No. 09-893

In the Supreme Court of the United States

AT&T MOBILITY LLC,

Petitioner,

v.

VINCENT AND LIZA CONCEPCION,

Respondents.

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

BRIEF OF CONTRACTS PROFESSORS AS *AMICI CURIAE* IN SUPPORT OF RESPONDENTS

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INTEREST OF *AMICI CURIAE*

Amici curiae are professors of contract law.[1] Based on their many years of experience teaching and publishing in the field of contracts, *amici* write to correct the account of contract law presented by AT&T Mobility ("ATTM") and its *amici* in this case. ATTM and its *amici* claim that courts in California—and by extension courts applying the law of nineteen other states—have "distorted" contract doctrine by finding class action bans in adhesion contracts to be unconscionable. However, ATTM and its *amici* fault these courts for failing to follow a version of the unconscionability doctrine that simply does not exist. This brief explains why it is ATTM and its *amici* that have distorted traditional contract principles.

SUMMARY OF ARGUMENT

This is a case about what the unconscionability doctrine is, not what ATTM and its *amici* want it to be. "Unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965). Courts will invalidate clauses that are procedurally unconscionable ("hidden and unexpected" or "arising from unequal bargaining

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[1] No counsel for a party authored this brief in whole or in part, and no such counsel of party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the *amici curiae*, or their counsel, made a monetary contribution to its preparation or submission. The parties have consented to the filing of this brief.

power") and substantively unconscionable ("one-sided, unreasonable, and lack[ing] justification"). *Perdue v. Crocker National Bank,* 38 Cal. 3d 913, 925 (Cal. 1985).

By empowering courts to strike down these terms, the unconscionability doctrine serves two purposes that are vital to the coherence of modern contract law. First, it preserves the role of mutual assent—contract's foundational principle—in the context of unilaterally-dictated, mass-produced adhesion contracts such as ATTM's. *See, e.g.,* RESTATEMENT (SECOND) OF CONTRACTS § 208, cmt. d. (noting that customers do not "assent or appear to assent" to "unfair terms" in adhesion contracts). Second, it prevents drafters from using fine print as a shield against liability, reducing their incentives to conform to the law, and rewriting their core duties to consumers into "guarant[ees of] nothing." *A & M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114, 125 (Ct. App. 1982) (voiding warranty disclaimer).

From these principles, it follows that class action bans in adhesion contracts can be unconscionable —whether they relate to arbitration or not. As the California Supreme Court explained in *Discover Bank v. Superior Court*, 113 P.2d 1100 (Cal. 2005), class action bans can be unconscionable for the same reasons that disclaimers of warranties and other one-sided terms can be unconscionable: they "serve[ ] as a disincentive for [drafters] to avoid the type of conduct that might lead to class action litigation in the first place," and thus grant "a license to push the boundaries of good business practices to their furthest limits." *Id.* at 1108 (quoting *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862, 868 (Ct. App. 2002)).

Nevertheless, ATTM contends that what it calls "California's rule" "bears no resemblance whatever to the traditional unconscionability principles that apply to contracts generally," and thus constitutes a special rule that governs "only . . . arbitration agreements." Brief for Petitioner ("ATTM's Brief") at 18. ATTM does not mention that "California's rule" is also far and away the *leading* rule: courts applying the law of nineteen other states have also voided class action bans in adhesion contracts. ATTM also does not mention that courts in California and elsewhere have invoked this supposedly "arbitration-specific" analysis to nullify class action bans in contracts that do not contain arbitration clauses. And finally, although ATTM asserts that California law establishes a "near-categorical ban on arbitration agreements that do not allow for class-wide dispute resolution," (ATTM's Brief at 15), ATTM does not mention that many courts in California alone have upheld class action bans in adhesion contracts when they do not exonerate the drafter from liability.

Instead, ATTM faults California courts for "deviating" from ATTM's own narrow, watered-down, idiosyncratic version of the unconscionability doctrine. First, ATTM claims that courts cannot deem a term to be substantively unconscionable unless it "shocks the conscience," or is so unfair that the non-drafting party must have been under a "delusion." But ATTM supports this position by citing late nineteenth and early twentieth century cases that applied the doctrine of intrinsic fraud: a hoary ancestor to the modern unconscionability defense that has little contemporary relevance.

Second, ATTM cites bounties that it supposedly provides for plaintiffs to arbitrate small-value claims on an individual basis as evidence that no reasonable court could deem its class action ban to be unfair. But these alleged rewards do not cure the inequity of ATTM's class action ban. As the Washington Supreme Court reasoned while voiding a supposedly incentive-laden class action ban written by ATTM's predecessor company, these asserted bonuses do not "make it worth the time, energy, and stress to pursue such individually small claims." *Scott v. Cingular Wireless,* 161 P.3d 1000, 1007 (Wash. 2007). Thus, ATTM retains its freedom from "potential liability for small claims, no matter how widespread." *Id.* at 1008. And in turn, as the district court in this case recognized, ATTM's ability to flout the law fundamentally reshapes its relationship with consumers. *See Laster v. T-Mobile USA, Inc.*, No. 05cv1167, 2008 WL 5216255, at *14 (S.D. Cal., Aug. 11, 2008) ("[t]his overarching policy concern of deterring corporate wrongdoing is not sufficiently addressed by ATTM's revised arbitration provision").

Third, ATTM faults *Discover Bank* for supposedly injecting ex post considerations into the unconscionability inquiry. ATTM argues that *Discover Bank* does so by conditioning a finding of unconscionability on plaintiffs both proving that small amounts of damages are at issue and alleging that the defendant misled or otherwise cheated customers. But these criteria are additional *hurdles* for plaintiffs; indeed, if plaintiffs cannot meet them, courts *enforce* class action bans. ATTM thus criticizes *Discover Bank* for actually increasing the odds that courts will *uphold* arbitration clauses.

ARGUMENT

I. The Policies Behind the Unconscionability Doctrine Apply With Full Force to Class Action Bans

"[C]onsent . . . is essential to the existence of a contract." CAL. CIV. CODE § 1550. To be sure, courts decide whether a party has consented objectively, based on "the reasonable meaning of their words and acts." *Bustamante v. Intuit, Inc.*, 45 Cal. Rptr. 3d 692, 699 (Ct. App. 2006). However, in the context of adhesion contracts such as ATTM's, this rule is subject to an important qualification. A drafter "does not ordinarily expect his customers to understand or even read the standard terms." RESTATEMENT (SECOND) OF CONTRACTS § 211 cmt. b (1979). Thus, as Karl Llewellyn, the architect of the Uniform Commercial Code, famously observed, a drafter cannot reasonably view a customer's *apparent* consent to one-sided terms in an adhesion contract as *actual* consent:

> Instead of thinking about 'assent' to boiler-plate clauses, we can recognize that so far as concerns the specific, there is no assent at all. What has in fact been assented to, specifically, are the few [negotiated] terms, and the broad type of the transaction, and but one thing more. That one thing more is a blanket assent (not a specific assent) to any not unreasonable or indecent terms the seller may have on his form.

KARL N. LLEWELLYN, THE COMMON LAW TRADITION 362 (1960).[2]

The unconscionability doctrine is one tool that courts use to nullify non-consensual terms in adhesion contracts. As the D.C. Circuit explained in the watershed case of *Williams*, 350 F.2d 445, the two-pronged test for unconscionability, with its procedural and substantive elements, pinpoints non-consensual terms:

> [W]hen a party of little bargaining power, and hence little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, *it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms*.

Id. at 449-50 (emphasis added); *accord A & M Produce*, 186 Cal. Rptr. at 122 (linking the unconscionability doctrine to the fact that "contract terms not actively negotiated between the parties fall outside the 'circle of assent'"); *cf. Ilkhchooyi v. Best*, 45 Cal. Rptr. 2d 766, 775 (Ct. App. 1995) ("The burden should be on the party submitting [an adhesion contract] to show that the other party had knowledge of any unusual or

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[2] *Accord* RESTATEMENT (SECOND) OF CONTRACTS § 211(3) (in the context of adhesion contracts, if a "party manifesting . . . assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement"); Randy E. Barnett, *Consenting to Form Contracts*, 71 FORDHAM L. REV. 627, 638 (2002) ("if most reasonable persons would not have agreed to such a term, then the other party cannot assume consent to be bound to such a term unless it is made visible").

unconscionable terms contained therein" (quotation marks omitted)).[3]

In addition, courts regulate adhesion contracts by striking down "clauses of limitation of liability which are unclear, unexpected, inconspicuous or unconscionable." *Steven v. Fidelity & Cas. Co.,* 58 Cal.2d 862, 879 (1962). In California, this principle emanates from Civil Code section 1668, which prohibits "[a]ll contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, . . . or violation of law, whether willful or negligent."

Two policies underlie rigorous judicial review of adhesive terms that reduce the drafter's accountability. First, these terms, often projected across thousands or even millions of contractual relationships, allow drafters to ignore their obligations under the substantive law. *See Hiroshima v. Bank of Italy*, 248 P. 947, 953 (Cal. 1928) (voiding damages limitation in contract imposed by bank because the "public . . . is interested in seeing that the bank is held

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[3] *See also* RESTATEMENT (SECOND) OF CONTRACTS § 208, cmt. d ("gross inequality of bargaining power, together with terms unreasonably favorable to the stronger party, may confirm . . . that the weaker party . . . did not in fact assent or appear to assent to the unfair terms"); *id.* at § 211 cmt. c (because customers only "assent[ ] to a few terms," standard forms are subject to "the power of the court to refuse to enforce an unconscionable contract or term"). Indeed, members of this Court have recognized that "a determination that a contract is 'unconscionable' may in fact be a determination that one party did not intend to agree to the terms of the contract." *Am. Airlines, Inc. v. Wolens*, 513 U.S. 219, 249 (1995) (O'Connor, J., joined by Thomas, J., concurring in part and dissenting in part).

accountable for the ordinary and regular performance of its duties"). More fundamentally, the fact that these clauses are "unjust and unreasonable" underscores that they are "wanting in the element of voluntary assent." *The Kensington*, 183 U.S. 263, 268 (1902) (voiding liability waiver in steamship ticket).

For instance, in *Tunkl v. Regents of University of Cal.*, 383 P.2d 441 (Cal. 1963), the California Supreme Court nullified a hospital's release of negligence liability. The state high court explained that section 1668 forbade damages waivers—even for bare negligence—in contracts that "involved the public interest." *Id.* at 444. The hallmarks of such a contract, the court reasoned, included the drafter's (1) status as a business "of a type generally thought suitable for public regulation," (2) performance of a service "which is often a matter of practical necessity for some members of the public," (3) "willing[ness] to perform this service for any member of the public who seeks it," and (4) use of a "standardized adhesion contract of exculpation." *Id.* at 445-46. According to the court, when these factors are present, "the releasing party *does not really acquiesce voluntarily in the contractual shifting of the risk*." *Id.* at 446 (emphasis added).[4]

In *Discover Bank*, 113 P.3d 1100, the California Supreme Court drew on California's well-established

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[4] On the other hand, where more than bare negligence is involved—"where the contract purports to avoid liability for fraud, willful injury, or violation of law, whether intentional or negligent"—then "[t]he plain language of section 1668 renders . . . exculpatory provisions invalid." *Capri v. L.A. Fitness Intern., LLC*, 39 Cal. Rptr. 3d 425, 429 (Ct. App. 2006).

unconscionability doctrine and section 1668 to establish parameters for the validity of class action bans. In that case, a company had unilaterally grafted a class action ban into a consumer contract through a non-descript "bill stuffer." *Id.* at 1108. The court cited that fact as evidence that "an element of procedural unconscionability is present." *Id.* The court then reasoned that because class action bans in small-dollar consumer cases "operate to insulate a party from liability," they can be found substantively unconscionable in certain circumstances:

> when the waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably involve small amounts of damages, and when it is alleged that the party with the superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money, then . . . the waiver becomes in practice the exemption of the party 'from responsibility for [its] own fraud, or willful injury to the person or property of another.'

Id. at 1110 (quoting CAL. CIV. CODE § 1668).

ATTM casts *Discover Bank* as a California-specific rule that amounts to a "near-categorical ban on arbitration agreements that do not allow for class-wide dispute resolution." ATTM's Brief at 15; Brief of DRI—The Voice of the Defense Bar as *Amicus Curiae* in Support of Petitioner ("DRI's Brief") at 21 (criticizing "California's novel and elusive approach"); Brief *Amici Curiae* of Distinguished Law Professors in Support of Petitioner ("Professors' Brief") at 3

("California courts have . . . erect[ed] an insurmountable barrier to bilateral arbitration in all consumer contracts"). These claims are mistaken.

For one, *Discover Bank*'s recognition that class action bans can be unconscionable is not just "California's" approach—it is the runaway *leading* approach. Courts applying the law of at least twenty states have also determined that class action bans are unconscionable when they "insulate [the drafter] from liability," *Kinkel v. Cingular Wireless LLC*, 857 N.E.2d 250, 274 (Ill. 2006) "act effectively as an exculpatory clause," *Muhammad v. County Bank of Rehoboth Beach, Delaware*, 912 A.2d 88, 99 (N.J. 2006), and thus license "a broad range of wrongful conduct." *Scott,* 161 P.3d at 1009.[5]

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[5] *See also Leonard v. Terminix Int'l Co., L.P.*, 854 So. 2d 529, 535-36 (Ala. 2002); *Cooper v. QC Financial Services, Inc.*, 503 F. Supp. 2d 1266, 1279-80 (D. Ariz. 2007); *Powertel v. Bexley*, 743 So. 2d 570, 576 (Fla. Ct. App. 1999); *Dale v. Comcast Corp.*, 498 F.3d 1216, 1224 (11th Cir. 2007) (applying Georgia law); *Lazado v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087, 1105 (W.D. Mich. 2000); *Feeney v. Dell, Inc.*, 908 N.E.2d 753, 762-68 (Mass. 2009); *Brewer v. Missouri Title Loans, Inc.*, No. SC90647., -- S.W.3d --, 2010 WL 3430411, at *4-*5 (Mo., Aug. 31, 2010); *Fiser v. Dell Computer Corp.*, 188 P.3d 1215, 1222 (N.M. 2008); *Tillman v. Commercial Credit Loans, Inc.*, 655 S.E.2d 362, 373 (N.C. 2008); *Vasquez-Lopez v. Beneficial Oregon, Inc.*, 152 P.3d 940, 944 (Or. App. 2007); *Thibodeau v. Comcast Corp.*, 912 A.2d 874, 886 (Pa. Super. Ct. 2006); *Coady v. Cross Country Bank, Inc.*, 729 N.W.2d 732, 746 (Wis. App. 2007); *Whitney v. Alltel Communications, Inc.*, 173 S.W.3d 300, 308, 310 (Mo. App. 2005); *Herron v. Century BMW*, 693 S.E.2d 394, 399 (S.C. 2010); *State ex rel. Dunlap v. Berger*, 567 S.E.2d 265, 272 n.3 (W. Va. 2002).

Moreover, despite ATTM's claim that these decisions evidence "discrimination" against arbitration, courts in California and elsewhere have employed the same reasoning and found class action bans to be unfair both when they are embedded in arbitration clauses and when they are not. *See, e.g., America Online, Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699, 712 (Ct. App. 2001) (striking down forum-selection clause that thwarted "the right to seek class action relief in consumer cases[, which] has been extolled by California courts"); *Dix v. ICT Group, Inc.*, 161 P.3d 1016, 1024 (Wash. 2007) (refusing to enforce forum selection clause that would eliminate the ability to bring a class action); *America Online, Inc. v. Pasieka*, 870 So.2d 170, 172 (Fla. Ct. App. 2004) (same).

Finally, although ATTM views these decisions as posing an "insurmountable barrier" to bilateral arbitration, numerous courts in California alone have upheld class action waivers under *Discover Bank*. *See, e.g., Arguelles-Romero v. Superior Court*, 109 Cal. Rptr. 3d 289, 305 (Ct. App. 2010) (enforcing class arbitration waiver in financing contract where "plaintiffs failed to establish that the individual amounts at issue are so small that a class action is the only viable remedy"); *Walnut Producers of California v. Diamond Foods, Inc.*, 114 Cal. Rptr. 3d 449, 461 (Ct. App. 2010) ("plaintiff's complaint does not establish that the Agreement's class action waiver acted as an exculpatory clause or unduly hindered plaintiffs from pursuing a legal remedy").[6]

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[6] *See also Gold v. Melt, Inc.*, No. B210452, 2010 WL 1509795, at *8 (continued...)

Accordingly, courts in California and other states invoke the unconscionability doctrine to preserve the role of mutual assent in contract law and to prevent drafters from using fine print to effectively rewrite or evade their duties and responsibilities. For precisely these reasons, courts find class action bans to be unconscionable—whether within a contract mandating arbitration or not.

II. ATTM Fails to Demonstrate that Courts Voiding Class Action Bans Deviate From Traditional Unconscionability Principles

Nevertheless, ATTM contends that cases invalidating class action bans under the unconscionability doctrine "bear[ ] no resemblance whatever to the traditional unconscionability

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[6](...continued)
(Cal. Ct. App., Apr. 16, 2010) ("The elements of unconscionability not being present, we conclude that the class action waivers in the Melt franchise agreements are enforceable."); *Dalie v. Pulte Home Corp.*, 636 F. Supp. 2d 1025, 1029 (E.D. Cal. 2009) ("plaintiffs ha[ve] not shown that a 'small' amount of damages was at issue for each plaintiff"); *Provencher v. Dell, Inc.*, 409 F. Supp. 2d 1196, 1202 (C.D. Cal. 2006) ("Mr. Provencher's claims do not involve a small amount of money"); *Smith v. Americredit Fin. Servs., Inc.*, No. 09cv1076, 2009 WL 4895280, at *7 (S.D. Cal., Dec. 11, 2009) ("the Court finds this case does not satisfy the second prong of *Discover Bank*"); *McCabe v. Dell, Inc.*, No. CV 06-7811, 2007 WL 1434972, at *4 (C.D. Cal., Apr. 12, 2007) ("Defendant has not immunized itself from liability"); *Torres v. Chrysler Fin. Co.*, No. C 07-00915, 2007 WL 3165665, at *3 (N.D. Cal., Oct. 25, 2007) ("Plaintiff has failed to allege that Defendants have 'deliberately cheat[ed] large numbers of consumers out of individually small sums of money' as required by *Discover Bank*" (quoting *Discover Bank*, 113 P.3d at 1110)).

principles that apply to contracts generally." ATTM's Brief at 18. ATTM is wrong.

A. ATTM Relies on an Obsolete Definition of Substantive Unconscionability

ATTM cites *Hume v. United States*, 132 U.S. 406 (1889) and *Eyre v. Potter*, 15 How. (56 U.S.) 42 (1853) for the proposition that "California equates unconscionability with terms that shock the conscience and to which no person who is not acting under delusion would agree." ATTM's Brief at 3-4, 18, 32-33; DRI Brief at 5-6; Law Professor Brief at 19-20. However, these cases deal with intrinsic fraud: an entirely different—and completely outdated—strand of the unconscionability doctrine.

The intrinsic fraud rule allowed judges to void deals between parties with *equal* bargaining power based on nothing more than gross inadequacy of consideration. For instance, in *Hume*, the party invoking the rule was none other than the federal government. 132 U.S. at 414. The Court held that the contract, which called for the government to buy items at "35 times their highest market value" was "fraudulent" because it was "such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other." *Id.* Similarly, in *Eyre*, a widow allegedly sold tens of thousands of dollars in inheritance rights for a mere $1,000, and the Court opined that "unconscionableness" may vitiate a contract if it "shock[s] the conscience[ ] and amount[s] in itself to conclusive and decisive evidence of fraud." *Eyre*, 56 U.S. at 60. Of course, nullifying a deal based on nothing more than a disparity of the values exchanged cuts hard against the grain of contract law.

Thus, it is no surprise that courts insisted on such forceful proof.

However, the intrinsic fraud rule has never been the sum total of the unconscionability doctrine. Courts sitting in equity routinely declined to specifically enforce contracts that were "unconscionable or inequitable." *Milton Kauffman, Inc., v. Smith*, 82 Cal.App.2d 302, 304-05 (1947). Unlike the intrinsic fraud rule, this equity-based unconscionability doctrine did not require proof that a bargain would "shock the conscience of the chancellor." *Haddock v. Knapp,* 171 Cal. 59, 61-62 (1915) (rejecting that very argument and refusing to specifically enforce deal to sell $2,500 of property for $1,800); *Wilson v. White*, 161 Cal. 455, 465 (1911) (refusing to specifically enforce agreement to sell for $14,000 a tract of land worth $15,000).

The modern version of unconscionability—the one that governs adhesion contracts—is a hybrid of the intrinsic fraud and equitable unconscionability rules. For instance, in *Williams*, 350 F.2d at 449, the D.C. Circuit defined substantive unconscionability as "terms which are unreasonably favorable to the other party." The court quoted *Hume*'s language about "delusion[s]" as representative of the distinct "common law doctrine of intrinsic fraud." *Id.* at 499 n.7. Most jurisdictions have now endorsed some version of *Williams*' definition of substantive unconscionability. For instance, the New Mexico Supreme Court recently "specifically disapproved" of the "delusion" test from *Hume*:

> Our law has never really required that a person seeking relief from an unconscionable contract

> must first establish that he or she actually had to have been a madman or a fool to sign it. The repetition of this unhelpful terminology from a bygone age only serves to confuse the unconscionability issues without serving any constructive purpose.

Cordova v. World Finance Corp., 208 P.3d 901, 909-10 (N.M. 2009).[7]

California also follows the modern view of substantive unconscionability. The legislative purposes section of California's unconscionability statute refers only to "one-sided" terms and says nothing about "delusions" or "shocked consciences." CAL. CIV. CODE § 1670.5. Moreover, the leading California appellate case, *A&M Produce*, 186 Cal. Rptr. at 122 merely declares that "a contractual term is substantively suspect if it reallocates the risks of the bargain in a objectively unreasonable or unexpected manner." In *Perdue*, 38 Cal. 3d at 925 n.9, the California Supreme Court expressly endorsed *A&M Produce*'s approach and stated that substantive unconscionability "involve[s] consideration of whether

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[7] For a non-comprehensive list of courts in other states that have also eschewed the "delusion" and "shock the conscience" tests, *see Fotomat Corp. v. Chanda*, 464 So.2d 626, 629 (Fla. Ct. App. 1985); *Branco v. Norwest Bank Minnesota, N.A.*, 381 F. Supp. 2d 1274, 1281 (D. Hawaii 2005); *Razor v. Hyundai Motor America*, 854 N.E.2d 607, 622 (Ill.2006); *Zapatha v. Dairy Mart, Inc.*, 408 N.E.2d 1370, 1376 (Mass. 1980); *Myers v. Neb. Inv. Council*, 724 N.W.2d 776, 799 (Neb. 2006); *Shell Oil Co. v. Marinello*, 307 A.2d 598 (N.J. 1973); *Collins v. Click Camera & Video, Inc.*, 621 N.E.2d 1294, 1299 (Ohio Ct. App. 1993); *In re Palm Harbor Homes, Inc.*, 195 S.W.3d 672, 678 (Tex. 2006); *Leasefirst v. Hartford Rexall Drugs, Inc.*, 483 N.W.2d 585, 587 (Wis. Ct. App. 1992).

the provision [i]s one-sided, unreasonable, and lack[s] justification." Neither case involved arbitration, and neither case adopted ATTM's "delusion" or "shock the conscience" tests.[8]

Indeed, the "delusion" or "shock the conscience" tests are out of step with modern unconscionability. The intrinsic fraud rule was a kind of super-substantive unconscionability: it applied even when there was no inequality of bargaining power or fine print. Yet the modern unconscionability doctrine imposes the additional requirement that a contract be procedurally unconscionable. Insisting that a procedurally unconscionable term *also* be "delusive" or "conscience shocking" would thus make it more difficult to challenge the validity of an adhesion contract than a bargained-for deal between equals: a result that cannot be correct. Thus, it is ATTM's

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[8] For California authority, ATTM and its *amici* rely on (1) decades-old cases that involve the intrinsic fraud rule, *see* ATTM Brief at 3-4 (citing *Herbert v. Lankershim*, 9 Cal.2d 409 (1937) and *Odell v. Moss*, 130 Cal. 352 (1900)) and (2) a handful of recent cases from the First and Fourth Appellate Districts that have disagreed with *A&M Produce*'s definition of substantive unconscionability. *See* ATTM Brief at 3-4, 34 n.10, 38; Professor Brief at 19-21 (citing, for example, *American Software, Inc. v. Ali*, 54 Cal. Rptr. 2d 477 (Ct. App. 1996), *California Grocers Assn. v. Bank of America*, 27 Cal. Rptr. 2d 396 (Ct. App. 1994), and *Morris v. Redwood Empire Bancorp*, 27 Cal.Rptr.3d 797 (Ct. App. 2005)). ATTM and its *amici* fail to explain, however, how the California Supreme Court "discriminates" against arbitration by failing to adopt a minority view among inferior appellate courts and instead following its own, non-arbitration-related precedent.

definition of substantive unconscionability—not the California Supreme Court's—that "distorts" the law.[9]

B. ATTM's Class Action Ban Is Unconscionable Because It Reduces ATTM's Potential Liability and Thus ATTM's Incentives to Conform to the Law

ATTM next argues that because it offers bounties for plaintiffs to arbitrate small-value claims on an individual basis, no court faithfully applying the common law of contracts could find that its class action ban is unfair. ATTM contends that the district court

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[9] ATTM's *amici* DRI purports to quote the RESTATEMENT (SECOND) OF CONTRACTS § 208, cmt. b as follows:

> "Traditionally"—and to this day—"a bargain was said to be unconscionable" only "'if it was such as no man in his sense and not under a delusion would make on the one hand, and as no honest and fair man would accept on the other.'"

DRI's Brief at 5. In full, however, the passage from section 208 reads:

> *b. Historic standards.* Traditionally, a bargain was said to be unconscionable *in an action at law* if it was 'such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other.'

By omitting the phrases "[h]istoric standards" and "action at law" and adding the words "to this day," DRI removes any reference to the doctrine of equitable unconscionability and thereby creates the false impression that the "delusion" test remains as influential as it was a century ago.

and Ninth Circuit "effectively" found that its class action ban is "fair to the Concepcions." ATTM's Brief at 35. According to ATTM, these courts thus voided its class action ban out of "concern for the rights of third persons other than the parties to the agreement before the court." *Id.* at 36. ATTM then asserts that this approach "finds no support" within contract law and is therefore "plainly discriminatory" against arbitration. *Id.*

ATTM is wrong on all counts. First, ATTM's purported rewards for pursuing claims individually do not make its class action ban "fair to the Concepcions"—and the courts below found no such thing. ATTM places tremendous emphasis on the district court's statement that "a reasonable consumer may well prefer quick informal resolution with likely full payment over class litigation." ATTM's Brief at 11, 18, 33, 34-36 (quoting *Laster*, 2008 WL 5216255, at *12). But this language does not mean that the district court found that ATTM's class action ban is fair for purposes of the unconscionability doctrine. The relevant question is not whether consumers would rather arbitrate individually or as a class *once a dispute arises*.[10] Instead, the issue hinges on whether, *at the time of contracting*, it is unfair to impose upon consumers a class action ban that supposedly creates incentives to pursue claims individually but also saddles each consumer with the sole responsibility for uncovering and challenging future wrongdoing.

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[10] Indeed, that would be exactly the kind of ex post perspective that ATTM condemns. *See infra* Part II(C).

The district court and Ninth Circuit below correctly held that the class action ban was unfair. These courts began by noting a fact that ATTM cannot and does not dispute: because few consumers will learn that their rights have been violated, and fewer still will seek redress, the class action ban "greatly reduc[es]" its "aggregate liability." *Laster v. AT&T Mobility LLC*, 584 F.3d 849, 856 (9th Cir. 2009); *Laster*, 2008 WL 5216255, at *13 (reasoning that the class action ban allows ATTM to "avoid potential liability to thousands of other customers who have no knowledge of the alleged wrongdoing").

Courts in several states have also determined that ATTM's class action ban acts as a bulwark against liability. For instance, in *Coneff v. AT&T*, 620 F. Supp. 2d 1248 (W.D. Wash. 2009), a district court applying Washington law concluded that a "miniscule" number—fewer than two hundred of ATTM's seventy million customers—had invoked its supposedly pro-consumer features, suggesting that they "are either unaware of their right[s]" or truly "have no incentive to bring their claims." *Id.* at 1258-59; *accord Hall v. AT&T Mobility LLC*, 608 F. Supp. 2d 592, 595, 603-04 (D.N.J. 2009) (reasoning that ATTM's class action ban "allows ATTM to escape liability . . . because while it may settle with several individuals for $175, the truth of the matter is that a large percentage of consumers will not file suit"); *Scott*, 161 P.3d at 1007 (voiding a supposedly incentive-laden class action ban drafted by ATTM's predecessor company because without the class action device, "many consumers may not even realize that they have a claim"); *Stiener v. Apple Computer, Inc.*, 556 F. Supp. 2d 1016, 1029 (N.D. Cal.

2008) (holding that ATTM's "incentives" are "illusory").[11]

In turn, this "'get out of jail free' card," *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862, 868 (Ct. App. 2002), all but abolishes ATTM's incentives to conform to the law. As the district court below explained, the class action ban "serve[s] as a disincentive for [ATTM] to avoid the type of conduct that might lead to class action litigation in the first place." *Laster*, 2008 WL 5216255, at *13-*14 (quoting *Discover Bank*, 113 P.3d at 1108). Under well-established California precedent, a term can be substantively unconscionable for precisely that reason. For instance, in *A&M Produce*, 186 Cal. Rptr. 114, the court of appeals nullified a disclaimer of warranties and consequential damages in a contract between two businesses. The court reasoned that by reducing its damages exposure, the drafter "was in essence guarantying nothing about what the product would do," and that it would be "patently unreasonable to assume that a buyer would purchase a standardized mass-produced product from an industry seller without any enforceable performance standards." *Id.* at 125.

As in *A&M Produce*, ATTM's class action ban undermines its core obligations to consumers. Without the specter of class action liability, ATTM can flout its contractual promises and other legal duties. This is true no matter what incentives ATTM creates to

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[11] It bears emphasis that the question before this Court is not whether these holdings are correct, but whether they deviate so flagrantly from traditional contract law that they evidence "discrimination" against arbitration.

pursue individual claims in arbitration. These bells and whistles do not cure the fact that ATTM's class action ban requires each individual consumer to bear the costs of (1) monitoring every aspect of ATTM's conduct, (2) acquiring information about the lawfulness of this conduct, and (3) affirmatively seeking relief for any malfeasance. This is a significant reallocation of risk. Indeed, consumers already "must spread their attention 'thinly across thousands of transactions and the management of hundreds of possessions.'" Jeff Sovern, *Toward a New Model of Consumer Protection: The Problem of Inflated Transaction Costs*, 47 WM. & MARY L. REV. 1635, 1661 (2006) (quoting E. Scott Maynes, *Consumer Problems in Market Economies*, in ENCYCLOPEDIA OF THE CONSUMER MOVEMENT 158, 163 (1997)).[12] Thus, because it is unfair to require consumers to police ATTM's conduct themselves, ATTM's class action ban is unconscionable.

But even if ATTM were correct that its class action ban was "fair to the Concepcions," it is wrong that courts must ignore "the impact of the challenged provision upon third parties." ATTM's Brief at 36-37. *Lynwood Redevelopment Agency v. Angeles Field Partners, LLC*, 2009 WL 4690213, at *8 (Cal. Ct. App.

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[12] As this case illustrates, there is also a real risk that consumers will neither notice nor understand ATTM's claimed incentives. ATTM unilaterally added these terms—which are so complex that ATTM requires three pages of briefing just to summarize them, see ATTM's Brief at 5-7—to all of its existing contracts by mailing "bill stuffers" to its customers. *See Laster*, 2008 WL 5216255, at *6-*7; David Horton, *The Shadow Terms: Contract Procedure and Unilateral Amendments*, 57 UCLA L. REV. 605, 655 (2010) (noting that ATTM's clause "is likely unintelligible to most consumers").

Dec. 10, 2009), the unpublished, non-precedential decision on which ATTM relies, reversed a trial court decision that had accepted the far-fetched argument that it would be unconscionable to voters to enforce a contract to which they were not parties: one between their city council and developers. Conversely, here the district court's fairness concerns—that ATTM had "granted itself a license to push the boundaries of good business practices to their furthest limits," *Laster*, 2008 WL 5216255, at *14 (quoting *Discover Bank*, 113 P.3d at 1108)—center on the very consumers who are subject to the class action ban. ATTM cites no authority for the proposition that a court cannot weigh the effect of its class action ban on other *contract signatories*.[13]

And in any event, courts applying California Civil Code section 1668 and *Tunkl*, 383 P.2d 441 strike down limitations on liability to protect other signatories who are not before the court and even

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[13] Courts can employ the unconscionability doctrine to "avoid any unconscionable result." CAL. CIV. CODE § 1670.5(b). Historically, this sweeping standard did, in fact, allow courts to consider effects of the contract on non-parties. For instance, in the intrinsic fraud cases on which ATTM relies for its definition of substantive unconscionability, courts often invalidated unwise deals entered into by prospective heirs to convey money they would soon inherit from their parents. Courts did so not to protect the heirs (who were parties to the contract), but the parents (who were not). *See, e.g., McClure v. Raben*, 25 N.E. 179, 181 (Ind. 1890) (noting that courts voided these contracts "because they unconscientiously compromise . . . the private rights, interests, duties, or intentions of third persons" (quoting STORY'S COMMENTARIES ON EQUITY JURISPRUDENCE AS ADMINISTERED IN ENGLAND AND AMERICA § 328)).

strangers to the contract.[14] Section 1668, which was enacted in 1872, forbids "[a]ll contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury . . . or violation of law, whether willful or negligent." Thus, in *Hiroshima*, 248 P. 947, the California Supreme Court voided a liability release in a banking form because "'the banking public, as well as the particular individual [in the case] . . . is interested in seeing that the bank is held accountable for the ordinary and regular performance of its duties." *Id.* at 953; *see also Fairfax Gas & Supply Co. v. Hadary*, 151 F.2d 939, 941 (4th Cir. 1945) (noting that in situations where "one person is dealing contemporaneously with several others . . . a clause limiting his liability to one of them is considered to have a tendency to lead to conduct injurious to others" (quoting 6 WILLISTON ON CONTRACTS § 1715(c)).[15]

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[14] Courts and commentators have noted that *Tunkl*'s rule against exculpatory clauses and the unconscionability doctrine are often interchangeable. *See, e.g., Continental Airlines, Inc. v. Goodyear Tire & Rubber Co.*, 819 F.2d 1519, 1527 (9th Cir. 1987) ("*Tunkl*'s approach is essentially rooted in the unconscionability doctrine"); Daniel I. Reith, *Contractual Exculpation From Tort Liability in California—The "True Rule" Steps Forward,* 52 CAL. L. REV. 350 (1964) (noting that unconscionability "is aimed at preventing over-reaching in the same adhesion contract situations dealt with in *Tunkl*"); RESTATEMENT (SECOND) CONTRACTS § 195 ("a party's attempt to exempt himself from liability for negligent conduct may fail as unconscionable").

[15] For this reason, ATTM is simply wrong when it asserts that section 1668 does not permit courts to consider "potential impacts on nonparties, as opposed to solely the party before the court." ATTM's Brief at 43-44.

ATTM argues that section 1668 does not apply because its class action ban "does not immunize [it] from *all* liability" and thus "is not 'exculpatory' in any ordinary sense of the term." ATTM's Brief at 47, 42 (emphasis added). But that is not the standard for determining whether section 1668 applies. Section 1668 vitiates "[a]ll contracts which . . . indirectly . . . exempt anyone from [legal] responsibility." As a matter of settled California law, a contract can violate section 1668 even if it is merely "a limitation on liability and . . . not a complete exemption." *Health Net of Cal., Inc. v. Dep't of Health Services*, 6 Cal. Rptr. 3d 235, 247 (Ct. App. 2003). For instance, in *Klein v. Asgrow Seed Co.*, 54 Cal. Rptr. 609, 617 (Ct. App. 1966), a clause in a seed manufacturer's agreement limited damages to the price of the seed, but did not exclude damages completely. The court held that "section 1668 makes the statement of limitation-of-liability void." *Id.* at 609.

In sum, because ATTM's class action ban delegates the task of preventing corporate wrongdoing to each individual consumer, it is unfair to impose that clause on consumers through an adhesion contract—even if ATTM is likely to make whole any consumers intrepid enough to sue. And even if ATTM were correct that the class action ban is fair to consumers who invoke its provisions, it is not fair to absent consumers who will never learn about or receive compensation for ATTM's malfeasance.[16]

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[16] ATTM's *amici* law professors also fault California courts for factoring the issue of "mutuality" into their unconscionability calculus. *See* Professors' Brief at 24-28. Yet even according to their own description, a lack of mutuality occurs when a contract

(continued...)

C. ATTM Fails to Show that *Discover Bank* Improperly Adopts an Ex Post Perspective

ATTM also argues that *Discover Bank* improperly adopts an ex post perspective because it instructs courts to consider whether a plaintiff "allege[s] that the party with the superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money." ATTM's Brief at 38 (quoting *Discover Bank*, 113 P.3d at 1110); DRI's Brief at 14 ("the clearest evidence of the court's ex post approach is its reliance on the customer's underlying allegations").

But ATTM misunderstands this aspect of the analysis. Rather than *expanding* the situations in which courts can deem class action bans to be unconscionable, it *limits* them. The first two *Discover Bank* variables stand for the proposition that class action bans in adhesion contracts are unconscionable at the time of contracting:

> when [1] the waiver is found in a consumer contract of adhesion [2] in a setting in which disputes between the contracting parties predictably involve small amounts of damages . . . .

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[16](...continued)
term is "one-sided." *Id.* at 25. As the California Supreme Court has declared outside of the arbitration context, a term can be substantively unconscionable precisely because it is "one-sided." *Perdue,* 38 Cal. 3d at 925.

Discover Bank, 113 P.3d at 1110. If this were the entire standard, few class action bans in consumer contracts would pass muster.

But the third factor—the one that ATTM attacks—recognizes *an exception* to what would otherwise be a bright-line rule: it requires plaintiffs to prove that they truly do seek "small sums of money." *Id.* Indeed, if the circumstances reveal that plaintiffs actually intend to pursue large damage awards, they do not meet this criterion. *See, e.g., Dalie*, 636 F. Supp. 2d at 1029 (enforcing class action ban for failure to show "that a 'small' amount of damages was at issue"); *Provencher*, 409 F. Supp. 2d at 1202 (same). Likewise, by conditioning unconscionability on specific allegations of misconduct, the third factor excludes plaintiffs with garden-variety tort and contract cause of action.[17]

Thus, the part of *Discover Bank* that ATTM challenges *exempts* contracts from invalidity and *narrows* the scope of the unconscionability doctrine. To the extent that there is any correlation between class action bans and arbitration clauses, this factor hardly "discriminates" against arbitration. To the contrary, it makes it more likely that courts will *enforce* arbitration clauses.

ATTM's *amici* DRI argues that the third prong of *Discover Bank* somehow prevents courts from

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[17] Not all states recognize this limitation. *See, e.g., Jones v. DirecTV, Inc.*, 667 F. Supp. 2d 1379, 1381 (N.D. Ga. 2009) (voiding class action ban when plaintiff merely alleged that the defendant breached a contract, not misled customers).

considering that "customer[s] benefit[ ] from . . . lower prices" in exchange for ATTM's class action ban. DRI's Brief at 11-12. But the proper target of DRI's ire is not *Discover Bank*, but rather the unconscionability doctrine itself. If courts presumed that (1) harsh terms lead to lower prices and that (2) buyers prefer lower prices to fair terms, then courts would *always* enforce harsh terms. That is not the law.[18] The unconscionability doctrine is firmly on the books. This case is not a referendum on it.

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[18] In any event, the proposition that drafters pass savings from harsh terms back to customers has been widely questioned. *See, e.g.,* R. Ted Cruz & Jeffrey J. Hinck, *Not My Brother's Keeper: The Inability of an Informed Minority to Correct for Imperfect Information*, 47 HASTINGS L.J. 635, 664 (1996) (noting that this theory "does not accurately describe what usually occurs in the market"); *Ting v. AT&T*, 182 F. Supp. 2d 902, 931 (N.D.Cal. 2002), *aff'd in part and rev'd in part by Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003) ("while lower costs can produce lower charges, they can also produce higher profits"). Moreover, the article on which DRI heavily relies, *see* DRI's Brief at 16-17, concludes that courts should invoke the unconscionability doctrine to nullify harsh terms *even if those terms result in lower prices to consumers*. *See* Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1293-94 (2003) ("enforcement of all [adhesion contract] terms will not create socially optimal contracts").

CONCLUSION

For these reasons, the Court should affirm the Ninth Circuit's decision.

Respectfully submitted,

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APPENDIX

APPENDIX INDEX

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