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MCGILL V CITIBANK: DID THE CALIFORNIA SUPREME COURT JUST FORCE JUSTICE GORSUCH AND THE U.S. SUPREMES TO PUT THE HAMMER DOWN ON STATE COURTS THAT DO NOT SEE THE ARBITRATION WRITING ON THE WALL?

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Given the past six years of undeniably pro-arbitration United States Supreme Court jurisprudence, does there remain any basis for a state court to place limits on the enforceability of arbitration clauses? The California Supreme Court still thinks so. In *McGill v. Citibank*, 2 Cal.5th 945, 2017 Cal. LEXIS 2551 (2017), the Court recently held that an arbitration clause was invalid — but only after assuring its readers (possibly including a certain, recently confirmed U.S. Supreme Court Justice) that the case is not really about the enforceability of arbitration clauses in the first place. Instead, the Court explained that *McGill* concerns whether a customer can waive a statutory right primarily intended to benefit the general public — a question that should produce the same answer *regardless of whether an arbitration clause is involved*.

In *McGill*, the Plaintiff purchased a "Credit Protector Plan" ("Plan") in connection with her credit card account with Defendant Citibank. Originally, the Plan did not contain an arbitration provision; however, in October 2001, Citibank sent a notice of change in terms which amended the Plan agreement to include an arbitration provision. The Plaintiff did not take advantage of the option to decline the arbitration provision. In 2005, Citibank sent another notice of change in terms informing the Plaintiff of changes in the arbitration provision. Again, the Plaintiff did not take advantage of the opportunity to opt out of the arbitration provision. Subsequently, in 2008, the Plaintiff lost her job and made a claim under the Plan. In 2011, she filed a class action against Citibank asserting claims under California's Legal Remedies Act ("CLRA"), Cal. Civ. Code §§ 1750 *et seq.*, California's unfair competition law ("UCL"), Bus. & Prof. Code §§ 17200 *et seq.*, and California's false advertising law, Bus. & Prof. Code §§ 17500 *et seq.*, arising out of Citibank's marketing of the Plan and handling of her claim under the Plan.

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The arbitration provisions subjected all claims relating to the credit card account to arbitration and barred the arbitrator from awarding relief for or against any nonparty. *McGill, supra.* It was undisputed that the arbitration provisions precluded McGill from seeking public injunctive relief — not only in arbitration, but also "in court, or *in any forum*." *Id*. at 956 (emphasis in original). Therefore, enforcing the arbitration clause as written would preclude the Plaintiff from pursuing a key part of the relief she sought: an injunction prohibiting Citibank from continuing to engage in its allegedly illegal and deceptive practices. *Id.* Citibank argued that a court could not avoid the Federal Arbitration Act ("FAA") by applying state law rules of contract interpretation to limit the scope of the parties' arbitration agreement.

It was undisputed that the arbitration provisions precluded McGill from seeking public injunctive relief — not only in arbitration, but also "in court, or in any forum."

The Court held the arbitration provision was invalid and unenforceable because McGill was effectively giving away something that was not hers to give away -- namely, the statutory right to sue for *public* injunctive relief (*i.e*., "injunctive relief that has the primary purpose and effect of prohibiting unlawful acts that threaten future injury to the general public") under three California consumer protection laws (the CLRA, the UCL, and California's false advertising law). In fact, the California Civil Code expressly disallows the waiver of rights that are established "for public reason" and the case law interpreting that Code provision makes such a waiver a ground for revoking a contract. *Id*. at 961; *see also* Cal. Civ. Code, §3513 ("Any one may waive the advantage of a law intended solely for his benefit. But a law established for a public reason cannot be contravened by a private agreement.").

But hasn't it already been settled that state laws that contradict the FAA are simply preempted by the FAA? It is clear that, under the FAA, arbitration clauses generally must be enforced as written — and the United States Supreme Court has consistently upheld their enforceability, even where plaintiffs forfeit class procedure protections and even where the arbitration system destroys plaintiffs' realistic chances of obtaining a cost-effective recovery. *See AT&T Mobility LLC v. Concepcion,* 563 U.S.333, 131 S.Ct. 1740, 179 L.Ed2d 742 (2011) and *American Express Co. v. Italian Colors Rest.,* 133 S.Ct.2304, 186 L.Ed.2d 417 (2013), respectively. After all, "[a]rbitration is a matter of contract" and, by enacting the FAA, Congress clearly manifested its intent to protect a consumer's right to freely enter into arbitration contracts with the expectation that they will be enforced as written. As a result, state laws that aim to protect consumers from agreeing to potentially unfavorable arbitration systems are generally preempted by the FAA.

Even though the parties in *McGill* had freely entered into an arbitration agreement and even though the problematic waiver happened to be wrapped up inside the arbitration provisions, the general requirement to enforce arbitration clauses under the FAA was not enough to shield the waiver from the scrutiny of the California Supreme Court. Again, the Court held the arbitration provisions to be invalid, at least insofar as it purported to waive McGill's statutory right to seek public injunctive relief *in any forum*. *Id.* at 961. The Court reasoned that this principle — that a generally unenforceable contract provision will not be enforced in an arbitration agreement — has always been a part of the statutory scheme, beginning with the text of the FAA and running throughout the U.S. Supreme Court's FAA jurisprudence, including the pro-arbitration opinions of the last six years. *Id.*

The California court's (or any court's) attempt to circumvent the clear language of an arbitration clause becomes more tenuous when reviewing the U.S. Supreme Court's FAA developments over the last six years:

- First, the final phrase of Section 2 of the FAA, known as the "saving clause," requires arbitration clauses to be enforced as written — save "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C.S. § 2. This exception plainly contemplates that some arbitration clauses are unenforceable, but it is unclear from the statutory text exactly when the exception will apply.

- Next, in *Concepcion*, *supra.*, the U.S. Supreme Court elaborated and explained that even contract defenses otherwise fitting within the bounds of the "saving clause" could be preempted if these defenses stand as an obstacle to the accomplishment of the FAA's objectives. *Concepcion*, 563 U.S. 333, 343 (2011). After all, the FAA would not make much sense if it included an exception inconsistent with and undoing the FAA's primary purpose of insuring the enforcement of arbitration agreements pursuant to their terms to facilitate streamlined proceedings. In *Concepcion*, the plaintiff opposed arbitration, contending that the parties' arbitration agreement was unconscionable because it disallowed classwide proceedings. The U.S. Supreme Court held that while the FAA's "saving clause" permits arbitration agreements

to be invalidated by generally applicable contract defenses, a blanket state-court rule invalidating class arbitration waivers in consumer contracts of adhesion as unconscionable would stand as an obstacle to the FAA's objectives. *Id.* at 348-52. Requiring costly and complex class action procedures in arbitration would negate the informality and efficiency that Congress intended to promote in the FAA. *Id.* The Court held, therefore, that the rule invalidating class arbitration waivers was preempted by the FAA. *Id*. After *Concepcion*, the logical possibility remained that a "saving clause"-type contract defense that did not frustrate the purposes of the FAA could, in a different case, be used to invalidate an arbitration clause.

In *McGill,* the California Supreme Court pulled these threads together to conclude that McGill's situation is exactly the sort anticipated by the FAA's saving clause, *Concepcion, Italian Colors*, and other similar cases.

- Then, in *Italian Colors*, the plaintiffs sought to invalidate a contractual waiver of class arbitration on the ground that the cost of individually arbitrating an antitrust claim exceeded the potential recovery. *American Exp. Co. v. Italian Colors Rest*., 133 S. Ct. 2304, 2306 (2013). The Court drew a distinction between contractual provisions that *eliminate* a party's right to pursue a statutory remedy (which could be legitimate grounds under the "saving clause" to find an arbitration clause unenforceable) and contractual provisions that simply make it "not worth the expense involved in *proving* a statutory remedy" (which are never grounds for invalidating an arbitration clause). *Id.* at 2311; *see also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc*., 473 U.S. 614, 637 (1985)). The Court held that barring the application of class action waivers to antitrust litigation fell in the latter category, and was therefore preempted by the FAA. Yet by taking the time to spell out this distinction, the U.S. Supreme Court again preserved the possibility that an arbitration clause could be unenforceable under a generally applicable contract defense - specifically, one that completely eliminates a plaintiff's right to pursue a statutory remedy.
- In *McGill*, the California Supreme Court pulled these threads together to conclude that McGill's situation is exactly the sort anticipated by the FAA's saving clause, *Concepcion*, *Italian Colors*, and other similar cases. The arbitration clause in Citibank's contract waived an unwaivable right — without regard to forum.

  Therefore, McGill's contract defense (that a waiver of an unwaivable right to seek public injunctive relief under California's CLRA, UCL or false advertising law is unenforceable) was generally applicable, as opposed to targeting arbitration in a manner incompatible with the purposes of the FAA. This comported with *Concepcion's* vision of the saving clause's function.

  Likewise, the contract defense in *McGill* was being asserted in order to protect against the *actual elimination* of a statutory remedy (not the mere procedural path to vindicating the statutory claims, as the U.S. Supreme Court suggested would be proper in *Italian Colors.* Therefore, the Court stated that finding the arbitration clause unenforceable did not modify the FAA, but actually "*implements* the FAA *as written*." *McGill* at 964 (emphasis in original).

Given the steady stream of recent U.S. Supreme Court cases interpreting the FAA it would not be surprising if the Court elects to weigh in on the *McGill* case in the near future. *See, e.g.*, *AT&T Mobility v. Concepcion*, *supra.; American Exp. Co. v. Italian Colors Rest*., *supra*; *DIRECTV Inc. v. Imburgia,* 136 S.Ct. 463, 193 L.Ed.2d 365 (2015). If the case is granted *certiorari*, it will be particularly instructive to observe how Justice Gorsuch impacts the decision. Both *Concepcion* and *Italian Colors* were authored by Justice Scalia, and both were decisions with five justices in the majority. Gorsuch's writings as a judge for the U.S. Court of Appeals for the 10th Circuit are certainly consistent with a continuation of *Concepcion* and its progeny—but then, as an Appellate Court judge, Gorsuch was bound to follow the holdings of the U.S. Supreme Court, which unambiguously lay down precedent in favor of the FAA preempting contradictory state laws.

On May 15, 2017, mere weeks after the California Supreme Court's *McGill* decision, the U.S. Supreme Court issued yet another opinion striking down a state court's attempt to circumvent the FAA. S*ee Kindred Nursing Ctrs. Ltd. P'ship v. Clark*, 197 L.Ed.2d 806, 811(2017) (The U.S. Supreme Court held that the Kentucky Supreme Court's "clear-statement" rule, under which "…a power of attorney could not entitle a representative to enter into an arbitration agreement without *specifically* saying so," violates the FAA by singling out arbitration agreements for disfavored treatment). The 7-1 opinion reinforced the Court's hard stance against state court attempts to "covertly" disfavor arbitration agreements, but it revealed nothing new about Justice Gorsuch, who did not take part in consideration or the decision of the case. With arbitration, as with many other controversial subjects, we will have to wait to see whether Justice Gorsuch follows in his predecessor's footsteps or forges a new course.

Even setting aside the Gorsuch-variable, it is unclear which way the Court would rule in this case, notwithstanding the recent streak of pro-arbitration opinions. On the one hand, the Court has repeatedly expressed a readiness to enforce all manner of arbitration clauses under the FAA, and it is not hard to imagine a straightforward extension of *Concepcion* -- perhaps requiring an arbitrator to consider claims for public injunctions (or else forcing such claims out into separate proceedings) introduces the sort of inefficient and costly formalities that thwart the FAA's basic purposes. On the other hand, the reasoning offered up by the California Supreme Court (*i.e.*, this case is not even about arbitration because this particular waiver applied regardless of forum) provides the Court with one option to affirm the enforceability of arbitration clauses generally, while reiterating the message that the FAA's saving clause can only be applied in the rarest of situations.