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One Minute Memo®

California Court Invents New Spell To Resuscitate Zombie Anti-Arbitration Ruling

Deepening a split among California courts, the Second District Court of Appeal, in *Franco v. Arakelian Enterprises*, No. B232583 (Nov. 26, 2012), has held that the California Supreme Court's anti-arbitration decision in *Gentry v. Superior Court* remains good law despite U.S. Supreme Court cases confirming that the Federal Arbitration Act ("FAA") preempts state laws that discriminate against arbitration agreements. *Franco* thus holds that an employer could not enforce an arbitration agreement that banned class actions and that banned representative actions under California's Private Attorney General Act of 2004 ("PAGA").

By way of brief background, the U.S. Supreme Court has repeatedly applied the FAA to repudiate state judicial and legislative efforts to impede the enforcement of arbitration agreements. A frequent target of the Supreme Court's censure has been the California Supreme Court. That court in recent years has issued two particularly prominent anti-arbitration decisions—*Discover Bank* (2005) and *Gentry* (2007). In *Discover Bank*, the California Supreme Court held that class action waivers in consumer arbitration agreements were unconscionable and thus unenforceable. In *Gentry*, the court held that class action waivers were also unconscionable in arbitration employment agreements whenever the facts indicated that an inability to pursue a class action waiver would frustrate the plaintiff's ability to enforce statutory rights.

The *Discover Bank* rule fell by the wayside in 2011, when the U.S. Supreme Court reaffirmed the preemptive power of the FAA to ensure that arbitration agreements are enforced according to their terms. In *AT&T Mobility v. Concepcion*, the Court expressly overruled the *Discover Bank* rule, because "it interferes with arbitration." The rationale of *Concepcion* also drew *Gentry's* fate into question, but the *Concepcion Court*, addressing a consumer contract, did not have the occasion to address *Gentry*.

Franco, like *Gentry*, is an employment case. The employer, which was sued in a class action for denying meal and rest breaks, moved to compel arbitration. The trial court denied the motion. The Court of Appeal, before Concepcion, affirmed this denial of the motion to compel, but then, after *Concepcion*, took the case again to see if *Gentry* remained good law.

After *Concepcion*, some supposed that *Gentry* was dead, but if that were ever so, *Franco* and other decisions have now bewitched it back to life. And *Franco* has done so not only by invoking a theory that plaintiffs need class actions to "vindicate[e] statutory rights," but also by inventing a new theory: *Gentry* survives—even if other anti-arbitration decisions do not—because *Gentry* invalidates class action waivers only on a case-by-case basis, and not on a categorical basis.

Franco borrowed its "statutory rights" theory from decisions refusing to enforce arbitration agreements in cases involving *federal* rights. That theory, now before the U.S. Supreme Court in *American Express Co. v. Italian Colors Restaurant*, posits that a plaintiff can avoid an arbitration agreement if the nature of the statutory rights at issue cannot be vindicated through arbitration. The *Franco* decision fails, in our view, to realize that while *federal* statutory rights can in some circumstances be litigated, notwithstanding the FAA, *state* statutory rights (such as those involved in *Franco*) are fully subject to the preemptive force of the FAA.

Franco's other basis for declaring that *Gentry* survives *Concepcion* is an argument that *Concepcion* invalidated the *Discover Bank* rule only because it was "a categorical rule against class action waivers in consumer contracts, thereby disfavoring arbitration." *Franco* reasons that *Gentry*, by contrast, created only a case-by-case test for unconscionability, which should avoid Concepcion's censure. We believe that the *Franco* decision in this respect misreads *Concepcion*, which held that the FAA preempts *any* state rule—categorical or not—that applies greater scrutiny to an arbitration agreement than to any other contract, regardless of state public policy consequences. This fundamental point is why other California courts and federal district courts have recognized that *Concepcion* effectively did overrule *Gentry*.

Gentry may in fact be dead, then. But until a higher authority corrects *Franco*, *Gentry* will walk among us, as the living dead, imposing obstacles to enforcing arbitration agreements in which the parties have waived resort to class actions and to representative proceedings such as PAGA claims.

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