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The Tale of How One Corporate Giant Prompted the Courts to Invalidate Its Arbitration Provisions

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Be careful what you wish for, for you will surely get it. Who among us hasn't heard that quaint little bromide a little too often? Under normal circumstances, I would avoid it for that reason alone. But two plaintiff-friendly arbitration decisions in the same week – coming out of the same Court of Appeal – is nothing normal. Especially when the defendant had gone to great lengths in both cases to seek judicial review of its own draconian arbitration provisions, only to have the courts oblige by publishing two opinions which separately obliterate the enforceability of those provisions.

A bad strategic call by that defendant, you say? Probably. A delicious irony for those of us who abhor the ever-increasing trend by corporate defendants to impose binding arbitration on consumers? Most definitely. But perhaps most of all, the Second District's two recent decisions in *Cohen v. DirecTV, Inc.,* 2006 *Daily Journal D.A.R.* 12633 ("*Cohen*") and *Cable Connection, Inc. v. DirecTV, Inc.,* 2006 *Daily Journal D.A.R.* 12921 ("*Cable Connection*") make clear once and for all that those defendants can't blithely manipulate arbitration provisions they insert into contracts of adhesion to either escape exposure to class action litigation or to manufacture judicial review when they simply don't like an arbitrator's findings.

The Foibles of DirecTV

Although briefed and decided separately, both the *Cohen* and *Cable Connections* cases share the same defendant: DirecTV. For those of you who just can't do without 437 cable channels covering anything from mastering lawn bowling to preparing gourmet treats for Fido, you may want to avert your eyes for a moment. DirecTV may be a lot of things to a lot of people, but no one can credibly deny that it has been quite the aggressive protagonist of arbitration clauses. Remember the recent watershed opinion of *Garcia v. DirecTV, Inc.* (2004) 115 Cal.App.4th 297 ("*Garcia*")? In that case, just two years ago, the Second District – following U.S. Supreme Court review in *Green Tree Financial Corp. v. Bazzle* (2003) 539 U.S.

444 ("*Green Tree*") – held that in arbitration proceedings governed by the Federal Arbitration Act, an arbitrator (and not a judge) must decide whether class-wide arbitration is available under the adhesion contract in question.

But what a difference a few years makes. On the heels of our Supreme Court's decision last year in *Discover Bank v. Superior Court* (2005) 36 Cal.4th 148 ("*Discover Bank*," [holding that class action waivers in consumer contracts of adhesion are unconscionable and unenforceable in most circumstances]), the same Second District that decided *Garcia* has now decided both *Cohen* and *Cable Connection*. And it would appear that DirecTV's hardball litigation strategy on arbitration continues (albeit inadvertently) to be the vessel for that change.

***Cohen*: Confirming the Invalidity of Class Action Waivers**

In *Cohen*, the issue before the trial court was a mandatory arbitration clause – including a class action waiver – which DirecTV imposed on its subscribers by slipping those provisions in an amended agreement mailed with its monthly billing statements. You know the type: that odd bundle of junk mail and promotional ballast that nobody reads and everybody quickly throws away in order to get to the real mail – *the bill*. But when DirecTV asserted that among all of the ads for life insurance and new vacuums, a binding change in the subscriber agreement was also included, the trial court was not biting. It therefore found that DirecTV's arbitration agreement added by that surreptitious amendment was not only procedurally unconscionable, but was also substantively unconscionable to the extent it expressly forbade class-wide arbitration. *Cohen, supra*, 2006 *Daily Journal D.A.R.* at 12634.

Upon DirecTV's appeal, the Second District in *Cohen* focused little on whether a valid arbitration agreement was formed by way of the bill stuffer amendment, thereby ducking the question of whether that issue was for the trial court to decide in the first place. Instead, it went straight to the heart of the matter, concluding that such an amendment – banning class-wide arbitration – was clearly unconscionable under *Discover Bank, supra*. *Id*. at 12634-12635. It then reasoned that because that invalid class action waiver was not severable from the rest of DirecTV's arbitration provisions, the entire agreement was invalid. *Ibid*. In doing so, the *Cohen* court engaged in a cogent overview of *Discover Bank*, as well as surveyed a number of cases which have since applied the High Court's holding in a variety of contexts. *Id*. at 12634-12636. Indeed, given that no issue was raised regarding the application of the Federal Arbitration Act (which might have implicated the holding in *Green Tree*), *Cohen* can be viewed as *Discover Bank's* chief progeny, including a concise analysis of class-wide arbitration as the only mechanism capable of holding defendants responsible for widespread fraud or other wrongful conduct. *Id*. at 12636-12638. As such, *Cohen* is a invaluable read for attorneys involved in class litigation where any portion of the putative class may be subject to a binding arbitration agreement.

***Cable Connection:* Making Arbitration a Two-Way Street**

Although the *Cable Connection* case also raised the question of whether class-wide arbitration was appropriate under a similar DirecTV agreement (this time with its dealers), at its core, the case focused more on the fundamental need for reciprocity in the application of binding

arbitration provisions. Indeed, by way of its superior bargaining power and "take-it-or-leave-it" market position, DirecTV had written into those arbitration provisions language which only a crafty corporate lawyer can fully appreciate. Specifically, although ostensibly calling for "binding arbitration" in all respects, the DirecTV arbitration provisions cleverly withheld from the arbitrator "the power to commit errors of law or legal reasoning," and provided a mechanism to have an arbitration award "vacated or corrected on appeal" by "a court of competent jurisdiction" should any such error occur. *Cable Connection, supra*, 2006 *Daily Journal D.A.R.* at 12921. In other words, DirecTV managed to find a way to make its "binding" arbitration provisions non-binding if DirecTV did not like what an arbitrator decided. *Id.*
So when a panel of arbitrators found that the plaintiff-dealers could proceed with class-wide arbitration, DirecTV tactically moved the trial court to vacate that finding, asserting that the arbitrators had "exceeded their contractual-limited authority" by making "errors of law and legal reasoning." *Id*. at 12922. On review, however, the Second District reversed, finding that DirecTV could not make an end run around the very nature of "binding arbitration" by inserting self-serving language in its arbitration provisions allowing DirecTV to seek judicial review when it did not like an arbitrator's finding. *Id*. at 12923.

Indeed, implicated at some level in the *Cable Connection* decision is the inherent right of parties to freely contract for any type of arbitration they may want and the Legislature's power to limit judicial review of binding arbitration awards. By reasoning that arbitrators do not necessarily "exceed their authority" if they reach an erroneous result, but simply "act within the scope of that authority" on the controversy submitted to them, the *Cable Connection* court confirmed that "binding" arbitration means what it says: that it must be *binding*. *Id.* at 12923 [citing *Moncharsh v. Heily & Blaze* (1992) 3 Cal.4th 1, 11, which held that courts will review neither the merits of a controversy submitted to binding arbitration, nor the validity of an arbitrator's reasoning]. Moreover, by deferring to the Legislature's power to invest the trial courts with the right to review binding arbitration awards in only very limited circumstances (see, *e.g.*, Code of Civil Procedure §1296 [permitting judicial review of arbitration arising out of public construction contract agreements only]), but not extending that power of review elsewhere, the *Cable Connection* court inferred that the Legislature did not intend to confer traditional judicial review in private arbitration cases. *Id*. at 12925.

Thus, the Second District held in *Cable Connection* that the trial court erred in ruling that arbitrators "exceeded their powers" by allowing for class-wide arbitration of the plaintiff-dealer's claims. *Id*. at 12926-12927. But just for good measure, it then also concluded that even when such a finding was reviewable by the trial court for legal error, the arbitrators correctly followed California substantive law (*i.e., Discover Bank*) by finding that class-wide arbitration was appropriate in that case. *Ibid*.

CONCLUSION

It is heartening to see that, in the wake of the *Discover Bank* decision, the intermediate courts of appeal are finally re-thinking their approach to binding arbitration. And it's about time, as the expansion of binding arbitration provisions in adhesion contracts is at an all-time high. At some level, DirecTV also deserves credit for pushing the envelope on this subject in a changing legal environment, although clearly not achieving the results it intended. Indeed, in both *Cohen*

and *Cable Connection*, DirecTV presented itself as the archetypal corporate giant, looking both to insulate itself from liability and to open an exclusive window of judicial review when it wasn't happy with a particular arbitration award, through artful, yet one-sided contractual doublespeak. Of the two decisions, only *Cable Connection* raised a serious issue regarding the right of parties to circumscribe the limits of binding arbitration by contract, albeit on facts not particularly favorable to DirecTV. Perhaps if the issue is raised again by parties of equal bargaining power, there may be a viable way to limit an arbitrator's power to make legal errors. But unless DirecTV is bracing to make more law favorable to plaintiffs in the near future, that question will have to be answered on another day.