other words, if the unconscionability does not taint the central purpose of the contract but is instead collateral to it) *and* (2) the court has the capacity to cure the contract by severing or restricting the offending clause(s), then severance is appropriate. Whether the unconscionability permeates the contract (that is, taints its central purpose) depends on whether enforcing the remainder would serve the interests of justice. This depends, in turn, on whether such enforcement would prevent undeserved benefit or detriment, and whether it would conserve a contractual relationship without condoning an illegal scheme. *Armendariz*, 24 Cal. 4th at 123-24. Whether a court has the capacity to cure a contract through severance depends on whether severing the offending clause(s) would require it to add terms to the contract, which California courts lack the power to do. *See id.* at 125. If severance would fail to serve the interests of justice *or* require a court to assume the role of contract author, then severance is not appropriate.

In this way, California's severance doctrine derives from statutes and case law that apply to all contracts. It is unsurprising, then, that even though the doctrine happens to have been distilled in a case involving an arbitration agreement (*Armendariz*), it

applies evenhandedly to contracts of all sorts. As discussed below, California courts have applied this standard equitably, finding some non-arbitration contracts unenforceable, and finding some arbitration contracts severable.

B. California Courts Apply the Same Equitable, Discretionary Severance Standard to All Contracts.

Petitioners argue that California applies a more stringent severance standard to arbitration agreements than to other types of contracts. In fact, the standard is the same for all contracts. Petitioners obscure this fact by describing the equitable, discretionary standard derived from § 1670.5 as though it were a categorical rule, and by inviting a mistaken reading of California law.

Armendariz itself illustrates the discretionary nature of the standard established by the Legislature. The court held that the presence of multiple unconscionable provisions in the agreement at issue "*indicate*[*d*] a systematic effort" to achieve an unlawful purpose, *justifying* the trial court's exercise of discretion to not sever. *Armendariz*, 24 Cal. 4th at 124 (emphasis added). The *Armendariz* court did not say that drafting multiple unconscionable provisions *constituted* a systematically unlawful effort or *required* severance. Rather, such overreaching supported the trial court's exercise of discretion.

It is therefore misleading for Petitioners to claim, as they do repeatedly, that *Armendariz* established an "arbitration-only anti-severance rule." Pet. 2, 10, 14, 15, 17, 18. The only "rule" is that courts must exercise their discretion in light of the interests of justice and the curability of the contract, no matter what the contract is about.

1. California's Severance Doctrine Is Not "Arbitration-Only."

The standard is not "arbitration-only," because it applies to contracts of all kinds. California courts have applied the state's severability standard to non-arbitration contracts in a variety of settings. *See, e.g.*, *MKB Mgmt., Inc. v. Melikian*, 184 Cal. App. 4th 796, 805 (2010) (holding that "the doctrine of severability may apply" to a property management agreement, "in the discretion of the trial court"); *Greenlake Capital, LLC v. Bingo Investments, LLC*, 185 Cal. App. 4th 731, 740 (2010) (reversing summary judgment and remanding for equitable consideration of severance issue in connection with financing agreement); *Shopoff & Cavallo LLP v. Hyon*, 167 Cal. App. 4th 1489, 1523 (2008) ("granting recovery under a contingent fee agreement although the charging lien may be invalid is consistent with the law of severability of contracts" when it would avoid an "unfair windfall").

And in so applying this neutral standard to non-arbitration contracts, California courts have sometimes exercised their discretion not to sever, finding

an entire contract unenforceable. *See, e.g.*, *Summit Media LLC v. City of Los Angeles*, 211 Cal. App. 4th 921, 938 (2012) (affirming lower court's refusal to sever unlawful zoning exemption from settlement agreement); *Chiba v. Greenwald*, 156 Cal. App. 4th 71, 81-82 (2007) (upholding lower court's decision not to sever unlawful portions of personal management contract). On the other hand, California courts sometimes exercise their equitable discretion to sever. *See, e.g.*, *Templeton Dev. Corp. v. Superior Court*, 144 Cal. App. 4th 1073, 1084 (2006) (severing faulty mediation provision to avoid conferring "undeserved benefit").

2. California's Severance Doctrine Is Not "Anti-Severance" as Applied to Arbitration Agreements.

Likewise, California's fact-sensitive severance standard is not "anti-severance" as applied to arbitration agreements. Petitioners argue that California courts take a more severance-friendly approach in non-arbitration cases. Pet. 12-16. But the approach Petitioners describe is based on a twofold misunderstanding of California law.

First, California law does not "generally prohibit[ ]" non-severance just because a contract has some lawful purposes, as Petitioners claim. Pet. 12 (citing

Cal. Civ. Code §§ 1599 and 1670.5).[2] The severance of illegal provisions under § 1599, like the severance of unconscionable provisions under § 1670.5, is always discretionary. "[S]everance is not mandatory and its application in an individual case must be informed by equitable considerations. [Section] 1599 grants courts *the power, not the duty*, to sever contracts in order to avoid an inequitable windfall or preserve a contractual relationship where doing so would not condone illegality." *Marathon*, 42 Cal. 4th at 992 (emphasis added) (citation omitted) (citing *Armendariz*, 24 Cal. 4th at 123-24); *see also Chiba*, 156 Cal. App. 4th at 81; *Yoo v. Robi*, 126 Cal. App. 4th 1089, 1105 (2005), *as modified on denial of reh'g* (Mar. 9, 2005). *Armendariz* harmonized the treatment of illegal provisions under § 1599 and unconscionable provisions under § 1670.5(a) by making clear that trial courts have the same guided discretion with respect to both types of defect: the "court may refuse to enforce the contract, or it may enforce the remainder." 24 Cal. 4th at 121.

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[2] Nor did the California Supreme Court hold in *Birbrower, Montalbano, Condon & Frank v. Superior Court*, 17 Cal. 4th 119, 138 (1998), *as modified* (Feb. 25, 1998), that non-severance is allowed "[o]nly '[i]f the court is unable to distinguish between the lawful and unlawful parts of the agreement,' " as Petitioners assert. Pet. 13 (second alteration in original). By inserting the word "only" before the quotation, Petitioners convert what the *Birbrower* court treated as a *sufficient* condition for discretionary non-severance into a *necessary* condition for it.

Second, contrary to Petitioners' assertion, California law has no rule by which the presence of "more than one unconscionable provision automatically . . . allows a court, without further inquiry, to decline to sever." Pet. 15-16. Rather, California law calls for trial courts assessing severability to weigh the interests of justice and to consider whether they can fairly rid the contract of the taint of unconscionability by excising (or restricting) the unconscionable provisions.[3] That is what the district court did in this case,[4]

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[3] Petitioners' amicus similarly misstates the law: "Under . . . *Armendariz* . . . , if a court finds 'more than one unlawful provision' in an arbitration agreement to be unconscionable, it *will* deny severance and refuse to enforce the agreement in its entirety." Pac. Legal Found. Amicus Br. 2 (emphasis added). That is incorrect. *See also id.* at 2-3 (misstating the facts in claiming that the court of appeals here "[a]ppl[ied] this principle"); *id.* at 3 (describing the court of appeals as having applied "the *Armendariz* severance rule: that a court should refuse to sever unconscionable provisions in an arbitration agreement, whether or not the offensive provisions permeate and infect the entirety of the contract"). Again, the presence of multiple unconscionable provisions is merely an indicator of permeation, not a substitute for a finding thereof.

[4] In describing the district court's conclusion that the five unconscionable provisions supported a finding of permeation, Petitioners suggest misleadingly that the contract's being an arbitration agreement was crucial. Pet. 8 (describing the district court as having held that it is proper to find such support "when the contract at issue is an arbitration agreement"). The fact that the five unconscionable provisions occurred in an *arbitration* agreement was of no moment. Neither *Armendariz* nor the district court here even hinted—much less held—that the presence of multiple unlawful provisions had special significance for arbitration agreements alone.

and that is why the court of appeals was correct to find no abuse of discretion.

In short, Petitioners' claim that there is a special severance standard for arbitration contracts has no basis in California law. The California Legislature has adopted the Uniform Commercial Code's generally applicable contract principles; the California Supreme Court has interpreted those principles in light of general contract law; and California courts have applied the resulting doctrine equitably. The result is a single discretionary standard for all contracts. This standard gets applied in a variety of contexts. Sometimes severance is the result; sometimes it is not. As the California Supreme Court made clear in the non-arbitration context in *Marathon*,

> Inevitably, no verbal formulation can precisely capture the full contours of the range of cases in which severability properly should be applied, or rejected. The doctrine is equitable and fact specific, and its application is appropriately directed to the sound discretion of the Labor Commissioner and trial courts in the first instance.

42 Cal. 4th at 998.

The standard is discretionary in practice as well as in principle, as is demonstrated by the many California courts that have recently done exactly what Petitioners suggest California law prohibits: sever multiple unconscionable provisions in order to save an arbitration agreement. *See, e.g.*, *Pope v.*

Sonatype, Inc., No. 05 Civ. 0956, 2015 WL 2174033, at *6 (N.D. Cal. May 8, 2015) (three provisions severed); *Grabowski*, 817 F. Supp. 2d at 1178-79 (three provisions severed); *Arreguin v. Global Equity Lending, Inc.*, No. 07 Civ. 6026, 2008 WL 4104340, at *8 (N.D. Cal. Sept. 2, 2008) (two provisions severed); *Bencharsky v. Cottman Transmission Sys., LLC*, 625 F. Supp. 2d 872, 883 (N.D. Cal. 2008) (three provisions severed);[5] *Lucas v. Gund, Inc.*, 450 F. Supp. 2d 1125, 1134 (C.D. Cal. 2006) (two provisions severed); *Bolter v. Superior Court*, 87 Cal. App. 4th 900, 910 (2001) (three provisions severed). Petitioners' amicus cites several such cases as evidence that "[n]ot all federal courts, applying California law, uncritically accept the *Armendariz* no-more-than-one rule." Pac. Legal Found. Amicus Br. 7-8. But what these cases actually show is that *there is no such rule*.[6]

II. The Ninth Circuit's Decision Does Not Conflict with This Court's Precedent.

Contrary to Petitioners' claims, California courts have embraced this Court's decision in *Concepcion*,

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[5] *Bencharsky* was decided by the same district court judge who decided the present case below, Judge Illston. *See* 625 F. Supp. 2d at 874; Pet. App. 30a.

[6] Respondents have not found a case involving as many unconscionable aspects as Petitioners included in their arbitration agreement. Presumably there are contracts with five major components that are unconscionable. But if so, they appear to be quite rare.

taking to heart its clarification of the "limits the FAA places on state unconscionability rules as they pertain to arbitration agreements." *Sonic-Calabasas A, Inc. v. Moreno*, 57 Cal. 4th 1109, 1143 (2013), *cert. denied*, 134 S. Ct. 2724 (2014) (noting that *Concepcion* "make[s] clear" that facially neutral state law "must not disfavor arbitration *as applied* by imposing procedural requirements that 'interfere[ ] with fundamental attributes of arbitration'" (second alteration in original) (quoting *Concepcion*, 131 S. Ct. at 1748, 1751)); *see also Sanchez v. Valencia Holding Co., LLC*, No. S199119, 2015 WL 4605381, at *6 (Cal. Aug. 3, 2015). Indeed, the California Supreme Court has held several California laws to be preempted by the FAA in light of *Concepcion*'s guidance. *See Sanchez*, 2015 WL 4605381, at *15 ("[T]he CLRA's anti-waiver provision is preempted insofar as it bars class waivers in arbitration agreements covered by the FAA."); *Iskanian v. CLS Transp. Los Angeles, LLC*, 59 Cal. 4th 348, 366 (2014), *cert. denied*, 135 S. Ct. 1155 (2015) ("We thus conclude in light of *Concepcion* that the FAA preempts the *Gentry* rule."); *Sonic-Calabasas*, 57 Cal. 4th at 1139 ("[T]he FAA as construed by *Concepcion* preempts *Sonic I*'s rule categorically prohibiting waiver of a Berman hearing in arbitration agreements."). This is hardly the conspiracy to evade the FAA that Petitioners depict.

Petitioners echo Judge Gould's partial dissent below, arguing that California's severance doctrine "should have been preempted" by the FAA because it "has a disproportionate impact on arbitration

agreements." Pet. 16 (internal quotation marks omitted). But they do not say what this last phrase means. One thing it cannot mean is: "affects arbitration agreements at a higher rate than contracts of other types." For on that reading, drafters of arbitration agreements could render *any* provision (no matter how unconscionable) immune to application of neutral contract law analysis simply by including that provision in sufficiently many arbitration agreements. For example, if it became standard practice to add unconscionable provisions to arbitration agreements in bad faith—a form of overreaching that many states aim to deter—perfectly neutral state laws disfavoring the severance of such provisions would come to be preempted by the FAA (that is, unless drafters of other types of contracts kept pace). Should an empirical study reveal that arbitration agreements happen to be likelier than contracts of other kinds to be grossly one-sided, it would immediately follow, on that crude reading of *Concepcion*, that state laws limiting the enforcement of grossly one-sided contracts are preempted by the FAA. Surely that was not Congress's intent. *Cf. Chavarria*, 733 F.3d at 927 (noting that "'disproportionate impact' . . . cannot be read to immunize all arbitration agreements from invalidation no matter how unconscionable they may be, so long as they invoke the shield of arbitration").

Here, the district court heeded its duty to "place arbitration agreements on an equal footing with other contracts." Pet. App. 15a (quoting *Concepcion*, 131

S. Ct. at 1745-46 (reaffirming that 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," including "generally applicable contract defenses, such as fraud, duress, or unconscionability" (quoting 9 U.S.C. § 2) (internal quotation marks omitted))). It applied a generally applicable contract defense precisely as state law requires. The state doctrine governing that defense was drawn from general contract law, for contracts generally. The court of appeals upheld the district court's exercise of discretion under the appropriate standard of review and determined that the governing state doctrine was consistent with the purposes of the FAA. At no point did either court single out arbitration for unfavorable treatment. Their decisions thus comported with this Court's precedent.

III. The Ninth Circuit's Decision Does Not Conflict with Those of Other Courts of Appeals.

Petitioners argue that the ruling below "puts the Ninth Circuit squarely in conflict with at least four other courts of appeals." Pet. 18. This is false both legally and factually.

It is impossible as a matter of law because the court of appeals' decision is an unpublished memorandum disposition, which is "not precedent." Pet. App. 1a; 9th Cir. R. 36-3(a). The panel does not speak for the Ninth Circuit, so its disposition simply cannot put the Ninth Circuit into conflict with other courts of

appeals. To establish a circuit split, Petitioners must therefore point to other, *precedential* Ninth Circuit decisions that are at odds with those of other courts of appeals. And they make no such showing.

But even if the panel's decision were precedential, there would be no conflict. The four decisions cited by Petitioners either disclaim the alleged conflict, lack occasion to address the relevant issue, apply a severance doctrine unlike California's, or recognize a doctrine somewhat like California's without finding it preempted. As if that were not enough, all of these courts confront agreements far less defective than Petitioners'. The agreements in these four cases contained zero, one, or two unconscionable provisions; here, Petitioners chose to insert five unconscionable provisions into their agreement.[7] Petitioners cite no evidence that any of these courts would have reached a different result in this case. Where these courts discuss severability at all, the differences Petitioners mislabel as "circuit splits" result not from any discord as to the FAA's requirements, but rather from the

[7] After this action was filed, Petitioners overhauled their arbitration agreement, abandoning the five unconscionable provisions and two other provisions that Respondents had criticized as unfair. *See* App. 22a-24a. If the severance-at-all-costs rule requested by Petitioners were to become law, Petitioners would have incentive to rework those unconscionable and unfair provisions back into their arbitration agreement, safe in the knowledge that the worst possible result of their overreaching would be severance of the offending provisions.

application of other states' laws to distinguishable facts.

A. The Ninth Circuit Does Not Disagree with the Seventh Circuit as to Whether California May Treat Arbitration Differently.

In *Oblix, Inc. v. Winiecki*, which does not discuss severability at all, the Seventh Circuit itself noted that according to the Ninth Circuit, *Armendariz* does not "establish any special hurdles for arbitration agreements." 374 F.3d 488, 492 (7th Cir. 2004). The *Oblix* court further noted that the Ninth Circuit "would enforce without ado an agreement like the one between Oblix and Winiecki," just as the *Oblix* court did. *Id.* (citing *EEOC v. Luce, Forward, Hamilton & Scripps*, 345 F.3d 742 (9th Cir. 2003) (en banc)). This is far from what Petitioners call a circuit split "as to whether California may enforce rules that 'treat[ ] arbitration differently.'" Pet. 18 (alteration in original). If there was a circuit split here, the Seventh Circuit certainly did not notice it.

B. The Ninth Circuit Does Not Disagree with the Sixth, Eighth, or D.C. Circuits as to the Effects of Severability Clauses.

Petitioners do not specify the subject of the second circuit split they allege. They suggest that the Sixth, Eighth, and D.C. Circuits disagree with the Ninth as to whether, under federal law, the presence

of a severability clause in an arbitration agreement requires severance of any invalid or unenforceable provisions in that agreement. *See* Pet. 19. But these circuits set forth no such rule. Moreover, two of them expressly distinguish cases like this one, in which the contract at issue is riddled with unconscionability.

1. The Sixth Circuit in *Morrison* Applied Other States' Severance Doctrines and Gave No Indication That It Would Have Reached a Different Result Here.

Petitioners claim that according to the Sixth Circuit, when an arbitration agreement contains a severability clause, "[the] intent of the parties and [federal] policy in favor of arbitration dictate that the remainder of the agreement be enforced." Pet. 20 (alterations in original) (quoting *Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646 (6th Cir. 2003)) (internal quotation mark omitted). But this "dictate" came from the particular state laws applied in that case, which, unlike California law, made contract severability depend primarily on the intent of the parties. *See Morrison*, 317 F.3d at 675, 677 n.21 (discussing the Ohio and Tennessee severance doctrines that governed the two agreements at issue). The court recognized that "a particular provision of an arbitration agreement" could "taint[ ] the entire agreement." *Id.* at 675. It simply held that under state laws making the parties' intent paramount, courts should not "lightly conclude" that such tainting has occurred in

the presence of a severability clause. *Id.* Faced with two agreements containing only one and two unenforceable provisions, respectively, see *id.* at 674, 677, the *Morrison* court elected to sever. Nothing in its decision suggests that the FAA is incompatible with California's contract doctrine, which also eschews a bright line rule in favor of giving trial courts discretion to reach the right result based on the facts at hand. Thus, *Morrison* did not assert that severability clauses always mandate severance under the FAA. And Petitioners cite no evidence that the Sixth Circuit would have reached a different result than the court of appeals in the present case, where (not just one or two but) five provisions were unconscionable.

2. The Eighth Circuit in *Gannon* Faced Only One Defective Provision and Recognized the Validity of a State Doctrine Like California's.

In *Gannon v. Circuit City Stores, Inc.*, only one provision of the contract was unenforceable under Missouri law. 262 F.3d 677, 679 (8th Cir. 2001). "[R]ecogniz[ing] that in certain situations one party may include so many invalid provisions that the validity of the entire agreement would be undermined," the court found the lone unenforceable provision insufficient to meet that hurdle. *Id.* at 681 (acknowledging that non-severance is appropriate "where there is some 'all-pervading vice, such as fraud, or some unlawful act which is condemned by

public policy or the common law and avoids all parts of the transaction because all are alike infected'"). Thus, the *Gannon* court joins the Ninth Circuit in recognizing that courts can, consistent with the FAA, exercise discretion to refuse to sever when there is too much overreaching by the drafter.[8] Here, too, Petitioners fail to establish a split.

3. The D.C. Circuit in *Booker* Faced Only One Defective Provision and Cast Doubt on the Existence of a Circuit Split Over Severance.

Booker v. Robert Half International, Inc. also involved an arbitration agreement with only one unenforceable provision. 413 F.3d 77, 85 (D.C. Cir. 2005). The *Booker* court discussed concerns about overreaching. Specifically, the court explained that trial courts have discretion under District of Columbia law to sever unenforceable provisions or find an entire arbitration agreement unenforceable, depending on the circumstances: "the more the employer overreaches, the less likely a court will be able to sever the provisions and enforce the clause, a dynamic that

[8] Contrary to Petitioners' assertion, *Gannon* does not say that non-severance in the face of a severability clause "represent[s] the antithesis of the 'liberal federal policy favoring arbitration agreements.'" Pet. 21 (quoting *Gannon*, 262 F.3d at 682). What *Gannon* actually says is that such an antithesis would result "if we were to hold entire arbitration agreements unenforceable *every time a particular term is held invalid*." *Gannon*, 262 F.3d at 682 (emphasis added).

creates incentives against the very overreaching Booker fears." *Id.* at 85. The court's discretion turns, as it does under California and many other states' laws, on the degree to which "illegality pervades the arbitration agreement." *Id.* at 84 (citing *Graham Oil*, 43 F.3d at 1248-49); *id.* at 85 ("We do not . . . question that there may be cases where a forbidden provision is so basic to the whole scheme of a contract and so interwoven with all its terms that it must stand or fall as an entirety." (quoting *NLRB v. Rockaway News Supply Co.*, 345 U.S. 71, 78 (1953))).

The *Booker* court also noted differing severance outcomes in various circuits. But the court cautioned that "[t]he differing results may well reflect not so much a split among the circuits as variety among" the arbitration agreements involved. *Id.* at 84. "Decisions striking an arbitration clause entirely often involved agreements without a severability clause . . . or agreements that did not contain merely one readily severable illegal provision, but were instead pervasively infected with illegality [citing Ninth Circuit precedent]. . . . Decisions severing an illegal provision and compelling arbitration . . . typically considered agreements with a severability clause and discrete unenforceable provisions." *Id.* (citing *Morrison*, 317 F.3d at 675, and *Gannon*, 262 F.3d at 680). The court also noted that unlike the arbitration agreement held unenforceable by the Ninth Circuit in *Graham Oil*, 43 F.3d 1244, Booker's agreement showed no evidence of "an integrated scheme to contravene public policy." *Booker*, 413 F.3d at 85.

In short, *Booker* explicitly recognized that courts can properly refuse to enforce arbitration agreements when they are sufficiently infected by unenforceable provisions. In that particular case, the court simply found that "[t]his one unenforceable provision does not infect the arbitration clause as a whole," finding that particular lone unconscionable provision "more readily severable" than others. *Id.* In other words, the court suggested not that a permeation-like standard was preempted, but only that Booker's agreement was not permeated. Like the other three cases cited by Petitioners, *Booker* is consistent with the Ninth Circuit's decision as to any FAA-mandated effects of severability clauses.

IV. This Case Is a Poor Vehicle for Review.

Now is not an opportune time for this Court to take up the issue presented here, because California law may be in flux on related matters. Over the past three years, the California Supreme Court has granted petitions to review and superseded several unconscionability opinions, deferring further action pending consideration and disposition of related issues in *Sanchez v. Valencia Holding Co., LLC*, 135 Cal. Rptr. 3d 19 (Cal. Ct. App. 2011), *review granted and opinion superseded*, 272 P.3d 976 (Cal. 2012). In *Sanchez*, a California court of appeal refused to enforce an arbitration agreement, finding that four provisions permeated it with unconscionability and that the unconscionability was incurable. *See id.* at 40-41. The California Supreme Court reversed on August 3,

2015 and has yet to dispose of the pending cases. *See Sanchez*, 2015 WL 4605381, at *9-15 (holding that none of the provisions were substantively unconscionable and that the FAA preempts a state anti-waiver law "insofar as [it] bars class waivers in arbitration agreements covered by the FAA").

Many of the cases deferred pending *Sanchez* address the severability of unconscionable provisions in arbitration agreements. *See Trabert v. Consumer Portfolio Servs., Inc.*, 184 Cal. Rptr. 3d 596, 607 (Cal. Ct. App. 2015) (severing two unconscionable provisions), *review granted and opinion superseded*, 349 P.3d 1067 (Cal. 2015); *Vargas v. Sai Monrovia B, Inc.*, 157 Cal. Rptr. 3d 742, 766-67 (Cal. Ct. App. 2013) (declining to sever four provisions), *review granted and opinion superseded*, 304 P.3d 1082 (Cal. 2013); *Natalini v. Imp. Motors, Inc.*, 153 Cal. Rptr. 3d 224, 234 (Cal. Ct. App. 2013) (affirming refusal to sever three provisions), *as modified* (Feb. 5, 2013), *review granted and opinion superseded*, 299 P.3d 700 (Cal. 2013); *Goodridge v. KDF Auto. Grp., Inc.*, 147 Cal. Rptr. 3d 16, 32 (Cal. Ct. App. 2012) (affirming refusal to sever four provisions), *review granted and opinion superseded*, 290 P.3d 1116 (Cal. 2012); *Mayers v. Volt Mgmt. Corp.*, 137 Cal. Rptr. 3d 657, 670 (Cal. Ct. App. 2012) (affirming refusal to sever two provisions), *as modified on denial of reh'g* (Feb. 27, 2012), *review granted and opinion superseded*, 278 P.3d 1167 (Cal. 2012).

The significance of any impact that California's severance doctrine may have on the FAA's objectives

depends, in the first instance, on the scope of the state's unconscionability doctrine. Given the recent development concerning that scope, the number of severability decisions that stand to be reconsidered in light of it, Petitioners' flawed presentation of the issues in this case, and the lack of any circuit split over them, this Court would do better to let *Sanchez*'s effects take shape before deciding whether the issue presented here merits review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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AUGUST 2015

APPENDIX

PROVIDER SERVICES CTO AGREEMENT

This Agreement is made by and between the provider named on the signature page of this Agreement ("Provider") and MHN Government Services, Inc., (hereinafter referred to as "MHN"). The effective date of this Agreement is set forth on its signature page.

Recitals:

WHEREAS, the Provider has the legal authority to enter into this Agreement and to deliver or arrange for the delivery of short term, situational, problem solving non-medical counseling support services; and

WHEREAS, the Provider maintains a duly licensed, private counseling practice, either as an individual or within a group practice or has retired from said practice; and

WHEREAS, the Provider desires to supplement (but not replace) his income from his private or group practice, employment, contracted work, other sources, or retirement by contracting to provide Services under this Agreement; and

WHEREAS, MHN desires to contract with the Provider to provide counseling services that constitute Services under this Agreement.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and promises contained

herein, and intending to be bound hereby, the parties agree as follows:

1. Provider Services.

(a) Services. In the event that Provider accepts a placement under a Consultant Task Order ("CTO") during the term of this Agreement, Provider shall deliver or arrange the short term, situational, problem-solving non-medical counseling services set forth in and subject to any additional terms in the CTO attached hereto or issued in the future and made a part of this Agreement (the "Services").

(b) No Additional Work Obligation. Provider agrees that MHN is not obligated to make new placements or issue any additional CTOs for work by Provider under this Agreement.

(c) Aggregate Placement Time Limit. The aggregate amount of time for all placements under this Agreement shall not exceed 180 days in any continuous 12 month period during the Term of this Agreement.

(d) Professional Liability Insurance. Provider shall maintain professional liability insurance at Provider's own expense in the amount of one million dollars ($1,000,000) per claim and one million dollars ($1,000,000) in the aggregate of all claims per policy year. Provider agrees to provide MHN with written evidence, acceptable to MHN, of such insurance coverage in accordance with MHN's

credentialing and recredentialing requirements and naming MHN, and the U.S. federal government, as additional insureds. Provider also agrees to notify, or to ensure that its insurance carriers notify, MHN at least thirty (30) days prior to any proposed termination, cancellation or material modification of any policy for all or any portion of the coverage required herein. Notwithstanding any insurance coverages of Provider, nothing in Section 1.(d) shall be deemed to limit or nullify Provider's indemnification obligations under this Agreement. Provider agrees to waive any rights of subrogation that Provider may have against MHN, or the U.S. federal government under applicable insurance policies related to the work performed by Provider. Indemnification by Provider shall not be limited or reduced by any insurance coverage limitations. Provider shall make certain that any and all subcontractors or employees of Provider are insured in accordance with this Agreement. If any subcontractor's coverage does not comply with the provisions herein, Provider shall indemnify and hold MHN harmless of and from any damage, loss, cost or expense, including attorneys' fees, incurred by MHN as a result thereof.

(e) **No or Limited Liability of MHN and Other Insurance Coverage.** To the extent required by federal laws applicable to government contracts, such as the Defense Base Act, MHN may maintain certain insurance coverage the benefit of which may extend to

Provider. MHN's liability to Provider or any third party is limited to the extent of such coverage. As such, Provider acknowledges that there may be a need for Provider, at Provider's discretion, to further obtain and maintain other insurance policies as MHN or Provider may reasonably deem necessary, including without limitation medical, disability, worker's compensation, and rescue/evacuation insurance in the event of medical emergency or death. In the event that Provider is a group practice that employs or subcontracts with other providers who provide Services hereunder, Provider shall maintain such policies of general liability and workers compensation as may be required by applicable law or as is reasonable and customary for such groups. In the instance where no insurance coverage is maintained by MHN the benefit of which may extend to Provider, MHN shall have no liability to Provider or any third party including acts of negligence on the part of provider or damage or theft of Provider's personal property. Nothing contained herein shall be interpreted or construed to require that MHN have any such insurance coverage, or if it has it, to continue to retain it or otherwise prevent MHN from modifying or eliminating such coverage in the future. Further, MHN shall have no obligation to provide insurance to Provider, or, if it maintains insurance that does cover Provider, from making any changes or otherwise terminating such coverage as it may pertain to Provider.

(f) **Credentialing.** Provider shall comply with MHN's credentialing and recredentialing requirements.

(g) **Professional Provider.** If Provider is a group practice, Professional Providers are the health care providers who contract with Provider, or are employed by Provider, and who have been credentialed and accepted by MHN to provide the Services described herein. Professional Providers accepted by MHN are limited to the Professional Providers named in the CTOs. Furthermore, Provider has the unqualified authority to and hereby binds itself, and any Professional Providers covered by this Agreement (referred to herein collectively as "Provider"), to the terms and conditions of this Agreement and the CTOs referenced herein.

(h) **Military and Family Life Consultant (MFLC) Provider Guidelines.** The MFLC Provider Guidelines issued by MHN, as updated from time to time, is incorporated into this Agreement by this reference and available on MHN's website or on hardcopy upon request. Provider agrees to be contractually bound to comply with the MFLC Provider Guidelines and any updates or revisions to such, which are effective as of the date of each respective CTO accepted hereunder. In the event that any provision in the MFLC Provider Guidelines or any updates thereto are clearly inconsistent with the terms of this Agreement, the terms of this Agreement, including any amendments, shall prevail.

2. <u>CTOs</u>.

(a) MHN, solely at its discretion, may issue CTOs under this Agreement to the Provider calling for the provision of the Services. The CTO will include the following minimum information:

2.a.1 CTO Number and MHN's Contract/ Subcontract Number.

2.a.2 Description of ordered Services.

2.a.3 Placement location.

2.a.4 Period of performance.

2.a.5 Invoicing and Payment Terms.

2.a.6 Rate of payment for the services, applicable Non-Labor expenses, and Ceiling Price.

2.a.7 Professional Provider(s) approved for placement.

2.a.8 Appendix A specifying the terms and conditions for the placement(s) covered by the CTO.

(b) Prior to the issuance of a CTO, MHN shall advise the Provider of the details of required performance (as depicted in 2.a.2 thru 2.a.4 above. Provider shall detail the name(s) of the Professional Providers(s) that Provider proposes to use to conduct the services. All Professional Providers named by Provider must be credentialed and approved by MHN.

Provider shall not substitute named Professional Providers without the express written authorization of MHN.

(c) MHN will issue the CTO to the Provider and shall name the Professional Provider agreed upon. Upon receipt of the CTO, Provider agrees to notify MHN within two (2) business days via email of the Provider's decision to "decline" the CTO. If MHN does not receive such a written declination within two (2) business days, this shall constitute Provider's acceptance of the CTO and Provider's agreement to performance thereunder.

(d) **Payment.** Subject to Section 3 of this Agreement, during the term of this Agreement, for Services provided in each placement, MHN shall pay to Provider as compensation for the Services provided the Payment specified in the CTO issued hereunder that describes the placement.

3. Invoicing and Payment.

(a) **Services.** MHN shall pay to Provider as full compensation for the Services provided under any resulting CTO, the Rate of Payment stated in such CTO for such services. MHN, however, may pay for partial delivery of services, through a progress payment, based upon Provider's submission of a properly prepared invoice, as stated below. In addition,

(b) **Invoice Submissions.** Provider shall submit invoices for services ("Invoices") in accordance with the terms and conditions set forth in the CTO and MFLC Provider Guidelines. Consistent submission of timely Invoices is a condition of continued participation under this Agreement.

(c) **Timely Filing of Invoices.** Payment under this Agreement and any placement hereunder shall be conditioned upon Provider submitting complete, timely and accurate Invoices, in accordance with the submission requirements hereunder. Provider expressly acknowledges its understanding and agreement, that Invoices must be submitted within thirty (30) calendar days from the date the expense was incurred or the services were provided, in order to be considered timely submitted and payable by MHN. Notwithstanding the foregoing, in the event that MHN denies an invoice submitted after the 30-day deadline on the basis that it was not submitted timely, upon demonstration by Provider of good cause for the delay through the provider dispute resolution process specified in the MFLC Provider Guidelines, MHN will reprocess the invoice as if it were timely.

(d) **Form W-9.** Payment under this Agreement and any placement hereunder shall be conditioned upon Provider submitting a completed and signed "Form W-9," Taxpayer Identification Number Request, as set forth in the MFLC Provider Guidelines.

(e) **Right of Set-off.** In relation to any collection and payment of monies owed by Provider to MHN, MHN shall have the right, after the 45th calendar day following MHN's submission of the reimbursement request to Provider or after Provider's appeal rights have been exhausted, to set-off any payments owed to Provider against any funds owing by Provider to MHN, provided that MHN submits to Provider an explanation in writing in sufficient details so that Provider can reconcile each invoice.

4. **Term and Termination of Agreement.**

(a) **Effective Date.** This Agreement shall become effective as of the date set forth on the signature page and shall remain in full force and effect, unless otherwise terminated as provided herein.

(b) **Termination of Agreement for Default.** Either party may terminate this Agreement upon fourteen (14) calendar days prior written notice to the other party if the party to whom such notice is given is in material breach of this Agreement and/or such CTO. The party claiming the right to terminate hereunder shall set forth in the notice of intended termination the facts underlying its claims that the other party is in material breach of this Agreement and/or such CTO. Remedy of such breach to the satisfaction of the party giving notice of intended termination within fourteen (14) calendar days of receipt of such notice shall revive the

Agreement and/or such CTO. Services to be performed during the cure period shall be as required in a written amendment to this Agreement or the applicable CTO.

(c) **Immediate Termination of Agreement or CTO.** This Agreement and/or a CTO shall immediately terminate upon notice to the effected party in the event of the occurrence of any of the following:

4.c.1 Either party's violation of law or regulation pertinent to this Agreement and/or such CTO, upon notice of said violation;

4.c.2 any act, conduct or circumstance which creates any cause for the revocation or termination suspension or other impairment of Provider's license, certifications or accreditation, to provide Services or causes Provider's ability to provide Services in accordance with this Agreement and/or such CTO to be materially impaired;

4.c.3 any misrepresentation or fraud by either party;

4.c.4 Provider's failure to adhere to MHN's credentialing requirements as determined by the MHN Credentialing Committee or failure to maintain professional liability insurance in accordance with this Agreement;

4.c.5 MHN's determination that the health, safety or welfare of any participant

may be in jeopardy if this Agreement and/or such CTO is not terminated;

4.c.6 MHN's determination in its sole discretion that Provider is not able to perform according to the standards of MHN and the Department of Defense; or

4.c.7 Provider is involuntarily terminated from the MHN commercial network; or

4.c.8 The Department of Defense's termination or failure to renew/extend the MHN contract and/or placement under a CTO, or the Department of Defense's request that Provider's placement under a CTO be terminated.

4.c.9 Any act or conduct by the Provider which results in any violation of applicable U.S., or state law or regulations, or the law of any country where the Provider is providing services, including, but not limited to the U.S. Foreign Corrupt Practices Act, Export Administration Act, Foreign Asset Control Act and regulations, Arms Export Control Act and regulations, or any breach of any covenant condition or representation and warranty contained herein.

(d) **Limited Termination Remedy.** In the event that MHN terminates pursuant to Sections 4.c.6 or 4.c.8 any CTO 30 days or greater in length with less than five days prior to

the Placement Start Date, MHN agrees to pay Provider the equivalent of one week's pay based on the Payment Rate and estimated number of hours per week specified in the applicable CTO. In the event that MHN terminates a CTO pursuant to Sections 4.c.6 or 4.c.8 following the start date, then MHN shall pay the provider for the remaining balance of the term of the placement or for one week, whichever is less, under the CTO at the rates specified in the CTO. Provider agrees that it shall have no additional remedy or damages applicable to such termination.

5. Confidential and Proprietary Information.

(a) Department of Defense Premises. Provider is hereby expressly prohibited from entering area(s) other than the work area(s) designated by the Government or the Provider's military service point of contact, as applicable. Any failure to adhere to this requirement shall constitute a material breach of this Agreement by the Provider.

(b) Confidentiality Provisions. The parties hereby agree to hold all confidential or proprietary information or trade secrets of each other in trust and confidence and agree that such information shall be used only for the purposes contemplated herein, and shall not be used for any other purpose. Moreover, it is understood that Provider and MHN shall release patient-related behavioral health information and records that contain individual

identifying information and Provider-specific information only in accordance with applicable state and federal laws. Provider also shall keep strictly confidential all compensation arrangements set forth in this Agreement and its addenda. Provider further acknowledges that medical and financial information of individuals counseled by or eligible for counseling by Provider under this Agreement, shall be deemed confidential, and shall not be disclosed or removed from Department of Defense facilities without the express prior written consent of MHN or as required by applicable Federal laws or regulations. Provider agrees to safeguard Beneficiary privacy and confidentiality as required by applicable law, including, but not limited to the United States Department of Health and Human Services Standards for Privacy of Individually Identifiable Health Information promulgated pursuant to the administrative simplification provisions of the federal Health Insurance Portability and Accountability Act of 1996 ("HIPAA"), as set forth in 45 C.F.R. Subtitle A, Subchapter 3, Parts 160 and 164.

(c) **No Customer Contact.** Provider, as an independent contractor, acknowledges that it is not authorized to represent MHN or to communicate with the Department of Defense on behalf of MHN. Accordingly, Provider agrees that under no circumstances shall Provider contact the Department of Defense, without the express prior written consent of MHN.

(d) Provider understands that any information obtained by Provider from a victim of domestic abuse is protected by the Privacy Act of 1974 and any unauthorized disclosures of client information may result in the imposition of possible criminal penalties.

(e) Provider shall maintain, transmit, retain in strictest confidence, and prevent the unauthorized duplication, use, and disclosure of client and beneficiary information.

(f) Provider shall follow appropriate administrative and physical safeguards to ensure the security and confidentiality of client records and to protect against any anticipated threats or hazards to their security or integrity that could result in substantial harm, embarrassment, inconvenience, or unfairness to the client.

(g) Provider agrees to protect the confidentiality of Government records, client or otherwise, which are not public information.

(h) Information made available to Provider by MHN for the performance or administration of this effort shall be used only for those purposes and shall not be used in any other way without the written agreement of MHN.

(i) If public information is provided to Provider for use in performance or administration of this effort, except with the written permission of MHN, Provider may not use such information for any other purpose. If Provider is uncertain about the availability or proposed

use of information provided for the performance or administration, Provider shall consult with MHN regarding use of that information for other purposes.

(j) Provider agrees to protect the confidentiality of Government records that are not public information.

(k) Performance of this effort may require Provider to access and use data and information proprietary to a Government agency or Government contractor which is of such a nature that its dissemination or use, other than in performance of this effort, would be adverse to the interests of the Government and/or others.

(l) Provider shall not divulge or release data or information developed or obtained in performance of this effort, until made public by the Government, except to authorized Government personnel or upon written approval of MHN. Provider shall not use, disclose, or reproduce proprietary data that bears a restrictive legend, other than as required in the performance of this effort. Nothing herein shall preclude the use of any data independently acquired by Provider without such limitations or prohibit an agreement at not [sic] cost to the Government between Provider and the data owner that provides for greater rights to Provider.

(m) All data received, processed, evaluated, loaded, and/or created as a result of this Agreement or resulting CTOs, shall remain the

sole property of MHN or the Government unless specific exception is granted by MHN, or the Contracting Officer directly through MHN.

(n) This Section 5 shall survive the termination of this Agreement for any reason.

(o) Failure to comply with the requirements of this Section 5 shall constitute a material breach of this Agreement.

6. <u>Warranties</u>.

(a) Provider represents and warrants that it has the full right and authority to execute and deliver this Agreement and to perform its obligations under this Agreement, and that neither the execution nor delivery of this Agreement by Provider nor consummation of the transactions contemplated hereby will result in a breach or default under the terms and conditions of any contract, CTO, license, charter document or other agreement by which Provider is bound.

(b) Provider represents and warrants that the Services provided under this Agreement or any CTO will be performed in a professional and workman-like manner by qualified personnel, and that Provider is appropriately credentialed to provide the Services.

(c) Provider represents and warrants that to the best of Provider's knowledge, there exists no actual or potential conflict between Provider's family, business, or financial interest and performance of the Services under this

Agreement, and in the event of change in either Provider's private interest or Services under this Agreement, Provider will raise with MHN any question regarding possible conflicts of interest which may arise as a result of such change. Treatment of TRICARE beneficiaries in the Provider's private practice does not constitute a conflict of interest.

(d) Provider represents and warrants that each person providing Services under this Agreement is physically fit and in good physical condition and has been screened to identify any medical conditions that might limit his or her ability to perform Services in the location(s) where Services must be performed. It is the responsibility of Provider's medical examiner to use sound medical judgment to determine fitness of each person to provide Services.

If any medical condition is identified that may limit his or her ability to perform Services, but which condition is not considered disqualifying by Provider's physician, the Provider shall obtain from the examining physician, in writing, a statement of the reasons why the finding is not likely to limit performance or cause undue risk to the Provider or others in the performance of Services.

(e) Provider represents and warrants that each Provider and Provider's physician has reviewed the required and recommended vaccinations, which requirements and recommendations

are issued by the United States Department of State, the Centers for Disease Control and Prevention, and/or other similar agency/ resource for each location where Services are to be performed, and that each Provider has received such required and recommended vaccinations in a timely manner prior to being deployed to or performing any Services in such location.

(f) Provider represents and warrants that each person providing Services under this Agreement has not and will not violate the any law or regulation of the United States or any state, including, but not limited to the Foreign Corrupt Practices Act, Export Administration Act, Foreign Asset Control Act and regulations, Arms Export Control Act and regulations or any law of any country where the Provider is providing Services.

(g) Provider represents and warrants that each person providing Services under this Agreement has reviewed the travel warnings and security advice as issued by the United States Department of State or other similar agencies and understands the reported risks of each location where Services will be performed.

(h) Provider represents and warrants that the information contained in Appendix XXX (Small Business Certification) is true and correct as of the date of this Agreement and that Provider shall, at least annually during

the term hereof, advise MHN of any changes to the facts set forth therein.

7. **Indemnification by Provider.** Provider shall indemnify MHN, its directors, officers, agents, and employees from and against any and all liabilities, suits, claims, losses, damages, costs, attorneys' fees, and expenses whatsoever arising from any breach of a representation or warranty hereunder or any act or omission of Provider, its agents, or employees during the performance of any of its obligations under this Agreement. Upon request of and at no expense to MHN, Provider shall defend any suit asserting a claim for any loss, damage or liability specified above, and Provider shall pay any such costs incurred in enforcing the indemnity granted above; provided that Provider shall not enter into a settlement of any such suit or claim without the prior written consent of MHN. Provider and its employees shall comply with all applicable laws, ordinance(s), codes and regulations; and Provider hereby indemnifies and agrees to hold MHN harmless from and against all liabilities and penalties imposed or failure to do so.

8. **Relationship of Parties.** MHN and Provider are independent contractors in relation to one another and no joint venture, partnership, employment, agency or other relationship is created by this Agreement. Neither MHN nor Provider is authorized to represent the other for any purposes. Neither of the parties hereto, nor any of their respective officers, agents or employees shall be construed to be the officer, agent or employee of the other party.

9. **Headings.** The section and paragraph headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement.

10. **Assignment.** Provider shall not assign, sell or transfer this Agreement or any interest therein without the prior written consent of MHN, and any unauthorized assignment or transfer of this Agreement or any interest therein shall be null and void. MHN reserves the right to assign this Agreement or any CTO to any present or future affiliate, subsidiary or parent corporation. MHN Government Services is an affiliate of Managed Health Network, Inc, and MHN at its sole discretion may assign this Agreement to Managed Health Network, Inc. Subject to the provisions of this Section 10, this Agreement shall inure to the benefit of and be binding upon the respective successors and assigns, of any of the parties hereto. Provider shall not assign this Agreement without the prior written authorization of MHN; such authorization shall not be unreasonably withheld.

11. **Waiver.** Waiver of a breach of any provision of this Agreement shall not be deemed a waiver of any other breach of the same or different provision.

12. **Severability.** In the event that any provision of this Agreement is rendered invalid or unenforceable by any valid law or regulation of the State of California or of the United States, or declared void by any tribunal of competent jurisdiction,

the remaining provisions of this Agreement shall remain in full force and effect.

13. **Modification.** This Agreement or any part or section of it can be amended only by mutual written consent of the parties.

14. **Notices.** Any notice required or desired to be given under this Agreement shall be in writing. Notices shall be deemed given five (5) days post deposit in the U.S. mail, postage prepaid. If sent by hand delivery, overnight courier, or facsimile, notices shall be deemed given upon documentation of receipt. All notices to the Provider shall be addressed to the applicable address appearing on the signature page of the Agreement. The addresses to which notices are to be sent may be changed by written notice given in accordance with this Section. All notices to MHN shall be as follows: _____

    MHN Services
    Professional Relations Department
    P.O. Box 10086
    San Rafael, CA 94912
    Fax: (866) 689-0605
    Attn: Vice President Professional Relations

15. **No Third Party Beneficiary.** Nothing in this Agreement, express or implied, is intended or shall be construed to confer upon any person, firm, or corporation other than the parties hereto and their respective successors or assigns, any remedy or claim under or by reason of this Agreement or any term, covenant, or condition hereof, as third party beneficiaries or otherwise, and all of the terms, covenants, and conditions

hereof shall be for the sole and exclusive benefit of the parties hereto and their successors and assigns.

16. **Compliance with Applicable Laws.** Provider and its employees shall comply with all applicable laws, regulations, ordinances and codes, including the procurement of permits and licenses when required, in the performance of this Agreement. Provider shall hold harmless and indemnify MHN against any loss, damage, penalties or liabilities that may occur by reason of Provider's failure to comply with such laws, regulations and codes.

17. **Survival.** The provisions contained in this Agreement that by their nature and context are intended to survive the completion and performance, cancellation or termination of this Agreement or any CTO hereunder, shall so survive.

18. **Governing Law.** This Agreement shall be governed by and construed according to the laws of the State of the Provider's residence, as last set forth in the Provider's credentialing application on file with MHN.

19. **Mandatory Arbitration. YOU SHOULD READ THE PROVISIONS OF THIS MANDATORY ARBITRATION CLAUSE CAREFULLY.** Arbitration replaces the right to go to court, including the right to a jury and the right to participate in a class action or similar proceeding, except as expressly discussed below. The parties agree that any existing or future controversy or claim between them whether the controversy

involves a claim in tort, contract or otherwise (collectively, "Covered Claims"), shall be settled by final and binding arbitration in accordance with the provisions of the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 1 et seq. This includes any dispute relating to the enforceability of this Agreement including, but not limited to any claim that all or part of this Agreement is void or voidable. This Mandatory Arbitration clause is the full and complete agreement relating to the formal resolution of disputes involving Covered Claims. The parties waive their right to a jury or court trial. The parties agree not to arbitrate any dispute between them on a class, collective or representative basis. In other words, all disputes will be resolved on an individual basis. The Arbitrator will not have the authority to hear claims on a collective, representative or class basis. The complaining party must serve a written demand for arbitration upon the other party to initiate these arbitration proceedings. The written demand shall contain a detailed statement of the matter and facts supporting the demand and include copies of all related documents. Arbitrations will be administered by the American Arbitration Association ("AAA") under the AAA's Commercial Arbitration Rules and Mediation Procedures, which are available for your review online at the AAA's website, www.adr.org. These rules are subject to modifications from time to time and the parties are responsible for reviewing the rules periodically. A single, neutral arbitrator who is licensed to practice law will be selected in a manner consistent with AAA's Rules. Upon notice of a demand, the parties will

agree upon an arbitrator or, if unable to agree, will follow the arbitrator selection process provided for by the AAA. Location of the arbitration proceeding shall be determined in a manner consistent with AAA's rules. The Arbitrator may, in his or her discretion, permit the parties to use discovery procedures that the arbitrator deems appropriate. Each party bears the responsibility of their attorney's fees, unless otherwise provided for by an award of the Arbitrator. However, the Arbitrator shall not have authority to award attorneys' fees or costs unless a statute expressly authorizes the award of attorneys' fees and costs. Any party presenting a witness will be responsible for paying that witness's fees and expenses. The cost of any evidence or proof produced at the Arbitrator's direction will generally be borne by the party producing that evidence or proof. Judgment upon the award rendered by the arbitrator may be entered in any court having competent jurisdiction. The decision of the arbitrator shall be final and binding. The arbitrator shall make findings of fact and conclusions of law and shall have no authority to make any award that could not have been made by a court of law. In the event any portion of this Mandatory Arbitration clause is deemed invalid, void or unenforceable, the remainder of this Mandatory Arbitration clause will be valid and enforceable.

20. **Entire Agreement.** This Agreement, inclusive of any CTOs that may be issued hereunder, constitutes the entire Agreement of the parties with respect to the subject matter hereof. No promises, terms, conditions, or obligations other than those contained herein shall be valid or binding. Any

prior agreements, statements, promises, either oral or written, made by any party or agent of any party that are not contained in this Agreement are of no force or effect.

21. **No Press or Public Contact.** Provider will not speak with the press or make any other public statement, press release or other announcement relating to the terms of or existence of this Agreement without the prior written approval of MHN, which approval may be withheld in MHN' sole discretion.

22. **Federal Acquisition Regulations (FAR).** Task Orders resulting from this Agreement shall constitute subcontracts issued under a U.S. federal government contract. All issued Task Orders are subject to the following requirements, as applicable, which are hereby incorporated by reference with the same force and effect as if set forth herein in full text. The full text of these clauses is available at: http://farsite.hill.af.mil/vffara.htm. "Subcontract" as used below denotes "Task Order".

(a) 52.219-8, Utilization of Small Business Concerns (Dec 2010) (15 U.S.C. 637(d)(2) and (3)) [Applicable if the subcontract exceeds $150,000].

(b) 52.222-26, Equal Opportunity (Mar 2007) (E.O. 11246). [Applicable if the value a single subcontract, or the combination of all Federally funded subcontracts in last 12 months, total $10,000 or more].

(c) 52.222-35, Equal Opportunity for Veterans (Sep 2010) (38 U.S.C. 4212(a)) [Applicable if Expected Subcontract Value is $25,000 or more].

(d) 52.222-36, Affirmative Action for Workers with Disabilities (Oct 2010) (29 U.S.C. 793) [Applies if subcontract is expected to exceed $15,000]

(e) 52.222-40, Notification of Employee Rights Under the National Labor Relations Act (Dec 2010) (E.O. 13496), if flow down is required in accordance with paragraph (f) of FAR clause 52.222-40. [Applicable if the subcontract exceeds $10,000 and is performed wholly or partially in the United States].

(f) 52.222-50, Combating Trafficking in Persons (Feb 2009) (22 U.S.C. 7104(g)).

(g) 52.247-64, Preference for Privately Owned U.S.-Flag Commercial Vessels (Feb 2006) (46 U.S.C. App. 1241 and 10 U.S.C. 2631), if flow down is required in accordance with paragraph (d) of FAR clause 52.247-64.

(h) 52.203-13, Contractor Code of Business Ethics and Conduct (Apr 2010) (Pub. L. 110-252, Title VI, Chapter 1 (41 U.S.C. 251 note)), if the subcontract exceeds $5,000,000 and has a performance period of more than 120 days. In altering this clause to identify the appropriate parties, all disclosures of violation of the civil False Claims Act or of Federal criminal law shall be directed to the agency

Office of the Inspector General, with a copy to the Contracting Officer.

(i) 52.203-15, Whistleblower Protections Under the American Recovery and Reinvestment Act of 2009 (Jun 2010) (Section 1553 of Pub. L. 111-5), if the subcontract is funded under the Recovery Act.

(Signatures following on next page)

In witness whereof, the parties have caused this Agreement to be executed by their respective duly authorized representatives as of the effective date below.

EFFECTIVE DATE. This agreement is effective on _____

[To be entered by MHN Government Services, Inc.]

This agreement is not effective until the effective date entered by MHN Government Services, Inc. above.

IN WITNESS WHEREOF, the parties hereto have entered into this agreement on the effective date specified.

PROVIDER NAME:	**MHN GOVERNMENT SERVICES, INC.**
_____ (Legal name/business name that matches Tax ID# or SSN below)	
_____ Address	P.O. Box 10086
_____	San Rafael, CA 94912
TEL: ( ) _____	
FAX: ( ) _____	FAX: (866) 689-0605
By: _____ (Authorized Signature)	By: /s/ John L. Roberts (Authorized Signature)
Name: _____ (Print Name)	Name: John L. Roberts
Title: _____	Title: Manager Health Net Government & Specialty Services
Date: _____	Date: _____

Federal Tax ID# or SSN: _____
(This is the number to which MHN will pay for services)