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Hon. Tani Cantil-Sakauye, Chief Justice
and the Honorable Associate Justices
Supreme Court of California
350 McAllister Street
San Francisco, CA 94102-4797

Re: ***Sonic-Calabasas A, Inc. v. Frank B. Moreno***
Case No. S174475
Supplemental Letter Brief

Honorable Chief Justice and Associate Justices:

This letter brief is filed by Frank B. Moreno ("Moreno") pursuant to the Court's order of June 21, 2013, requesting briefing from Moreno and his former employer, Sonic-Calabasas A, Inc. ("Sonic") on the significance, if any, of the United States Supreme Court's recent decision in *American Express Co. v. Italian Colors Restaurant* (June 20, 2013) ___ U.S. ___ , 133 S.Ct. 2304 ("*American Express"*). For all of the reasons set forth below, we urge this Court to hold that *American Express,* if anything, strengthens our argument that the Federal Arbitration Act (the "FAA") does not compel the enforcement of an agreement to arbitrate an employee's wage claims until the employee has first had the opportunity to avail him or herself of the statutory protections afforded under Labor Code sections 98, *et seq.* (the "Berman hearing" process).

The question presented in *American Express* was "[w]hether the Federal Arbitration Act permits courts ... to invalidate arbitration agreements on the ground that they do not permit class arbitration of a federal law claim." (*American Express, supra,* 133 S.Ct. at 2308. The mere recitation of this question highlights some of the central differences between *American Express* and *Sonic.* The issue in this case is not whether an arbitration agreement should be invalidated, but whether its enforcement may be deferred to allow a wage claimant to first bring his claim to the California Labor Commissioner for a preliminary, non-binding determination which, if in the wage claimant's favor, would entitle him to various statutory rights that are otherwise unavailable. Here there is no challenge to traditional bilateral arbitration and no attempt to replace that sort of arbitration with class proceedings.

Notably, *American Express* did not consider the issue of unconscionability. There was no discussion at all about unconscionability, which is expressly recognized as a defense to the enforcement of an arbitration agreement under Section 2 of the FAA. Instead, as Justice Thomas explained in his concurrence, "Italian Colors makes two arguments to support its conclusion that

the arbitration agreement should not be enforced. First, it contends that enforcing the arbitration agreement 'would contravene the policies of the antitrust laws.' Second, it contends that a court may 'invalidate agreements that prevent the 'effective vindication' of a federal statutory right.... **Because Italian Colors has not furnished 'grounds ... for the revocation of any contract,' 29 U.S.C. § 2, the arbitration agreement must be enforced.**" (*Amercan Express, supra,* 133 S.Ct. at 2312-2313. Emphasis added.)

That unconscionabilty remains a valid defense to the enforcement of an arbitration agreement pursuant to Section 2 of the FAA post-*AT&T Mobility LLC v. Concepcion* (2011) 563 U.S. ___, 131 S.Ct. 1740, was made clear by the Supreme Court in twice in the past two years. First, in the *AT&T Mobility* decision, where the Court observed that the Section 2 "saving clause permits agreements to arbitrate to be invalidated by generally applicable contract defenses, such as fraud, duress or unconscionability" that are not arbitration-specific. (*Id.,* at 1746.) Again, in that decision, the Court repeated: "Section 2 makes arbitration agreements 'valid, irrevocable, and enforceable' as written (**subject, of course, to the saving clause.)** (*Id.,* at 1748, emphasis added.) One year later, in *Marmet Health Care Center v. Brown* (2012) 132 S.Ct. 1201, when the Supreme Court remanded based on potential unconscionability, for a determination of whether the arbitration clauses at issue "are unenforceable under state common law principles that are not specific to arbitration and pre-empted by the FAA." (*Id.,* at 1204.) And there is absolutely nothing - not even a single sentence - in *American Express* that says anything different about Section 2 unconscionability defenses.

American Express did address the "effective vindication" principle, a judge-made exception to the enforcement of arbitration agreements, in analyzing whether that principle operates to invalidate the class action waiver set out in the arbitration agreements between merchants and a credit card company, where, according to the merchants, class proceedings are the only way to affordably pursue their anti-trust claims. The Court majority held that the effective vindication principle operates in a more limited fashion: "[T]he exception comes for a desire to prevent 'prospective waiver of a party's right to pursue statutory remedies,' ... but the fact that it is not worth the expense involved in *proving* a statutory remedy does not constitute elimination of the *right to pursue* that remedy." (*American Expresss,* 133 S.Ct., at 2310-2311.) However, the effective vindication principle "would certainly cover a provision in an arbitration agreement forbidding the assertion of certain statutory rights." (*Id.,* at 2310.)

Thus, under *American Express,* a class action waiver contained in an arbitration agreement will be enforced *only if the bilateral arbitration proceeding established under that agreement affords the litigant the right to pursue the very same statutory remedies* as those that could be pursued in a class proceeding. The Court reasoned: "The class action waiver merely limits arbitration to the two contracting parties. It no more eliminates those parties' right to pursue their statutory remedy than federal law before its adoption of the class action for legal relief in 1938." (*Id.,* at 2111.) If, however, the arbitration agreement actually "eliminates [the] right to pursue [a] statutory remedy," the effective vindication principle will operate to preclude enforcement of the agreement.

Here, the arbitration agreement between Sonic and Moreno provides that "any claim, dispute, and/or controversy ... which would otherwise require or allow resort to any court or other governmental dispute resolution forum arising from, related to, or having any relationship or connection whatsoever with my ... employment by, or other association with the Company, whether based on tort, contract, statutory or equitable law, or otherwise ... shall be submitted to and determined exclusively by binding arbitration under the Federal Arbitration Act...." (CT 009.) On its face, this language does not explicitly deny Moreno the right to any statutory remedies. But this language masks what amounts to an absolute *per se* elimination of Moreno's right to pursue statutory remedies that are only available through the Labor Commissioner's Berman wage claim process.

These statutory remedies include the following rights:

- The wage claimant's right to one way attorneys' fee shifting under Labor Code 98.2(c), so that the wage claimant faces no liability for the employer's attorneys' fees regardless of the outcome of the employer-filed *de novo* arbitral proceeding, and so that the wage claimant will be entitled to recoup his or her attorneys' fees if the employer is not successful in its *de novo* appeal of a Labor Commissioner decision;

- The right to have a Labor Commissioner attorney appointed to represent the wage claimant, at no cost to the claimant, in the prosecution of her wage claim, pursuant to Labor Code § 98.4;

- The right to have the employer post a bond equal to the amount determined by the Labor Commissioner owing to wage claimant, pursuant to Labor Code § 98.2(b);

- The right to have the Labor Commissioner enforce any judgment in favor of a wage claimant, pursuant to Labor Code § 98.2(i); and

- The right to have a translator, provided by the Labor Commissioner at no cost to the wage claimant, at all hearings as needed, pursuant to Labor Code § 105.

By denying Moreno the right to have his wage claim initially heard by the Labor Commissioner, Sonic's arbitration agreement operates as an outright prohibition of the above-listed statutory rights, because under California law, all of these statutory rights are conditioned on the Labor Commissioner's involvement in the Berman process. Sonic's arbitration agreement completely and methodically deprives Moreno of each of these statutory rights, in a manner that is no different than an agreement that expressly recites that under the agreement, the employee waives the right to one-way attorney fee shifting, and waives the right to no-cost representation by a Labor Commissioner attorney, etc., etc.

In its original decision in this matter, this Court noted that "the statutory protections pursuant to sections 98.2 and 98.4 are contingent on the Labor Commissioner's findings in a

Berman hearing that the employee's claim is meritorious." (*Sonic-Calabasas A, Inc. v. Moreno* (2011) 51 Cal.4th 659, 682.) It would be contrary to statute beyond the authority of a court to order the Labor Commissioner, or an arbitrator, to provide these statutory protections to a wage claimant when there has been no prior favorable determination in a Berman hearing. (*Id.*) Consequently, an arbitration agreement that deprives an employee of access to the Berman process utterly deprives that employee of "the right to pursue [these] statutory remed[ies]," to use the exact words of the U.S. Supreme Court in *American Express.*

Under Sonic's arbitration agreement, there is an absolute *per se* deprivation of statutory remedies. This, according to the U.S. Supreme Court, triggers application of the effective vindication exception. This sort of arbitration agreement, according to the U.S. Supreme Court, differs in a fundamental way from an arbitration agreement which provides for a waiver of class proceedings without any restriction on otherwise available statutory remedies. When, as in *AT&T Mobility* and *American Express,* an arbitration agreement prohibits class proceedings, without limiting available statutory remedies, the FAA mandates enforcement of the arbitration agreement without regard to the possibility that the low value of the individual's claim relative to the cost of prosecuting the claim at a bilateral proceeding might dissuade the individual from proceeding with the claim. In the context of an arbitration agreement that does not deprive the weaker party of statutory remedies, "the FAA's command to enforce arbitration agreements trumps any interest in ensuring the prosecution of low-value claims." (*American Express,* 133 S.Ct., at 2312, fn. 5.)

In contrast, the FAA does not command, and has never been construed to command the enforcement of an arbitration agreement that deprives a person of substantive statutory rights. "By agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral ... forum." (*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc.* (1985) 473 U.S. 614, 628.) Indeed, in ruling that the FAA compelled enforcement of an agreement to arbitrate disputes between a television performer and his "personal manager," notwithstanding a California law (the Talent Agencies Act or "TAA") that vested the Labor Commissioner with initial jurisdiction to hear the dispute, the U.S. Supreme Court specifically noted that the case "presents only a question concerning the forum in which the parties' dispute will be heard," in that under the arbitration agreement, the performer "relinquishes no substantive rights the TAA (or other California law) may accord him," and thus, "he cannot escape resolution of those rights in the arbitral forum." (*Preston v. Ferrer* (2008) 552 U.S. 346, 359.) The Court majority in that case would undoubtedly have reached a different decision as to the enforceability of the arbitration agreement before it had that agreement operated to deprive the performer of substantive rights under the TAA or other California law.[1]

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[1] In his dissent, Justice Thomas restated his long-held opinion that the FAA "does not apply to proceedings in state courts.... Thus, in state-court proceedings, the FAA cannot displace a state law that delays arbitration until administrative proceedings are completed." (*Preston v. Ferrer, supra,* 552 U.S. at 363.) The other justices, as made clear in the majority opinion, would apply the FAA to state court proceedings on a petition to compel arbitration, and would compel arbitration unless the agreement deprived a party of otherwise available statutory remedies. It

Armendariz v. Foundation Health Psychcare Services, Inc. (2000) 24 Cal.4th 83 followed a similar analysis as to the enforceability of provisions in an arbitration agreement that deprive an employee of substantive statutory remedies, with the holding that provisions in an arbitration agreement that limit statutory remedies such as attorneys' fees are substantively unconscionable and thus, when contained in a mandatory employment agreement, are unenforceable.

And this is precisely the analysis that this Court followed in its original decision in *Sonic*. "[T]he question is whether the employee's statutory right to seek a Berman hearing, with all the possible protections that flow from it, is itself an unwaivable right that an employee cannot be compelled to relinquish as a condition of employment. We conclude that it is." (*Sonic-Calabasas A Inc. v. Moreno, supra,* 51 Cal.4th at 678.) This Court concluded that the statutory remedies that are embedded in the Berman process cannot be stripped away by any mandatory employment agreement, whether that agreement provides for arbitration or not. (*Id.,* at 688-689.)[2] The fact that an employee may him or herself choose to forego the Berman process "does not alter the nonwaivability of the Berman hearing protections, for it is precisely that *option* which an employer may not foreclose in a predispute agreement.... As we recognized in *Armendariz*, our concern is with the impermissible waiver of certain rights and protections as a condition of employment before a dispute has arisen." (*Id.,* at 682.)

Here, Sonic conceded in its petition to compel arbitration that the arbitration agreement was a contract of adhesion, as it was imposed as a condition of employment: "All employees of Sonic-Calabasas A, Inc., are subject to the company's arbitration program by accepting or continuing employment with the company." (CT 007.) "The procedural element of an unconscionable contract generally takes the form of a contract of adhesion, 'which, imposed and drafted by the party of superior bargaining strength, relegates the subscribing party only the opportunity to adhere to the contract or reject it." (*Armendariz, supra,* at 113.) "[I]n the case of preemployment arbitration contracts, the economic pressure exerted by employers on all but the most sought-after employees may be particularly acute, for the arbitration agreement stands between the employee and necessary employment, and few employees are in a position to refuse a job because of an arbitration requirement." (*Id.,* at 115.) For these reasons, this Court, in its original decision in this matter, held that the arbitration agreement between Sonic and Moreno was procedurally unconscionable. (*Sonic-Calabasas A, Inc. v. Moreno, supra,* 5 Cal.4th at 685-

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remains an open question, however, as to whether a majority of the Court would apply *AT&T Mobility* or *American Express* to state court proceedings, as Justice Thomas was a necessary vote in the majority opinions for both of those cases, neither of which involved state court proceedings.

[2] The Court explained that the prohibition of the enforcement of a "Berman waiver" in a predispute mandatory employment agreement "does not discriminate against arbitration agreements. We neither construe the arbitration agreement 'in a manner different from that in which [we would] construe nonarbitration agreements' nor do we 'rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable.'" (*Id.,* at 688-689.)

686.) There is nothing whatsoever in *AT&T Mobility* or *American Express* that would support changing this conclusion.

As to substantive unconscionability, in its original decision this Court noted that an employee subject to Sonic's arbitration agreement would be deprived of a host of statutory remedies that are made available under the Berman process, including the following: "He or she must pay for his or her own attorney whether or not able to afford it – an attorney who may not have the expertise of the Labor Commissioner.... Nor is their any guarantee that the employee will not be responsible for any successful employer's attorney's fees, for under section 218.5, an employee who proceeds directly against an employer with a wage claim not preceded by a Berman hearing will be liable for such fees...." (*Id.,* at 681.) In analyzing the impact of the deprivation of the various statutory remedies that are available only through the Berman process, this Court held that Sonic's arbitration agreement "is markedly one-sided," and "is oppressive," and is "therefore substantively unconscionable." (*Id.,* at 686-687.) Once again, there is nothing in *AT&T Mobility* or *American Express* that would support changing this conclusion.

So, what we have before us is an arbitration agreement that has already been found by this Court to be unconscionable, both procedurally and substantively, and hence, unenforceable under California law until the employee covered by the agreement is availed of the opportunity to have his wage claim heard and decided by the Labor Commissioner, so that the employee may have access to the various statutory remedies that are only available through the Berman process. Neither *American Express* nor *AT&T Mobility* casts the slightest doubt on this state-law ruling. Unconscionability remains as a Section 2 defense to the enforcement of an arbitration agreement under both of these cases. The principle that an arbitration agreement will not be enforced if it deprives a party of statutory remedies survives both *American Express* and *AT&T Mobility.* Neither of these cases construe the FAA to preempt a state-law rule that denies enforcement of a mandatory arbitration agreement, imposed as a condition of employment, that deprives the employee of statutory remedies that would otherwise be available under state law, particularly when that state-law rule applies to all employment agreements, not just those that provide for the arbitration of disputes. And, of course, neither of these recent U.S. Supreme Court cases overrules *Armendariz,* or for that matter, even suggests that *Armendariz* is no longer good law.

Numerous cases decided since *AT&T Mobility* have held that unconscionability remains a defense to the enforcement of arbitration agreements, and that *Armendariz* continues to prohibit the enforcement of arbitration agreements that deprive employees of statutory remedies or protections regarding attorneys' fees. (See, e.g., *Samaniego v. Empire Today LLC* (2012) 205 Cal.App.4th 1138 [agreement to arbitrate employment disputes unconscionable and unenforceable under *Armendariz* where it subjected claimants to liability for employer's attorneys' fees in contravention of statutory protections], *Ajamian v. CantorCO2e, L.P.* (2012) 203 Cal.App.4th 771, 804 fn. 18 [same].) Nothing in *Amercan Express* changes this analysis. Quite the opposite: now we know that "elimination of the *right to pursue* [a statutory] remedy" is a basis, in the view of the U.S. Supreme Court majority, for denial of enforcement of an arbitration agreement. (*American Express, supra,* 133 S.Ct., at 2310-2311.) And this is *precisely* the fatal flaw in Sonic's arbitration agreement – it purports to prevent Moreno from pursuing statutory remedies and protections that are only available under the Berman process.

For that reason, this Court correctly held, in its original decision in this matter, that the FAA does not mandate enforcement of Sonic's arbitration agreement unless and until Moreno has had his wage claim heard and decided by the Labor Commissioner.

We therefore ask that this Court reaffirm its prior decision in this matter, and hold that neither *AT&T Mobility* nor *American Express* warrants any change in the conclusions set out in that prior decision.

Respectfully submitted,

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