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Richard M. Alderman
University of Houston Law Center
Krost Hall #210
4604 Calhoun Rd.
Houston, TX 77204-6060
or
alderman@uh.edu

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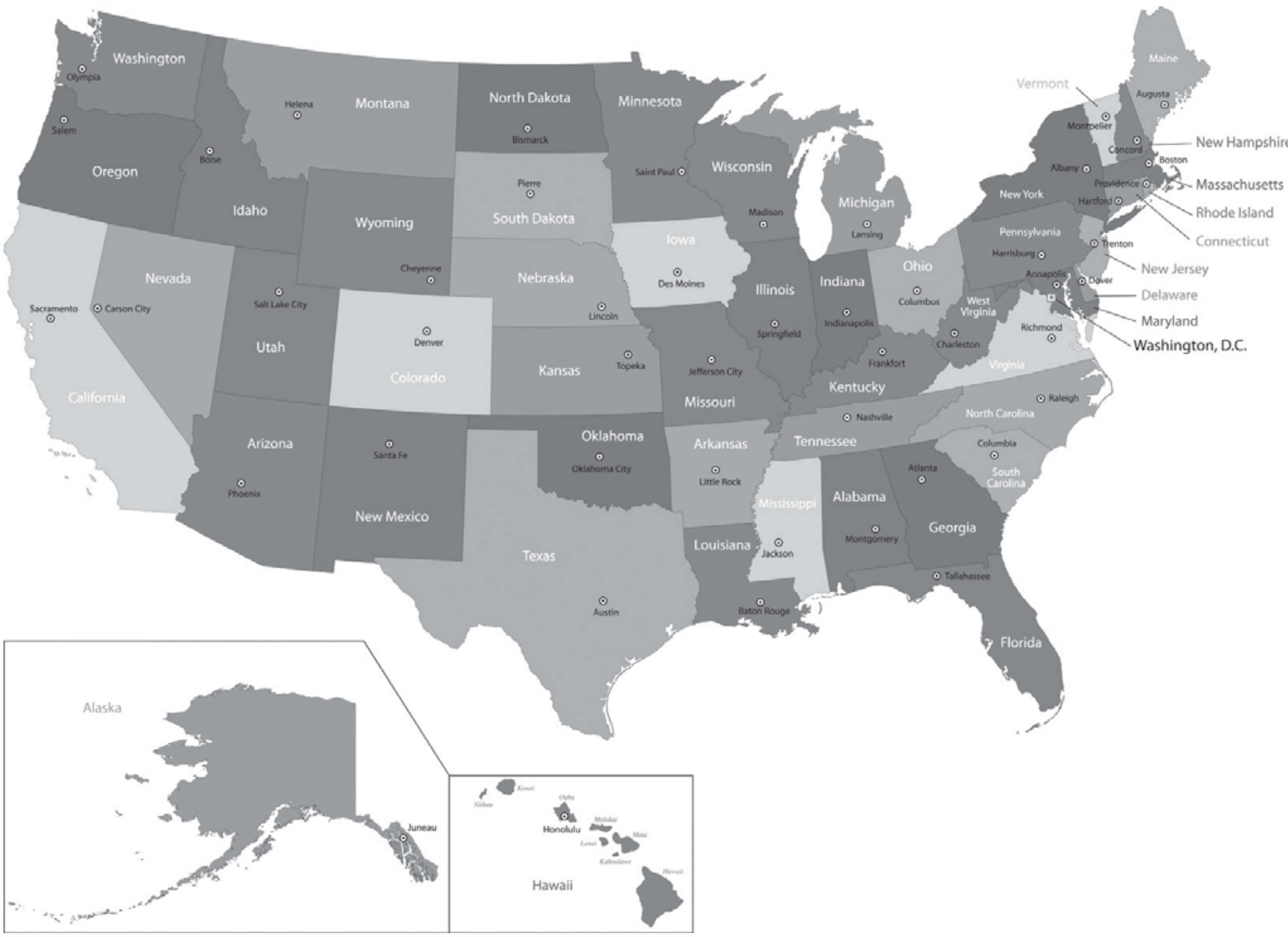

Protecting Consumers, Employees, and States from the Harms of Forced Arbitration through State-Level Reforms

by David Seligman*

INTRODUCTION

Much attention is now being paid to the expanded use of forced arbitration clauses in employment and consumer contracts, the attendant harms to consumers and employees, and the possibility of federal intervention.[1] Recent media attention has highlighted the harms that arbitration inflicts on Americans every single day.[2] And a flurry of federal activity (both congressional and regulatory) has sought to chip away at many of these harms.[3]

Perhaps because of a concern that their efforts would be preempted by federal law, however, states have not yet fully examined the tools available to them to minimize forced arbitration's harms and to protect consumers and employees from some of the harmful effects of forced arbitration that are not shielded by federal law as it currently stands.

This introduction explains the harmful effects of "forced arbitration" clauses in employment and consumer contracts, not just for a state's residents, but also for the state's own interests in state law enforcement and in the efficient procurement of goods and services. The introduction also details eight areas where state legislation is *not* preempted by the Federal Arbitration Act, and where states can address some of these harms *now*.

The Model State Consumer and Employee Justice Enforcement Act provides model statutory language to implement these eight possible state interventions. Titles I and II of the model act seek to protect the state's interests both in enforcing laws consumer and employment laws and in ensuring efficient contracting and procurement. Titles III through VIII seek to protect employees' and consumers' access to justice without running afoul of federal law. This article presents each title of the Act, complete with notes and analysis. The complete Act, without notes or analysis, may be found in the **Appendix**.

I) Background: The Harms of "Forced Arbitration" & Federal Attention to the Issue

A) Forced Arbitration and its Harms

"Forced arbitration" clauses are fine-print terms included in contracts of adhesion—often contracts between an employee and her employer or a consumer and a merchant—that, in the case of consumer and employment contracts in non-unionized workplaces, require the consumer or employee to give up her constitutional right to assert claims against the merchant or employer in court as a condition of obtaining or keeping her job or using the consumer good or service.[4] These clauses are prevalent in a number of types of contracts including, among others, cellphone contracts, credit agreements, auto loans, school enrollment forms, nursing home contracts, and employment contracts in non-union workplaces.

These clauses purport to provide employees and consumers with a private forum to resolve their claims against the company instead of the public forum—whether judicial or administrative—that is generally available for such claims. But in actuality many consumers and employees are never able to access this alternative, private forum. As explained further below, most forced arbitration clauses require the employee or consumer to pursue her claims individually, without the benefit of class or collective action procedures that many consumers and employees rely on to assert their rights. Moreover, some clauses require the consumer or employee to pay exorbitant arbitration fees or even to arbitrate in a far-off forum. And, finally, some businesses are now adept at manipulating the procedures of the arbitration provider to prolong the duration of the arbitration.[5]

Even when the employee or consumer is able to pursue her claims in arbitration, she often finds that the deck is stacked against her. The arbitration process is secret, and arbitrators are often subject to "repeat player" bias in favor of the business and against the employee or consumer—the business, after all, is the entity appearing in front of the arbitrator most frequently and is the one paying the arbitrator's salary.[6] What is more, under federal law, the right to appeal an arbitrator's decision is extremely limited. A consumer or employee cannot obtain relief on an appeal from an arbitrator's decision even when the arbitrator is clearly wrong on the facts or the law.[7]

For the most part, businesses are allowed to write their contracts this way because of the Supreme Court's recent interpretations of the Federal Arbitration Act (FAA),[8] a law that has been on the books since the 1920s. Although Congress's purpose in enacting the FAA was to allow companies, bargaining at arms-length, to settle on an alternative dispute resolution forum, a series of recent Supreme Court decisions has expanded the Act's reach to cover almost all employment and consumer contracts, whether or not the parties actually bargained over the term.[9]

B) Federal Action

In recognition of the harms caused by forced arbitration, the federal government has taken a number of positive steps to address the issue. The extent of these steps reflects a growing consensus that forced arbitration is often unfair, but these measures nonetheless fall far short of fully protecting all consumers and employees:

- The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") prohibits the use of forced arbitration clauses in mortgage loan and manufactured home loan agreements;[10]
- The Military Lending Act prohibits arbitration in certain forms of credit (as defined by Department of Defense regulations) extended to military service members and dependents, and the Department of Defense has recently extended the forms of covered credit to include most unsecured credit;[11]
- The Federal Trade Commission recently has reaffirmed its position that binding arbitration agreements do not apply to disputes related to written warranties;[12]
- The Department of Health and Human Services proposed severe restrictions on long-term care facilities' use of arbitration agreements, including prohibiting these facilities from making assent to such an agreement a condition of entering a long-term care facility.[13]
- President Obama in 2014 signed the Fair Pay and Safe Workplaces Executive Order,[14] which prohibits pre-dispute, binding arbitration agreements covering discrimination, assault, and sexual harassment claims in contracts between large federal contractors and their employees.

Perhaps the most notable federal enactment addressing forced arbitration, however, is the Dodd-Frank Act's express authorization that the Consumer Financial Protection Bureau (CFPB) may—after first conducting a study on the issue—promulgate regulations prohibiting or limiting arbitration agreements involving consumer financial products.[15]

In March 2015, the CFPB published the final results of its study, which includes a thorough, empirical analysis stretching over 700 pages. The report details many of the harms that forced arbitration clauses cause consumers of financial products, noting in particular that forced arbitration prevents many consumers from ever being able to assert claims or obtain redress arising from corporate wrongdoing.[16]

On October 7, 2015, the CFPB released an "Outline of Proposals under Consideration and Other Proposals Considered" in preparation for the convening of a Small Business Advisory Review Panel that must precede the publishing of the Bureau's rule on forced arbitration.[17] The proposal, while significant, would not end the practice of forced arbitration in consumer financial product agreements. First, the CFPB is considering a proposal that would require many covered entities to explicitly state in their arbitration agreements that the arbitration agreements are inapplicable to class actions filed in court unless and until class certification is denied or the class claims are dismissed.[18] The CFPB has analogized this rule to the Financial Industry Regulatory Authority's (FINRA) similar requirements with respect to arbitration agreements adopted by broker-dealers.[19] Second, the CFPB is poised to propose that covered entities submit initial claim filings and written awards in consumer finance arbitration proceedings to the CFPB.[20]

II) Need for State Action

A) Why Federal Actions Do Not Solve the Problem

Forced arbitration of consumer and employment disputes is a scourge on the American justice system that calls for action at every level of government. Moreover, despite these recent and important federal actions, there is a continuing need for state action concerning forced arbitration.

First, most of these recent federal enactments cover only certain kinds of contracts. The Fair Pay and Safe Workplaces Executive Order only applies to a limited number of employee claims, and then only in cases brought against large government contractors. The Department of Defense regulation only covers certain credit agreements with military personnel. And the Health and Human Services rulemaking will only affect some long-term care facilities.

The CFPB rulemaking will have the broadest reach, but will still only address arbitration in consumer financial product agreements, and will not apply to most automobile sales[21] or many other sales transactions.[22] Moreover, at least as of now, the CFPB does not appear ready to prohibit or otherwise regulate forced arbitration of *individual* disputes. The Dodd-Frank Act also specifies that any CFPB arbitration rule will only apply to arbitration agreements entered into more than 180 days after the CFPB rule's effective date.[23] This means that the CFPB rule will likely not apply to the millions of arbitration agreements in existence at the time the rule is enacted, and there is still no clear timetable as to when that will likely occur.

Thus states should see recent federal attention to the issue as a call to action. While federal regulators consider the problem, states should act quickly to do their part too. Forced arbitration harms not only consumers and employees but also the states themselves, and states have the authority to protect against these harms to state interests, notwithstanding federal law. Additionally, federal law, even as it is currently interpreted, leaves considerably more room for states to protect consumers and employees than many states may have realized.

B) How Forced Arbitration Harms States

1) Forced Arbitration Undermines Enforcement of State Laws

On November 19, 2014, sixteen state attorneys general submitted a joint letter to the Consumer Financial Protection Bureau (CFPB) urging the CFPB to exercise its statutory authority to regulate the use of forced arbitration clauses in consumer agreements for financial products and services. The letter recognized that unfair forced arbitration clauses not only create problems for individual consumers, but that the pervasiveness of these clauses results in a "systematic failure to hold accountable those companies that abuse the trust placed in them by consumers."[24] In other words, forced arbitration has harmful ripple effects throughout the entire marketplace because enforcement officials like these state attorneys general cannot, on their own, protect consumers from abusive practices.

Public enforcement agencies suffer from at least three systematic limitations that inhibit their capability to enforce the law adequately: (1) limited resources, (2) "informational disadvantages" that make it difficult for them to discover wrongdoing, even when it is apparent to its victims, and (3) the possibility of "capture" by wealthy and powerful interests.[25] To fill the enforcement void, the American legal system—at both the federal and state level—explicitly encourages private civil litigation.[26] Every state in the country provides consumers with a private cause of action under its unfair and deceptive practices law, and the vast majority allow for the full recovery of actual damages and litigation costs and attorney fees, with the aim of deterring wrongful conduct and encouraging private enforcement.[27]

Relying on private causes of action and fee-shifting provisions, private enforcement has historically played a critical role in helping to police the marketplace. In the employment context, for example, commentators writing before the proliferation of arbitration clauses and class and collective action bans reported that private enforcement actions recovered approximately $1 billion per year in lost wages for victims of wage-and-hour violations.[28]

In many ways the need for private enforcement of state protections has only increased in recent years. Economic pressures on state budgets have shrunk state public enforcement capacity. At the same time the pervasiveness and sophistication of wrongdoing has exacerbated the "informational" divide between public enforcement officers and employees and consumers. For example, "wage theft"—the practice of failing to pay workers for wages owed to them—has become increasingly prevalent, yet it is often difficult to detect by public enforcement officers who may not, for example, recognize that employees are being asked to work "off the clock."[29]

The CFPB's study also highlights the importance of private civil litigation in enforcing the law. Section 9 of the study discusses the "relationship between public enforcement and consumer financial class actions." One finding sticks out: In cases where the CFPB found "overlapping" enforcement activity by "government entities and private class action lawyers"— which would occur in the relatively rare instances where corporate wrongdoing involving a consumer financial product or service was not shielded by an arbitration clause and class waiver — "public enforcement activity was *preceded* by private activity seventy-one percent of the time."[30]

States have never needed private enforcement more. And yet the proliferation of forced arbitration has dramatically undermined state laws encouraging private enforcement. On its face, arbitration would not seem to bear on a consumer's or worker's ability to enforce state law, but merely to alter the forum in which such laws are enforced. According to the Supreme Court, after all, the Federal Arbitration Act embodies nothing more than a federal interest in encouraging alternative dispute resolution mechanisms that are "efficient and speedy."[31] In practice, however, forced arbitration prevents most consumers and employees from bringing private enforcement actions against their employers and merchants in any forum.

As explained above, recent data highlights the extent of the "claim suppression" consequences of forced arbitration. The CFPB concluded that from 2010 to 2012 consumers of credit cards, checking accounts/debit cards, payday loans, prepaid cards, private student loans, and auto loans filed, on average, only 411 cases with the American Arbitration Association per year—this figure notwithstanding the prevalence of arbitration clauses in consumer financial agreements governing these contracts and the number of consumers using these products.[32] The preliminary results of the CFPB's study noted that "[p]lainly, the number of arbitrations [during the 2010 to 2012 period] was low relative to the total populations using these products."[33]

The dearth of consumer claims arises in part from the pervasiveness of "class action waivers" that prevent consumers and employees from aggregating claims. According to the CFPB's report, over ninety percent of arbitration clauses in contracts for most kinds of financial services include class waivers.[34] Since 2011, when the Supreme Court endorsed the enforceability of these provisions, class action waivers have effectively squelched hundreds of viable consumer and employment class actions—often in cases that are impossible or very difficult to bring on an individual basis.[35]

Class action waivers suppress claims—and thus interfere with public enforcement of important state laws—in a number of ways. First, they interfere with consumers' and employees' ability to seek redress for "small dollar" claims, even when the consumer or employee knows she has been wronged. According to the CFPB report, a survey of credit card consumers revealed that just over two percent of credit card consumers would consider seeking legal redress against a credit card company for a wrongful fee. The majority of consumers responded that they would instead simply cancel their credit card.[36] In the aggregate, the failure to seek private redress for these wrongs dramatically undermines the effective enforcement of state law.

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Second, the possibility of class or collective litigation is important in cases where not all consumers or employees understand that their rights have been violated, or where they might be intimidated or lack the initiative to come forward on their own.[37] Class actions allow a few named plaintiffs to represent a broader group of consumers or employees who do not know that they have been harmed or who want to remain anonymous.

Finally, arbitration agreements frequently make individual arbitration more burdensome and costly than filing in court—thus suppressing individual claims as well—by, among other things, requiring consumers or employees to pay thousands of dollars in arbitration costs, prohibiting the award of remedies that would otherwise be available, dramatically limiting discovery, requiring consumers or employees to arbitrate in far-off forums, and shortening the statutes of limitation applicable to consumer and employment claims. Although these features of arbitration clauses may, in some cases, render the clauses in which they appear unconscionable and unenforceable, many consumers and employees never have an opportunity to challenge these clauses in court because these unfair provisions deter consumers and employees from bringing claims. And, even when consumers or employees do file claims, many of the most unfair arbitration agreements "delegate" the question of enforceability to an arbitrator, preventing consumers and employees from accessing a judicial forum to establish that the arbitration agreement is unconscionable.[38]

Even arbitration agreements that appear fair by requiring the business to bear the costs of arbitration suppress individual consumer and employment claims. Increasingly, businesses require their consumers and employees to arbitrate disputes but then refuse to pay the arbitration costs, putting the consumer or employee in the difficult position of having to front the business's costs or convince a court to hear her claims notwithstanding the arbitration agreement.[39]

States are unlikely to be able to offset the reduction in private enforcement caused by these trends by increasing their budgets for public enforcement. One response to this problem is to allow private attorneys general to assist in the enforcement of state law. This approach would fill the gap caused by the reduction in private litigation, because such actions on behalf of the state are not subject to arbitration agreements. Model language for such an approach is set out in the Model State Consumer and Employee Justice Enforcement Act, Title I.

2) The Secrecy of Forced Arbitration Proceedings Hinders State Procurement and Contracting

The secret nature of forced arbitration obscures essential information on which states rely in making informed and efficient decisions about the procurement of goods and services and in overseeing private contractors after entering into a contractual relationship. Arbitration clauses exacerbate the difficulties states might ordinarily have gathering information about potential recipients of state funds.

Many arbitration clauses contain "confidentiality provisions" expressly prohibiting the parties from disclosing information about cases brought through arbitration.[40] Even when the clause does not prohibit the parties from publicizing their case, the public (including states) rarely finds out about arbitration awards or claims in arbitration because, unlike judicial decisions and publicly filed complaints, arbitration filings are generally not provided in a publicly accessible database.

During the initial stages of the public contracting process, public agencies usually rely on open bidding processes to select government contractors. Although public bidding may help the government identify the costs of a contract, it will not, on its own, reveal whether a potential contractor is involved in legal disputes with consumers or employees. The government will have difficulty identifying whether the contractor provides the services it claims to provide unless the contractor or other business resolves its disputes with consumers and employees publicly.

For example, consider a for-profit college that receives state funds to train state employees on the use of software used by various state agencies. Without having the opportunity to review claims brought against the school by former students alleging that they did not receive the promised education, the state will not be able to effectively evaluate whether the services provided by the school merit the state selecting that school to train its employees. In other words, transparent dispute resolution is critical to evaluating the quality of the goods or services offered by a business before entering into a contractual relationship.

The state's interest in transparent dispute resolution among its contractors does not end, however, at the time the state enters into a contract. Transparent dispute resolution during the course of the contract's performance helps the state evaluate whether the contractor is effectively performing its obligations.

Without being able to examine employee and consumer claims against the contractor, the state might have difficulty determining whether the contractor is breaching its contractual obligations, which would justify termination of the contract. For example, if a state is paying a contractor to provide meals to low-income consumers, the state might learn that those meals are tainted only if one of the meal's recipients is able to bring suit in a public forum.

Additionally, transparent resolution of consumer and employment disputes prevents the contractor from concealing chronic problems that might interfere with the quality of the goods or services provided to the state, even if the contractor does not breach the contract. A recent scandal involving sexual harassment problems at the clothing manufacturer and retail store American Apparel illustrates the problem.

For decades, American Apparel's chief executive officer had been the subject of sexual harassment claims and accusations on the part of employees, but he remained in control of the company until 2014. An article in *The New York Times* noted that forced arbitration clauses in employment contracts had helped to insulate his practices from public scrutiny and thus injured shareholders and customers. "If American Apparel hadn't been able to use arbitration and confidentiality clauses to keep investors and the public in the dark over those accusations, [the CEO] would most likely have been shown the exit some years earlier."[41] As *The Times* further explained, "A board can use [arbitration clauses] to hide a pattern of bad conduct. Either employees will be deterred from bringing claims or, if they do, the claims will be buried in the silence of arbitration."[42]

A large government contractor could similarly use arbitration clauses to conceal pervasive and chronic wrongdoing and harm the state's financial interests in any number of ways during the performance of the contract. For example, as in the situation with American Apparel, a contractor might use forced arbitration clauses in employment contracts to conceal and insulate from public scrutiny ongoing legal violations, which, when allowed to persist outside the public eye, interfere with the quality of the goods and services provided. Alternatively, a large contractor might be able to conceal consumer claims brought in arbitration that allege illegal charges to individual consumers. Without being able to track these claims, the state might not identify ways in which it too is illegally overcharged by government contractors, perhaps in violation of the contract.

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To the extent that the state—acting as a market participant and not as a regulator—determines that companies utilizing arbitration clauses in employment or consumer contracts adversely affect the state's procurement activities, the state can choose not to contract with those companies. Model language for such an approach is set out in the Model State Consumer and Employee Justice Enforcement Act, Title II, which allows states to use their "market participant" powers to ensure that their contractors resolve consumer and employment disputes transparently.

C) Forced Arbitration's Other Harmful Effects That Call for State Action

Forced arbitration has a number of other harmful effects on consumers and workers. Many of these aspects of forced arbitration are entirely unrelated to federal law regarding arbitration, and therefore are susceptible to state intervention. The following list sets out a number of these problems and the corresponding title in the model act that is designed to address the harm without conflicting with federal law.

Notwithstanding the number of rights that forced arbitration agreements often require consumers and employees to waive, these terms are often buried in long form contracts or employment manuals that consumers and workers rarely have the time to read and understand. *See* Title III, *infra.*

The Federal Arbitration Act purports to protect arbitration as an alternative dispute resolution mechanism that is faster and cheaper than litigation in court. In practice, however, many arbitration clauses contain unfair terms that are entirely inconsistent with even the most arbitration-friendly understandings of federal law, including terms that require consumers and employees to waive important rights and remedies, to arbitrate in a far-off venue, or to pay extraordinary arbitration fees. *See* Title IV, *infra*.

Express and implied limitations on the scope of the Federal Arbitration Act provide states with fairly broad authority to prohibit arbitration contracts in certain contexts, including in employment contracts for transportation workers and any contract for insurance. Additionally, state law governs when the contract containing the arbitration clause does not affect interstate commerce or when the parties agree that state law governs. Too often, states fail to utilize this authority. *See* Title V, *infra*.

Private arbitrations are administered by private organizations that have been susceptible to bias in the past and that tend to administer disputes opaquely. *See* Title VI, *infra*.

Disputes regarding arbitration prolong litigation and often make it difficult for employees and consumers to have their day in court even when a judge determines that they are *not* bound to arbitrate their dispute. *See* Title VII, *infra*.

Even when consumers or employees do bring claims in arbitration, they often face difficulty having their case heard by an arbitrator. When the arbitral forum requires the employer or business to pay the arbitration fees, the employer or business can stall the arbitration process by refusing to make a payment. In theory, arbitrators should formally refuse to administer the arbitration, making the forum unavailable and allowing the consumer or employee to pursue her claims in court. In practice, however, it is often difficult and time consuming to obtain this result. *See* Title VIII, *infra*.

III) Overview of Federal Preemption

Notwithstanding the ways in which arbitration of consumer and employment disputes harms states, consumers, and employees, little state legislation has been enacted to address these problems. In large part, this is because of a fear that the Federal Arbitration Act (FAA) preempts any state law that limits forced arbitration. Although federal law does protect arbitration agreements from some state laws that might otherwise limit their enforceability, this Model Act provides a number of possible avenues for state action that do not conflict with or obstruct federal law.

The FAA provides that a written agreement to settle a dispute by arbitration "shall be valid, irrevocable, and enforceable, save upon such grounds that exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. In a number of contexts, courts have stated that this language embodies a "liberal federal policy favoring arbitration."[43] At the same time, however, the Act's express language preserves general state contract rules and other rules that do not conflict with that policy. The challenge for states is identifying measures that protect states themselves, along with the state's consumers, and employees from forced arbitration's harmful effects without conflicting with the FAA's purposes.

The United States Supreme Court's FAA preemption jurisprudence, culminating in its 2011 decision in *AT&T Mobility L.L.C. v. Concepcion*,[44] suggests that there are two ways in which a state law or rule of decision can be preempted by the Federal Arbitration Act.

First, a state rule is clearly preempted if it singles out arbitration clauses for disfavor relative to other contractual terms or singles out private dispute resolution for disfavor relative to judicial or administrative dispute resolution.[45] Rules requiring that certain kinds of disputes or claims be resolved through litigation as opposed to arbitration and rules requiring that arbitration clauses take a particular form fall into this category.[46]

Second, the FAA preempts state rules of decision that interfere with the "fundamental attributes of arbitration." According to the Court, the FAA "encourage[s] efficient and speedy dispute resolution."[47] The aspects of arbitration that facilitate this idealized notion of arbitration are "fundamental" to arbitration, and rules that interfere with these fundamental attributes are preempted. For example, in *Concepcion*, the Court held that a California rule prohibiting some arbitration clauses which required that disputes be arbitrated only on an individual, not classwide, basis was preempted because bilateral dispute resolution is *fundamental* to arbitration.[48]

Mindful of these constraints, the proposals that follow provide states with opportunities to protect themselves from the harms of forced arbitration without interfering with private parties' right, embodied in the FAA, to enter into agreements to resolve disputes efficiently and expeditiously. These proposals are guided by the following principles, some specific to FAA preemption but others relating to states' powers more generally:

- **Although the FAA preempts some state laws regulating private agreements to arbitrate, it cannot prevent states from using their public enforcement and procurement powers to protect their own financial and enforcement interests.** One of a state's primary responsibilities is regulating private businesses and entities, but this is not the state's sole function. In addition to being a regulator, the state is also an enforcer of state laws and a large consumer of and investor in goods and services in the private marketplace. In these latter arenas, the state is considerably less encumbered by federal law from mitigating the harms of forced arbitration to state interests. *See* Title I & Title II, *infra*.
- **The FAA leaves considerably more leeway for state action addressing the *formation* of arbitration agreements than the *enforcement* of arbitration agreements.** As the Supreme Court made clear in *Concepcion*, one of the FAA's primary goals is the enforcement of arbitration clauses pursuant to the parties' private, consensual agreement. But when there is no private, consensual agreement, the FAA's presumption in favor of arbitrability does not apply. For this reason, state laws focusing on the formation of arbitration agreements are more likely to survive challenge than state laws focusing on the enforcement of arbitration agreements. *See* Title III, *infra*.
- **The FAA does not require the enforcement of arbitration clauses that are unconscionable and unfair, as long as what renders such clauses unfair is not a "fundamental" attribute of arbitration.** As explained above, the Supreme Court has held that some aspects of forced arbitration clauses, including the requirement that consumers and workers arbitrate their disputes on an individual basis, are so "fundamental" to arbitration that they are protected by the FAA and cannot be defeated by general state contract defenses. But the FAA does not protect arbitration clauses from generally applicable state-law challenges, including unconscionability, if they call for an inefficient, prolonged, or costly arbitration forum. States should act to clarify that certain terms included in some arbitration clauses are presumptively unconscionable. *See* Title IV, *infra*.
- **Federal law provides an exception to the FAA for insurance contracts and contracts regarding transportation workers, and the FAA does not apply to contracts that do not involve interstate commerce or when the parties agree that state law applies.** In these contexts, states have the authority to prohibit the formation and enforcement of forced arbitration agreements. *See* Title V, *infra*.
- **The FAA does not regulate the private companies that administer arbitrations.** Federal law may prevent states from adopting certain regulations related to the enforcement of private agreements to arbitrate, but the FAA does not prevent the states from regulating the private arbitration administrators that arbitration agreements often designate to resolve disputes. *See* Titles VI & VII, *infra*.
- **The FAA does not govern the procedures by which private parties must litigate questions about arbitration in state court.** Pursuant to black-letter principles of civil procedure, state procedural law applies to cases brought in state court, even where those cases raise issues of federal law, like the scope of the Federal Arbitration Act. *See* Title VII, *infra*.

THE NATIONAL CONSUMER LAW CENTER'S MODEL STATE CONSUMER AND EMPLOYEE JUSTICE ENFORCEMENT ACT SUMMARY:

The Model State Employee and Consumer Justice Enforcement Act includes eight separate titles that protect against different harms related to forced arbitration of consumer and employment disputes. Although they are presented as a single Act, these subparts also stand alone. Thus, states can enact any or all of the titles. A definitions section applies to terms used throughout all eight titles, and each title is followed by notes and analysis. The complete Act, without notes or analysis, may be found in the Appendix.

Definitions of Terms—The model act invites states to use their existing definitions for a number of terms that appear throughout the model act and to replace terms included in these model provisions with language that is more appropriate for the state's legislative scheme. However, the model act does define "forced arbitration agreement" and "employee." The definition of "forced arbitration agreement" is designed to cover all situations where a consumer or employee cannot meaningfully understand and assent to an arbitration agreement because it is a condition of entering into a relationship with the business or would be considered by a reasonable person to be a condition of entering into the relationship. The definition of "employee" is designed also to cover disputes where plaintiffs argue that a business has "misclassified" them as something other than an "employee."

Title I: Delegation of State Public Enforcement Authority—To preserve public resources while ensuring adequate enforcement of state worker and consumer protection laws, Title I embodies a delegation to private attorneys general of the authority to enforce these laws on behalf of the state. Consistent with age-old *qui tam* doctrine, the law allows the private attorney general to recoup an incentive award capped at a percentage of the recovery remitted to the state. The state maintains control over the litigation by preserving the state's opportunity to intervene in the action for the purposes of dismissing it with prejudice, settling it, or pursuing it on the state's own behalf.

Title II: Conditions on Persons Doing Business with the State—Pursuant to their market participant powers, states can prohibit the entities with which they do business from forming or enforcing forced arbitration clauses in employment and consumer contracts. As explained above, forced arbitration obscures information that is often essential to government contracting and procurement, and states have an interest as market participants in ensuring that the entities with which they do business do not use arbitration clauses to obscure claims that might reveal something about the quality of their products or services. Title II requires that any entity seeking to do business with the state notify its consumers and employees that it will cease enforcing forced arbitration clauses in employment and consumer contracts. Importantly, the Title covers all of the entity's employment and consumer contracts, not just those contracts directly tied to the government contract or project.

Title III: Clear Notice and Single Document Rule—For a set of contracts identified by the state, Title III requires that merchants and employers provide clear notice of all material terms in language that the consumer or employee can understand. For consumer contracts, Title III also requires that material terms be included in a single document. Such "material terms" include, among others, forced arbitration clauses.

Title IV: Unconscionable Terms in Standard Form Contracts—Title IV sets out types of contractual terms related to dispute resolution found in form contracts between an individual and the drafter of the contract that are presumptively unconscionable, including, among others, terms requiring the individual to waive substantive rights or to resolve her dispute in a far-off forum. Title IV also seeks to deter employers and merchants from inserting unconscionable terms that would chill consumer and employee claims. The Title creates a presumption that such terms are not severable from the arbitration agreement and by making the inclusion of such terms in a standard form contract an unfair and deceptive practice under state law.

Title V: Prohibition of Forced Arbitration Clauses under State Law—Title V amounts to a catch-all provision that prohibits the enforcement of forced arbitration clauses in employment and consumer contracts that are not covered by the Federal Arbitration Act, including in contracts for insurance and in employment contracts for transportation workers.

Title VI: Data Disclosure Requirements for Arbitration Providers—Title VI does not regulate private arbitration agreements but instead the private companies that administer arbitrations. It requires that these companies comply with certain data disclosure requirements. For example, arbitration administrators must disclose how many consumer and employment arbitrations are conducted during specified time periods, the arbitrator conducting the arbitration, and the award.

Title VII: Appellate Jurisdiction—Title VII removes the jurisdiction of appellate courts to consider appeals from denials of motions to compel arbitration. In this way, it ensures that employers and merchants are not able to force a plaintiff through costly and prolonged litigation regarding the applicability of an arbitration clause that a court has declined to enforce.

Title VIII: Preventing Respondents from Improperly Delaying the Arbitration Proceeding—Like Title VI, Title VIII does not regulate arbitration agreements, *per se*, but rather arbitration providers that administer a minimum number of disputes brought by consumers or employees. Title VIII provides that if a respondent in an arbitration brought by a consumer or employee fails to pay arbitration fees, the administrator must either administer the arbitration or promptly refuse to move forward with the arbitration and notify the parties in writing of that refusal.

DEFINITION OF TERMS

[*Note*: States will likely need to define other terms used throughout the Act (including, for example, "consumer"), but because many states already include such definitions in their employee and consumer protection statutes, the Model Act does not provide such definitions here. Furthermore, some terms used throughout the Act will be inappropriate for certain states' statutory schemes. As just one example, the term "civil penalties" might not be appropriate in some states that impose "fines" or "sanctions."]

Forced arbitration agreement is an agreement to subject disputes between the parties to a binding dispute resolution procedure separate from federal or state judicial or administrative process if such agreement (1) is a condition of entering into a relationship with the party that presented the agreement or is presented in such a way that a reasonable person would consider it to be a condition of entering into a relationship with the party that presented it; and (2) was not negotiated by a labor union through collective bargaining; pursuant to this definition, for a consumer and employment contract an arbitration agreement is a "condition of entering into a relationship" with a business if the business retaliates against the consumer or employee for failing to assent to the agreement or if the consumer or employee reasonably fears that the business would retaliate against the consumer or employee for failing to assent to the agreement. The right to "opt-out" of the agreement at a later time does not affect or alter the agreement's status as a "forced arbitration agreement."

Employee is, for the purpose of this Act, any person employed by another as defined by state law, and any person who is not classified by a business as an employee but who claims to be an employee and whose claims against the purported employer relate to this alleged misclassification.

Notes

Definition of forced arbitration. The definition of "forced arbitration agreement" stretches broadly to cover any agreement that a consumer or employee enters into as a condition of her relationship with a business. The definition also applies to arbitration agreements that are in actuality "forced," even when the employer or business attempts to hide that forced nature. Under this definition an arbitration agreement is "forced" if a reasonable consumer or employee would think that it is a condition of entering into the relationship. Furthermore, a business cannot remove an arbitration agreement from the ambit of this definition by including an opt-out clause.[49]

Definition of "employee." "Employee" is defined as anyone falling with the state's definition of an employee and also, for the purpose of this Act, anyone who claims that she is an "employee" but that her employer has "misclassified" her as something else—like a franchise or an independent contractor—to avoid following wage-and-hour laws. If "employee" were not defined in this manner, and instead shared the definition of "employee" used in the state's wage-and-hour protections, then a court would have been placed in the awkward position of first having to result the merits of the misclassification claim before addressing the preliminary issue as to whether the arbitration clause applied.[50]

TITLE I: DELEGATION OF STATE ENFORCEMENT AUTHORITY

Section 1. Findings.
Limits on the availability of public enforcement resources have deleterious effects on the marketplace by allowing abuses targeting consumers and workers to persist unprosecuted. To ensure the robust enforcement of [*designated State consumer and worker protection statutes*], while simultaneously minimizing the outlay of scarce State funds, this Title provides for private attorneys general to represent the State's enforcement interests in certain contexts in which the State does not have the means to enforce fully state consumer and worker protections.

Section 2. Civil penalties.
Unless State law provides a different amount as the civil penalty recoverable by the State for violations of [*designated State consumer and worker protection statutes*], a person who commits a violation of such State consumer or worker protection laws shall be subject to a civil penalty not to exceed $5,000 per violation.

Section 3. Private attorney general suits:

(a) A person may initiate on behalf of the State an action alleging violations of [*designated State consumer and worker protection statutes*] to recover civil penalties on behalf of the State and to seek injunctive, declaratory, or other equitable relief that the State would itself be entitled to seek;

(b) In initiating an action under this Title, a person may allege multiple violations that have affected different consumers or employees, as long as those violations are of a sufficiently similar kind that they can be efficiently managed in a single action;

(c) For the purpose of encouraging the enforcement of public protections, a court may award a person who initiates a claim under this Title an incentive award of up to twenty-five (25) percent of the total monetary recovery if that person pursues the action to final judgment as the prevailing party, or up to ten (10) percent of the total recovery if the state intervenes in the action and pursues it to final judgment as the prevailing party, including after settlement. In deciding an appropriate incentive award, a court shall consider the complexity of the case, the resources dedicated to prosecuting the case, whether the private attorney general obtained equitable relief on behalf of the state, and the extent of such relief, and the importance of the case as measured by the extent of actual damages caused by the wrongdoing to consumers or employees; and

(d) When a private attorney general or the State prevails in an action originally brought under this Title, the private attorney general and the State each shall be entitled to attorney fees and costs, as reasonable based on their participation in the action.

Section 4. State's opportunity to intervene and proceed with the action.
A person initiating an action under this Title shall serve a copy of the complaint and a letter describing the action on the State Attorney General, at which point the action shall be stayed for thirty (30) days. The State may intervene in the action and proceed with any and all claims in the action:

(a) As of right within the thirty-day stay; or

(b) For good cause, as determined by the court, after the expiration of the thirty-day stay.

Section 5. Discovery.
Whether or not the State proceeds with the action, upon a showing by the State that certain actions of discovery by the person initiating the action would interfere with the State's investigation or prosecution of a criminal or civil matter arising out of the same facts, the court may stay such discovery for a period of not more than 60 days. Such a showing shall be conducted *in camera*. The court may extend the 60-day period upon a further showing in camera that the State has pursued the criminal or civil investigation or proceedings with reasonable diligence and any proposed discovery in the action will interfere with the ongoing criminal or civil investigation or proceedings.

Section 6. Prohibition of duplicative actions.
No action may be brought by a private party acting pursuant to this Title for any violations already alleged as the basis for an action brought by the State, or by another private party pursuant to this Title, and no action may be brought by the State for any violations already alleged as the basis for an action brought by a private party pursuant to this Title. Furthermore, when a person initiates an action under this Title, no person other than the State may intervene or bring a related action under this Title based on the facts underlying the pending action.

Section 7. Settlement.
The court in which the action is filed shall review and approve any proposed settlement of an action brought under this Title to ensure that the settlement provisions are reasonable in light of State law. The court shall also ensure that any incentive fees and attorney fees or costs included in a settlement are reasonable and that the private attorney general does not recover, as an incentive payment, more than twenty-five (25) percent of the recovery remitted to the State under the proposed settlement. The proposed settlement shall be submitted to the State Attorney General at the same time that it is submitted to the court. If the State Attorney General opposes the settlement and expresses such opposition by filing a motion with the Court, the Court must decline approval of the settlement.

Section 8. Limitations on State actions initiated by a private party.

(a) The State may dismiss any action in which it decides to intervene under Section 4 of this Title notwithstanding the objections of the person who initiated the action.

(b) The State may settle any action in which it decides to intervene under Section 4 of this Title notwithstanding the objections of the person who initiated the action.

Section 9. Res judicata.
Notwithstanding any other provision of law, an action initiated by a private person under this Title shall not bar that person or any other individual from filing a private action based on the same nucleus of operative facts, nor shall a prior private action based on the same nucleus of operative facts bar an action under this Title.

Section 10. Relationship to forced arbitration.
Actions under this Title are prosecuted on behalf of the State and not an individual, and forced arbitration agreements between private parties do not apply to actions under this Title. No contract shall waive or limit a private party's right to act as a private attorney general under this Title by waiving that party's right to bring such an action in a public forum or by preventing the party from being able to bring an action alleging multiple violations committed against multiple consumers or employees pursuant to Section 3(b) of this Title.

Section 11. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

Notes
Section 2—Rules relating to civil penalties for violations of consumer and worker protection laws. Depending on whether preexisting law already provides for civil penalties for violating state consumer or worker protections, a state enacting Title I may not need to provide such penalties separately. States should ensure, however, that this Title expressly identifies that its purpose is to provide for public enforcement capabilities for private parties, not to provide a private cause of action to consumers and workers.

Section 3—Delegation of public enforcement powers. Some of the provisions of this Title are based on the *qui tam* provisions of the California Private Attorneys General Act, California Labor Code §§ 2698 to 2699.5 (West) ("PAGA"),[51] and some are based on the federal False Claims Act, 31 U.S.C. § 3130.

Title I includes the essential characteristics of a *qui tam* action as identified by Blackstone: (1) the prohibition of conduct as being contrary to the interests of the sovereign; (2) a penalty or forfeiture imposed for violations; (3) allowance of civil enforcement actions pursued by private parties for conduct that may not have directly affected that party; (4) provision of an incentive for private parties bringing actions under the statute; and (5) a provision binding the government to the outcome of the private parties' enforcement actions.[52]

Section 3(a)—Claims seeking injunctive or other equitable relief. Because much of the most important relief available to the state in enforcement actions brought under consumer or worker statutes is injunctive (for example, debt relief for debtors), Title I allows the state to delegate enforcement actions seeking that type of relief in addition to claims seeking monetary relief. Whether a private attorney general under this Title obtains injunctive relief for consumers or workers is one consideration a court may take into account in deciding an appropriate incentive payment, but note that obtaining injunctive relief does not increase the twenty-five (25) percent incentive payment limit in cases brought to final judgment.

Sections 3(a) & (b)—Representative actions by any member of the public. Like the federal False Claims Act, but unlike the *qui tam* provisions in California's PAGA, Title I does not require that a party bringing an action on behalf of the state be "aggrieved" by the conduct of which the public enforcement action complains. California's requirement has confused some courts and commentators who have misapprehended that PAGA's purpose is to provide a remedy to aggrieved employees instead of to enforce state law on behalf of the state.[53] Title I avoids the possibility of this confusion.

The virtue of narrowing the set of persons who can bring *qui tam* claims to aggrieved persons, however, is not that it allows injured parties to seek redress. The California law is clearly intended to allow private parties to enforce the state's right on behalf of the state. But by limiting the universe of potential relators to "aggrieved" parties, PAGA guards against the possibility of a multitude of frivolous lawsuits brought by private attorneys general from out of state or who are otherwise entirely disconnected from the alleged wrong.

While Title I does not require that the private attorney general be aggrieved, it protects against frivolous lawsuits through other means. Title I gives courts wide discretion to award incentive payments, but restricts that discretion to issues related to the complexity of the case, the outlay of resources used in prosecuting the case, and the extent of *actual* damages to consumers or workers. In this way, courts are entitled to award minimal incentive payments in uncomplicated cases involving minor violations.

Furthermore, Title I contains two other built-in checks against extensive frivolous litigation: First, if a case is truly frivolous, the State Attorney General may intervene and dismiss the case, resolving the matter quickly, and preventing the private attorney general from recovering any incentive payment. Second, under Title I, the private attorney general's recovery is capped at a percentage of the state's recovery. In this way, the private attorney general will not be able to recover unless the state recovers, and if the state recovers little, the private attorney general will also recover little.

If a state adopts Title I but limits private attorneys general to aggrieved parties, it should make it crystal clear through legislative findings and statutory language that the private attorney general is still allowed to proceed only on behalf of the state, and not on her own behalf and that the state will have the right to control the litigation completely.

Section 3(c)—Actions protecting a number of consumers or employees. In the interests of the efficient administration of justice, Title I allows private attorneys general to bring in a single action claims related to a number of different violations committed against multiple consumers or employees. Although the aggregate nature of these actions mimics some of the procedural benefits of a class action, actions brought under Title I differ from class actions in important ways. First, the private attorney general represents the interests of the state, not the interests of private individuals harmed by the consumer or worker abuses. Second, unlike class actions, which preclude members of the class from bringing individual claims for the same misconduct, claims brought under this Title do not alter the rights of the consumers or employees affected by the alleged wrongdoing to bring individual claims for the same misconduct. Because the private attorney general brings claims on behalf of the state, not to seek redress for the wrongs done to her or others, the private attorney general suit does not affect the private attorney general's or any other person's right to bring a separate private suit.[54]

Section 4—State's opportunity to intervene and proceed with the action. Because claims under this section belong to the state and are subject to the state's control, the state has the opportunity to take over the conduct of any action brought under this Title. PAGA and the federal False Claims Act similarly allow for such government action. Unlike PAGA and the False Claims Act, however, Title I allows the state an opportunity to intervene at *any* point in a private attorney general suit under this Title, even after the initial thirty-day stay as long as the state shows good cause for the delay. In this way, the state can ensure that its interests are protected during a private attorney general suit under this provision.

Section 5—Discovery. This provision is modeled on a provision of the federal False Claims Act that similarly allows the United States Government to move for stays of discovery in actions brought by relators, even where the government has declined to intervene in the action. 31 U.S.C. § 3730(c)(4). In the context of Title I—where the state may intervene at any point, upon a showing of good cause—this provision allows the state to have some control over discovery that might be harmful to the state's public enforcement interests without requiring the State to intervene in the action.

Section 6—Limitation on duplicative actions. Actions brought under this Title are public enforcement actions brought on behalf of the state with the state as the real party in interest. Therefore, a merchant or employer cannot be subject to two actions on behalf of the state seeking to enforce the same worker or consumer protection laws concerning the exact same conduct, even if one of those actions is brought under this Title and another of those actions is brought by the state in its own capacity.

Section 7—Settlement. Because claims brought under this Title are brought on behalf of the state and designed to protect the state's interests, the state has the authority to review and reject any settlement, just as the federal government has the authority to review and veto a settlement of any claim brought by a relator under the False Claims Act. 31 U.S.C. § 3730(b)(1). Importantly, this Section also caps the amount that private attorneys general can recover personally, through an incentive payment after settlement, at twenty-five (25) percent of the amount remitted to the state through the settlement. By expressly limiting settlements in this way, even when the State does not veto the settlement, Title I protects against "sweetheart" settlements through which defendants "buy off" private attorneys general who may not have an incentive to protect the State's public enforcement interests.[55]

Qui tam actions, insofar as they are brought by private parties on behalf of the state, are not covered by the private contractual relationship that often exists between employees and employers and consumers and merchants.

Section 8—State's control over the action. Because claims brought under this Title belong to the state, once the state decides to intervene in an action brought under this Title, the private person who initially filed the action immediately relinquishes all control over the litigation to the state.

Section 9—*Res judicata.* Actions brought under this Title belong to the state and preclude subsequent state enforcement efforts, whether brought by the state or a private attorney general under this Title. Conversely, actions under this Title are not duplicative of private actions related to the same issues or touching the same nucleus of operative facts. Therefore, an action brought under this Title does not have any preclusive effect on private actions addressing similar wrongdoing.

Section 10—Relation to forced arbitration. As explained below, courts have concluded that *qui tam* actions are not covered by arbitration agreements between the individual bringing the action and the defendant. In line with this precedent, Title I expressly prohibits consumers and employees from waiving their right to bring an action under this Title on behalf of the state or from waiving either their right to bring such an action in a public forum or their right to bring a *qui tam* action alleging multiple violations committed against multiple consumers or employees.

By contrast, some courts have interpreted PAGA to allow businesses and employees to "agree" that "representative" PAGA action must be brought in arbitration. *See, e.g.*, *Sakkab v. Luxottica Retail N. Am., Inc.*, 803 F.3d 425, 440 (9th Cir. 2015). This makes little sense, particularly in the context of Title I, where any party—whether or not she has a contractual relationship with the defendant—may bring an action on behalf of the state. Furthermore, allowing private contracts to dictate the forum in which these fundamentally *public* claims can be brought undermines the argument that private attorney general claims belong to the state and not to any private party.

<u>Analysis of Title I</u>

I) State Precedent for *Qui Tam* Actions to Enforce State Consumer or Worker Protections

In broad strokes, *qui tam* statutes (named for the Latin phrase "*qui tam pro domino rege quam pro se ipso in hac parte sequitur*," or "he who sues in this matter for the king as well as for himself") allow private individuals to sue to enforce essentially public rights. By far the most notable extant mechanism for *qui tam* enforcement in American law is the False Claims Act,[56] which, among other things, allows for private "whistleblower" actions brought on behalf of the government alleging that the defendant has committed fraud against the government.

California's PAGA is one example of an alternative type of *qui tam* statute. Under PAGA, an "aggrieved employee" is authorized to bring a civil action "on behalf of himself or herself and other current or former employees" to recover "civil penalties."[57] In light of the decline in "[s]taffing levels for state labor law enforcement," the legislature crafted PAGA to "deputize[ ] an aggrieved employee to sue for civil penalties . . . as an alternative to [public] enforcement."[58]

Title I begins from the premise that *qui tam* actions, insofar as they are brought by private parties on behalf of the state, are not covered by the private contractual relationship that often exists between employees and employers and consumers and merchants. This is consistent with the cases discussing the issue in the False Claims Act context.[59]

This position was endorsed by the California Supreme Court in *Iskanian v. CLS Transportation Los Angeles, L.L.C.*[60] The court concluded that "aggrieved" employees under PAGA could bring claims in court on behalf of the state asserting violations of California Labor Law notwithstanding the presence of enforceable arbitration clauses that prevented them from bringing claims in court in their own capacity.

While some California federal courts initially refused to follow *Iskanian*,[61] the *Iskanian* defendant's petition for *certiorari* in the United States Supreme Court was rejected,[62] and the Ninth Circuit recently sided with the California Supreme Court in *Sakkab* in deciding that the FAA does not preempt a rule prohibiting the waiver of private attorneys' general right to bring "representative" actions under PAGA.[63] Whether or not the Supreme Court ultimately considers this issue, Title I takes extra precautions, not found in PAGA, to ensure that it sits comfortably alongside the Federal Arbitration Act. Title I, therefore, is even less susceptible to challenge than PAGA.

First, PAGA's requirement that a party be an "aggrieved" employee in order to bring a *qui tam* action detracts somewhat from the argument that it is a true *qui tam* statute. For example, the dissent in *Sakkab* placed considerable emphasis on the ways in which the *Iskanian* rule interfered with the "parties' freedom to limit their arbitration only to those claims arising between the contracting parties," a freedom endorsed by the United States Supreme Court in *Concepcion*.[64] Title I does not limit its application only to aggrieved parties who necessarily have a contractual relationship with the defendant. Therefore, Title I does not directly implicate private agreements or private parties' right to agree to an "efficient and speedy" dispute resolution mechanism.

Second, Title I allows the state considerably more control over a private attorney general action than PAGA and even more than the federal government retains over False Claims Act actions. Like the federal government in FCA actions, the state maintains some control over discovery in private attorney general actions under Title I and can veto any settlement of a private attorney general action. Furthermore, unlike either California's powers with respect to PAGA actions or the federal government's powers with respect to FCA actions, under Title I, the state has the right to intervene in a private attorney general action at any point during the litigation, as long as the state can show good cause for its delay in intervening. After intervening, the state can dismiss the action, settle it, or prosecute it to final judgment. In this way, the state maintains substantially greater control over a private attorney general action under Title I than California maintains over a PAGA action.

Qui tam claims are not subject to private arbitration agreements because they are not private claims, and, for this same reason, state rules creating unarbitrable _qui tam_ claims are not preempted by the FAA.

II) Arbitration Clauses Do Not Bind Private Attorneys General under Title I

Because any individual can act as a private attorney general under Title I, in some cases that individual may not have agreed to mandatory arbitration, and in those cases it should be clear that dispute is not subject to an arbitration agreement. But even when an individual's private action against a defendant would be subject to an arbitration clause—because, for example, that individual is a customer or employee of the defendant—that individual's private attorney general suit under Title I is not subject to the arbitration agreement, and this outcome is entirely consistent with the FAA.

The California Supreme Court's decision in *Iskanian* provides a useful framework for analyzing Title I as a true *qui tam* statute. There, the court first concluded that even though PAGA was silent as to whether "representative" actions could be waived by agreement, separate provisions of the California Civil Code dictated that the right to bring such claims is not waivable.[65] Second, the court addressed whether the holding that an employee could *not* waive this right was preempted by the FAA (just as California's rule prohibiting class action waivers had been deemed preempted in *Concepcion*).[66] In addressing this question, the court began its analysis by noting that the FAA is focused on *private* disputes arising out of the "contract or transaction" that includes the arbitration agreement.[67] The court acknowledged that this language extends to cover private enforcement of statutory rights (even when those rights serve a public purpose)[68] but held that it does not encompass public *enforcement* efforts brought by the state.

For support, the court pointed to *Equal Employment Opportunity Commission v. Waffle House, Inc.*,[69] in which the United States Supreme Court concluded that an arbitration clause in the contract between Waffle House and one of its employees did not require the Equal Employment Opportunity Commission to arbitrate its enforcement action against Waffle House to obtain relief for that employee, even though the EEOC sought victim-specific relief. In that case the Supreme Court noted that despite an employer's or merchant's intention to shield itself from judicial actions seeking redress for wrongs committed against an employee or consumer covered by an arbitration clause, the contractual relationship between the parties is dispositive: "Because the FAA is at bottom a policy guaranteeing the enforcement of private contractual relationships, we look first to whether the parties agreed to arbitrate a dispute, not to general policy goals, to determine [whether a party is bound to arbitrate a dispute]."[70] As the EEOC was not a party to the contract, it had not agreed to the arbitration clause and could bring suit in court.

Because, according to the court in *Iskanian*, a private party's claim under PAGA is nothing more than a mechanism for enforcing "the *state's* interest in penalizing and deterring employers who violate California's labor laws," PAGA's *qui tam* provisions "do[ ] not interfere with the FAA's policy goals."[71] Therefore, the FAA does not preempt the rule that the right to bring PAGA actions in a public forum cannot be waived by agreement.[72]

The underpinnings of *qui tam* law support the *Iskanian* court's finding. While acknowledging that *qui tam* enforcement is unique in the law, the Supreme Court has confirmed that *qui tam* plaintiffs have Article III standing to bring actions on behalf of the government, whether or not they have themselves experienced a constitutional injury-in-fact, because they are the assignees of claims that could be brought by the government. Through this lens, a *qui tam* plaintiff's incentive payment is not an award to redress a statutorily defined injury, but rather a portion of the monetary judgment assigned to the "relator" as compensation for her efforts.[73]

This understanding is also consistent with the approach most courts have taken in deciding whether False Claims Act *qui tam* claims can be arbitrated. A federal district court has found, for example, that as a matter of contract interpretation, a whistleblower's *qui tam* claims are not subject to the arbitration clause in an employment contract:

> [P]laintiff's *qui tam* claims in no way impinge on her employee status. Even if plaintiff had never been employed by defendants, assuming other conditions were met, she would still be able to bring a suit against them for presenting false claims to the government. Moreover, as a relator plaintiff stands as a private representative of the government, participating in any recovery to which the government may be entitled.[74]

In other words, *qui tam* claims are not subject to private arbitration agreements because they are not private claims and, for this same reason, state rules creating unarbitrable *qui tam* claims are not preempted by the FAA.

Moreover, not only are actions brought under Title I brought on behalf of the state, they are also controlled by the state in important ways. In *Waffle House*, the Court noted that the EEOC had "exclusive authority over the choice of forum and the prayer for relief once a charge has been filed."[75] By allowing the state to intervene as of right within the first thirty days and at any point in the litigation as long as it demonstrates good cause, Title I gives the state a similar ability to control the litigation as the EEOC had, and considerably more than the state has under PAGA.

Furthermore, in a similar manner to the federal False Claims Act, Title I allows the state considerable authority and control over private attorney general actions even when it does not intervene. The state may, for example, move to stay discovery that interferes with public enforcement efforts and veto a private attorney general settlement.[76]

Although a private attorney general bringing an action under Title I would initially determine the forum and demands for relief, the state has the ability to intervene and take complete control over these and all other decisions regarding the litigation. Ultimately, an action brought under Title I belongs to the state and is the state's to prosecute (or dismiss).

Finally, unlike PAGA, where only "aggrieved" employees can bring actions under the statute, the private attorney general's status does not derive from any relationship with the defendant, let alone a contractual relationship that includes an arbitration clause. Under Title I, any private party can bring a claim on behalf of the state and prosecute that action as long as the state declines to intervene and drop or settle the matter, or bring the action on its own.[77] In the context of a Title I action, the private attorney general is akin to a government contractor, performing the state's enforcement duties in exchange for compensation.

In this sense, actions brought under Title I are reminiscent of actions brought under state attorneys general contingency arrangements with private attorneys—arrangements that have consistently been upheld by courts.[78] Although contingency-fee arrangements have been the subject of some political criticism,[79] there is little question about the state's legal *authority* to contract out enforcement duties to private lawyers. Moreover, Title I avoids many of the critiques normally leveled against contingency-fee arrangements. Unlike contingency-fee arrangements, which are sometimes negotiated behind closed doors, under Title I a proposed private attorney general suit is filed publicly. The attorney general's perspective on a proposed private attorney general suit is transparent and demonstrated by its public actions—intervention and dismissal demonstrates the attorney general's view that the case is frivolous; intervention and prosecution of the case reflects the attorney general's determination that the case is important but that it is not a good candidate for a private attorney general suit; and a decision not to intervene, but to allow the private attorney general suit to move forward, reflects a determination that the case has merit but is appropriately brought by a private attorney general under Title I.

III) A Note about the FAA and the Procedures Governing Multi-Employee or Multi-Consumer Actions under Title I

Much of the litigation surrounding the viability of the *Iskanian* rule has focused on the procedures for bringing a "representative action" under PAGA. In many ways, this focus flows naturally from the Supreme Court's analysis in *Concepcion*, where the Court concluded that "the switch from bilateral to class arbitration sacrifices the principal advantage of arbitration—its informality—and makes the process slower, more costly, and more likely to generate procedural morass than final judgment."[80] In *Sakkab*, the Ninth Circuit reasoned that the *Iskanian* rule is consistent with *Concepcion* largely based on its conclusion that "[b]ecause representative PAGA claims do not require any special procedures, prohibiting waiver of such claims does not diminish parties' freedom to select the arbitration procedures that best suit their needs."[81]

Like a "representative" action under PAGA, a suit under Title I that "allege[s] multiple violations that have affected different consumers or employees" does not require nearly the same procedural formality as a class action. Because it does not waive or limit "absent" consumers' or employees' rights to bring private actions on their own, there is no notice requirement and no requirement that the private attorney general or her counsel be "adequate."[82]

However, the procedural differences between a class action and a private attorney general action under Title I are not the sole—or even the most important—justification for the conclusion that Title I is not preempted by the FAA. After all, some courts, like the dissent in *Sakkab* may conclude that multi-employee or multi-consumer actions under Title I are "more likely to make the process slower, substantially more costly, and more likely to generate procedural morass than non-representative, individual arbitration."[83] More importantly, however, the informality of the procedures governing actions under Title I is only relevant to the preemption analysis if such actions could ever be arbitrated. But allowing such actions to be subject to private arbitration agreements, even while prohibiting waiver of the right to bring multi-employee or multi-consumer actions, would suggest that those actions *belong* to private parties and would undermine the state's argument that Title I actions belong to the state and are controlled by the state. In this sense, Title I escapes FAA preemption not because its procedures are consistent with "speedy and efficient" dispute resolution, but because it involves *public* enforcement actions that do not implicate *private* agreements to arbitrate.

TITLE II: CONDITIONS ON PERSONS DOING BUSINESS WITH THE STATE

Section 1. Findings.
To ensure that the State spends its limited funds in the most efficient manner possible, this Title prohibits the State from doing business with persons that form or enforce forced arbitration agreements with their consumers or employees. The secret nature of forced arbitration agreements between persons doing business with the State and their consumers or employees undermines the efficient management of State funds in the following ways:

(a) It prevents the State from learning whether goods or services provided by persons doing business with the State are the subject of consumer grievances concerning the quality of the good or service or whether the employees producing such goods or providing such services complain of unfair and illegal treatment that might interfere with the quality of the good or service;

(b) It obscures the extent to which persons doing business with the State violate the legal rights of their consumers or employees, and therefore whether such persons are breaching their obligations to the State or concealing from public scrutiny conduct that interferes with the quality of a good or service provided to the State; and

(c) It obscures the extent to which persons doing business with the State might be destabilized by the person's conduct as to consumers or its employees—such destabilization increases the likelihood that such person will defraud the State or be unable to perform under a contract with the State.

Section 2. Definition of "doing business with the State."
A person "does business with the State" when it or any of its subsidiaries or parent entities receives State funds exceeding $100,000 in exchange for goods or services provided to the State or a third party. Persons "doing business with the State" include but are not limited to persons performing public work on State contracts, merchants of goods or services purchased by the State, and persons providing services to third parties in exchange for funds provided directly from the State.

Section 3. Prohibition against the State doing business with persons that form or enforce forced arbitration agreements.

(a) The State shall not do business with any person or any of its parent entities or subsidiaries if that person includes forced arbitration clauses in any of its contracts with consumers or employees, unless one-hundred-eighty (180) days before doing business with the State, the person or its parent entity or subsidiary provides reasonable notice to its consumers or employees that it will cease enforcing arbitration clauses in consumer or employment contracts if such clauses exist in consumer or employment contracts.

(b) The State shall not do business with any person or any of its parent entities or subsidiaries if that person or any of its parent entities or subsidiaries enforces forced arbitration agreements against any of its employees or consumers.

Section 4. Enforcement.

(a) Before doing business with any person, the State agency representing the State in the business relationship shall confirm that such person, its parent entities, and its subsidiaries do not form or enforce forced arbitration agreements with consumers or employees and shall ensure, when appropriate, that a contract between the State and the person includes a provision prohibiting that person, its parent entities, and its subsidiaries from forming or enforcing forced arbitration agreements. Under this provision, a person or its parent entities or subsidiaries forms forced arbitration clauses in its contracts with consumers or employees if current contracts with consumers or employees include forced arbitration clauses, unless, one-hundred-eighty (180) days before doing business with the State, the person or its parent entity or subsidiary provides reasonable notice to its consumers or employees that it will cease enforcing arbitration clauses in consumer or employment contracts.

(b) If the State Attorney General, after giving a person doing business with the State notice and an opportunity to be heard, concludes that such person has violated the provisions of Section 3, the State Attorney General shall notify all State agencies doing business with the person about the violation and can seek actual damages owed to the State caused by such violation.

(c) If a State agency receives notice from the State Attorney General that a person with whom the agency does business has violated the provisions of Section 3, the agency shall terminate its business dealings with such person as soon as practical.

Section 5. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

Notes

Section 1—Findings. This section makes clear that the purpose of Title II is to protect the state's procurement interests by ensuring that the state has access to accurate information about any legal claims asserted by employees or consumers against persons doing business with the state.

Section 2—Broad definition of "person doing business with the State." The broad definition of "person doing business with the State" covers, among others, persons who sell goods and services to the state or who provide those services to third parties in exchange for state funds, but only when such funds are provided directly by the state and not a third party. In other words, a for-profit school is covered by Title II if it receives state funds in exchange for providing training to students, whether or not those students are employed by the state, but the school is not covered by the definition if it receives tuition payments from students, even if those payments originated in state grants. The definition is intended to extend the meaning of "person doing business with the State" to the full limits of the state's "market participant" authority.

Section 3—Application. Title II covers both the formation of new forced arbitration agreements and the enforcement of arbitration clauses that pre-exist the enactment of Title II. Businesses that have already entered into contracts with consumers or employees that include forced arbitration clauses are not barred from doing business with the state, as long as they have ceased enforcement of those clauses and so informed their consumers or employees sufficiently before contracting with the state so that the state has a public record on which to evaluate the contractor.

When the state acts like a private actor in the marketplace, it may affect the formation and enforcement of arbitration agreements pursuant to its "market participant" authority.

Analysis of Title II

The FAA preempts states from enacting laws that prohibit private parties from entering into forced arbitration agreements or that prohibits the enforcement of such agreements in private civil litigation. The FAA may also preempt state laws conditioning private persons' receipt of state funds on the requirement that they refrain from entering into arbitration agreements.[84] However, when the state acts like a private actor in the marketplace, it may affect the formation and enforcement of arbitration agreements pursuant to its "market participant" authority, described below.[85]

I) Federal Precedent for Title II

In 2014, the White House acted to protect its own financial interests in procurement matters from the dangers of opaque dispute resolution. On July 31, 2014, President Obama signed the Fair Pay and Safe Workplaces Executive Order.[86] Under a section titled "Complaint and Dispute Transparency," the order prohibits pre-dispute, binding arbitration agreements covering discrimination, assault, and sexual harassment claims in contracts between large federal contractors and their employees. Importantly, the executive order covers all of these contractors' employment agreements, even those with employees who do not work on federal contracts.

The Fair Pay and Safe Workplaces Executive Order provides an important precedent for states. Executive orders, like state laws, cannot conflict with federal statutes. Although the Federal Arbitration Act allows parties to agree to arbitrate discrimination and sexual harassment claims, the President has the authority to trump this general rule based on the "market participant" rule, which authorizes him to require that federal contractors resolve their disputes transparently, and which would allow states to enact similar requirements.[87]

II) "Market Participant" Authority Explained

The origin of the "market participant" rule lies in the centuries-old "government-proprietary" distinction,[88] under which governmental bodies are protected by sovereign immunity when acting pursuant to their governmental functions but are treated like any other private actor when acting pursuant to proprietary interests.[89] States acting like private actors—so the reasoning goes—should not benefit from a privilege derived from the special status of sovereign authority. Over the past several decades, courts have applied the distinction to support a different proposition: just as states cannot benefit from their governmental status (via sovereign immunity) when acting like private parties in the marketplace, they should also not be "punished" for their governmental status when acting pursuant to their proprietary interests and authority. In other words, a state should be able to set the same kinds of policies as private actors when it comes to the state's private activities. This is the "market participant" rule.

The "market participant" rule applies when a government agency requires an entity with which it does business (generally in a contracting relationship) to take certain actions that the agency could not normally require the entity to take because of limitations on the agency's authority as a governmental actor, but that a private market participant could require the entity to take as a condition of its business relationship with the entity. As long as the governmental agency acts as a "market participant," the requirement is not subject to federal preemption or other normal limitations on the agency's regulatory authority. But if the agency's purpose is *actually* to regulate the entity with which it does business, then the requirement is subject to the same constraints as other kinds of regulations.

Litigation concerning the "market participant" rule has arisen frequently in two categories of cases: first, in cases involving governmental action favoring in-state residents, which might violate the Dormant Commerce Clause;[90] and, second, in cases involving governmental action that pressures private companies to depart from the default labor-management practices prescribed by federal labor law, which might contravene the implied preemption doctrine derived from the National Labor Relations Act.[91] In these contexts, when applying the "market participant" rule, Supreme Court and lower court decisions accommodate "a complex range of competing constitutional values"[92] to determine whether the state or locality is acting as a regulator or a private market participant.

First, courts examine whether the governmental expenditure takes the *form* of private action. In other words, to act like a "market participant," the state's conduct must look like the conduct of a "market participant."

Second, courts examine whether the governmental purpose is proprietary or regulatory.[93] Courts consider a wide range of sources, including the legislative history of the state enactment, the expressed legislative findings supporting the enactment, and whether the enactment, considered as whole, is fully congruent with the putative proprietary interest.[94] However, courts do not perform a "factual investigation into the particular subjective motives of the relevant government [policymaker]." [95]

Third, depending on the analysis under the second prong, courts examine whether the challenged action has a sufficiently "narrow scope [to] defeat an inference that its primary goal was to encourage a general policy rather than address a specific proprietary problem."[96] This prong of the inquiry assumes that private actors motivated by proprietary (as opposed to ethical or regulatory) interests are only concerned with how the actors with which they do business conduct themselves inside the business relationship, and not with these actors' conduct outside of the proprietary relationship. Similarly, according to this view, a governmental agency generally acts with a regulatory purpose if it acts out of concern with a private party's conduct outside of its relationship with the government.[97]

III) Application of "Market Participant" Rule to Title II

Title II is a proper exercise of state "market participant" authority. Not only does it have a logical and defensible proprietary purpose, but its effects are targeted toward achieving these proprietary aims.

A) The State Acts As a Market Participant in Enacting Title II

Title II takes the form of "market participant" conduct. Title II does not govern all recipients of government expenditures, just those who are paid by the government for the provision of a good or service to the government or a third party. The state does not act like a "market participant" when it makes unconditional payments to private parties. The state does, however, act like a "market participant" when it makes payments with the expectation that recipients of such payments perform a service in return, and the state has a "market participant" interest in ensuring that it selects recipients that can perform that service efficiently.[98]

B) Title II Establishes a Valid "Market Participant" Purpose

The policies expressed in Section 1 of Title II describe strong reasons for prohibiting persons doing business with the government from entering into or enforcing forced arbitration clauses. As explained above, the state is at risk of experiencing financial harm if its contractors resolve their disputes privately, because the state will not be able to make informed contracting decisions or be confident that its contractors will be able to perform their obligations efficiently.

A state enacting Title II might be wrong about the net effect such a provision would have on public expenditures. It could be, for example, that arbitration decreases overall costs or that claim suppression results in a net-negative effect on the amount of funds the state must pay for the service or good at issue. These possibilities, however, "bear[ ] only on whether the [state] made a good business decision, not on whether it was pursuing regulatory, as opposed to proprietary, goals."[99] The real inquiry, as applied by the Supreme Court is whether the statutory language or structure is consistent with a plausible, stated proprietary goal. Title II passes that test.

C) The "Scope" of Title II Is Appropriate

Title II is closely tied to the stated "market participant" purpose. Title II is designed to ensure that the state can access information about any legal claims made by employees or consumers against a potential government contractor or other person doing business with the state both before entering into a contracting relationship and after commencing such a relationship, to ensure that the entity is performing its obligations efficiently and as prescribed by the contract. Toward this end, the Title prohibits persons doing business with the state from entering into or enforcing forced arbitration agreements.

The fact that Title II might have broad effects does not mean that its scope is impermissibly broad. The Ninth Circuit has explained that courts should look first to the "*nature* of the [state] expenditure" to determine whether a "comprehensive state polic[y] with wide application" is, nonetheless, "essentially proprietary" or at least lacking the effect of "broad social regulation." If so, the state action survives.[100]

Furthermore, the D.C. Circuit has flatly rejected the argument that the government acts as a regulator when it pursues "blanket, across-the-board rules that prohibit certain actions on the part of its contractors and recipients of its financial assistance."[101] The issue, according to the court, is not the breadth of the government action but the relationship between the conduct the government seeks to compel among recipients of government funds and the work these persons do for the government. On this last measure, although Title II proposes an "across-the-board" rule, there is a close connection—explained in the legislative findings—between the rule and government expenditures.

Moreover, the fact that Title II affects all of a potential contractor's employment and consumer contracts, not just those contracts directly tied to the government project, is also logically and closely tied with its proprietary purposes. The state has an interest in ensuring that its private contractors and other parties with which it does business do not form or enforce forced arbitration agreements with consumers and employees because forced arbitration obscures the private dealings of government contractors (and other persons doing business with the state). In doing so, the contractor undermines the state's ability to make informed and economical decisions as a market participant both before entering into a contract and while a contracting entity is performing under a contract, in order for the state to ensure that the contracting entity is performing its obligations effectively and efficiently.

The state's interest in the transparency of its business partners' dispute resolution processes is unique relative to other proprietary interests at stake in "market participant" cases because the interest is implicated by *all* of the business partners' relationships with consumers and employees. The concerns against which Title II seeks to protect potentially would arise if any of a business partner's consumers or employees filed claims against it. Any of these claims might provide valuable information to the state about the quality of goods or services provided to the state. And the financial costs and destabilizing effects of these disputes potentially would spill over into the entity's business relationship with the state whether or not the disputes arose from consumer or employment relationships that were directly tied to the business relationship with the state. Therefore, although Title II would have a broad reach, its effects are precisely tailored to its stated purpose.

TITLE III: CLEAR NOTICE AND SINGLE DOCUMENT RULE

Section 1. Findings.
Obscure and overly complex language in consumer and employment contracts interferes with employees' and consumers' ability to provide meaningful assent to their consumer and employment contracts. To ensure that private parties comprehend the material terms of the consumer and employment contracts into which they enter, this Title requires that merchants and employers in designated forms of contracts adequately disclose terms and condition.

Section 2. Coverage.
This Title applies to contracts of the categories set out in Section 3 formed after this Title's effective date that meet any one of the following three criteria:

(a) An employment or consumer contract not written in plain language that an average consumer or employee would understand;

(b) An employment or consumer contract not written in the language in which the transaction was conducted, unless it can be proven that fewer than ten percent (10%) of the entity's transactions are conducted in that language; or

(c) If a consumer contract, all of the material terms are not found in a single document.

Section 3. Categories of contracts covered.
[*TO BE FILLED IN BY EACH STATE*]

Section 4. Rights when a covered contract is non-conforming.
A consumer or employee may seek a court order reforming any contract covered by Section 2. Such reformed agreement shall reflect the understanding of the parties, and the court may exclude terms not written in plain English, not written in the language in which the transaction was conducted, or found in a separate document.

Section 5. Pre-existing rules.
This Title shall be applied in conjunction with pre-existing rules regarding contract formation, including rules regarding reasonable notice and the conduct a consumer or employee must manifest in order to assent to an agreement.

Notes

Section 1—Findings. This section makes clear that Title III is not concerned with the substance of contractual terms, nor with arbitration clauses in particular, but rather with providing consumers and employees the opportunity to truly assent to their contractual arrangements.

Section 2—Contracts that do not meet the Title's conditions are voidable. Title III does not automatically void contracts that do not meet the conditions set out here. Employees and consumers must affirmatively raise this defense if they seek to avoid a material obligation. In this way, consumers and employees may raise rights protected by a contract that does not meet the technical requirements of this Title.

Section 2(a)–(c)—Coverage. This Title does not apply especially to arbitration clauses, and this Title does not target arbitration clauses.

Section 3—Allowing states to identify the industries at issue. Because of the number of different considerations that might apply in each industry depending on the state, the Model Act allows states to identify the types of contracts to which this Title will apply.

Section 4—Allowing the court to reform a non-conforming contract. This Title allows the court the discretion to reform a non-conforming contract, consistent with the parties' intent, with recognition of the criteria specifically identified in Section 2 that frequently characterize unclear and unfair contractual terms.

Section 5—Consistent with the common law. This Title provides additional rules regarding the provision of adequate notice of material terms to consumers and employees. The Title does not abrogate pre-existing common law rules regarding notice and assent. In other words, even if the material obligations of a contract are clearly set out in the manner prescribed by this Title, the consumer or employee is not bound by those terms unless she manifests assent to those terms by, for example, signing the agreement.

Analysis of Title III

Individuals rarely read the fine print in their form contracts, and even when they do read these contracts, they rarely understand their import.[102] Although states cannot prohibit employers and merchants from conditioning employment or provision of goods or services on a consumer's or employee's assent to an arbitration agreement, states can require that employees and consumers be on reasonable notice of the terms.

Because the "federal policy favoring arbitration" does not apply to questions of contract formation, and the parties cannot delegate the question of contract formation to an arbitrator, state courts (and federal courts applying state law) have an important role in policing arbitration agreements to ensure that consumers and employees are not bound by "forced" arbitration agreements unless they are on notice (either inquiry or actual) of the agreement and then assent to it through conduct that is sufficient to bind them. Since 2013, a number of state supreme courts—including the highest courts in Florida, Missouri, and West Virginia—have issued sweeping and important decisions governing the question of contract formation. These courts have concluded, in a variety of contexts, that businesses need to mount actual evidence to establish contract formation and that merely pointing to an arbitration clause in a form contract is not enough to bind a consumer to that clause.[103]

These cases illustrate the important role of rigorous judicial analysis in determining whether parties have actually assented to arbitrate. There is less precedent regarding rules regulating the formation of arbitration agreements on an *ex ante* basis because rules that specifically target the mechanism of forming arbitration clauses, in particular, are likely preempted by the FAA.[104] Therefore, any law regulating the formation of arbitration agreements must speak to the formation of other kinds of contractual agreements as well. The most helpful precedent for rules like Title III, then, lies in state laws that regulate categories of contractual terms that include more than just arbitration clauses—for example, rules relating to the formation of agreements to waive statutory or constitutional rights,[105] or rules relating to assent to material terms.[106]

A state rule targeting all material terms, even when applied to arbitration clauses in specific cases, is unlikely preempted. For support, states can point to precedent concluding that stand-alone arbitration agreements entered into between car dealers and buyers are not enforceable when the relationship is covered by a "single document rule" requiring that all material terms be included in a single document.[107]

It is important to note that Title III might be subject to a specific and narrow preemption argument. The FAA makes agreements to arbitrate "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[108] In the Ninth Circuit case *Ting v. AT&T*,[109] the court held that a California rule prohibiting class action waivers in consumer contracts was preempted by the FAA because the state rule did not apply to *any* contract, but only to consumer contracts.[110] The argument could be made here that because these rules do not apply to *any* type of contract, but only to those identified by the state, they are preempted by the FAA.

This argument should fail. As the Ninth Circuit recently explained:

> The Supreme Court has clarified that a state contract defense must be "generally applicable" to be preserved by [the FAA's] saving clause. *Concepcion*, 131 S.Ct. at 1746. It is well established that the FAA preempts state laws that single out arbitration agreements for special treatment. At minimum, then, [the savings clause's] "any contract" language requires that a state contract defense place arbitration agreements on equal footing with non-arbitration agreements. . . . Some of our cases can be read to suggest that the phrase "any contract" in [the FAA's] saving clause requires that a defense apply generally to all types of contracts, in addition to requiring that the defense apply equally to arbitration and non-arbitration agreements. *See Ting v. AT & T*, 319 F.3d 1126, 1147–48 (9th Cir. 2003). However, the Court's decision in *AT & T Mobility, LLC v. Concepcion* cuts against this construction of the saving clause. The Court in *Concepcion* held that the FAA preempted California law providing that class action waivers in certain consumer contracts of adhesion were unconscionable and unenforceable. 131 S.Ct. at 1748–53. Even though the state-law rule at issue only applied to a narrow class of consumer contracts, the Court strongly implied that the rule was a "generally applicable contract defense[ ]." *See id.* at 1748.[111]

In other words, the FAA protects against differential treatment of arbitration agreements as compared to other agreements, but it has no bearing on state contract rules that do not single out arbitration agreements for disfavor but that do treat some kinds of contracts differently than others. As explained above, then, Title III escapes FAA preemption because it applies to all material terms, not just arbitration clauses; it is not relevant to this analysis that the state may choose to apply Title III to some types of contracts and not others.

Title III escapes FAA preemption because it applies to all material terms, not just arbitration clauses.

TITLE IV: UNCONSCIONABLE TERMS IN STANDARD FORM CONTRACTS

Section 1. Findings.

The inclusion of unconscionable terms in standard form contracts regarding dispute resolution is unfair not only because any resulting dispute resolution proceeding is unfair to the party forced to agree to the unconscionable terms, but also because the unconscionable terms discourage valid claims. Furthermore, when the provisions are challenged, courts may simply strike the unconscionable terms but enforce the remainder of the agreement regarding dispute resolution. As a result, businesses have little incentive not to include these terms. Furthermore, because this Title governs form contracts, it is unlikely that there is any meeting of the minds over a dispute-resolution agreement that does not include severed unconscionable terms.

Section 2. Unconscionable terms.

There is a rebuttable presumption that the following contractual terms are substantively unconscionable when included in a standard form contract to which only one of the parties to the contract is an individual and that individual does not draft the contract:

(a) A requirement that resolution of legal claims take place in an inconvenient venue. An inconvenient venue is defined for State law claims as a place other than the county where the individual resides or the contract was consummated, and for federal law claims as a place other than the federal judicial district where the individual resides or the contract was consummated;
(b) A waiver of the individual's right to assert claims or seek remedies provided by State or federal statute;
(c) A waiver of the individual's right to seek punitive damages as provided by law;
(d) A requirement that the individual bring an action prior to the expiration of the applicable statute of limitations;
(e) A requirement that the individual pay fees and costs to bring a legal claim substantially in excess of the fees and costs that this State's courts require to bring such a State law claim or that federal courts require to bring such a federal law claim.

Section 3. Relation to common law and the Uniform Commercial Code.
In determining whether the terms described in Section 2 are unenforceable, a court shall consider the principles that normally guide courts in this State in determining whether unconscionable terms are enforceable. Additionally, the common law and Uniform Commercial Code shall guide courts in determining the enforceability of unfair terms not specifically identified in Section 2.

Section 4. Severability.
There is a rebuttable presumption that unconscionable terms in form contracts are not severable from the agreements in which they are situated, thus rendering the entire agreement unenforceable. In determining whether this presumption has been rebutted courts should consider general state law principles regarding the severability of unenforceable terms.

Some of the aspects of arbitration that are most likely to chill claims are insulated from state regulation by the FAA.

Section 5. Unfair and deceptive act and practice.
It is an unfair and deceptive practice in violation of [*the State deceptive practices statute*] to include one of the presumptively-unconscionable terms identified in Section 2 in a standard form contract to which only one of the parties to the contract is an individual and that individual does not draft the contact. Notwithstanding any other state laws to the contrary, a party who prevails in a claim under this Section shall be entitled to $1,000 in statutory damages per violation. Additionally, such an action may be maintained by an employee against her employer whether or not [*the State deceptive practices statute*] otherwise allows for such claims.

Notes

Section 2—Unconscionable terms. This Title expresses legislative findings that there is a presumption that certain contractual terms are substantively unconscionable. The state's courts should be guided by this provision in determining whether a particular contractual term is unconscionable based on all the factors involved in such an analysis under state law. This Title, however, shifts the burden to the party seeking to enforce the contract to show that, given all the factors involved, an enumerated provision is *not* unconscionable.

Section 3—Relation to the common law and the UCC. Section 2 of Title IV should be considered a codification of general common law and Uniform Commercial Code rules regarding the unconscionability of unfair terms. Section 3 clarifies that this Title does not alter the normal factors dictating whether unconscionable terms are unenforceable. In most states, one of those factors, in addition to the unfairly one-sided nature of the contract terms in question, is whether the manner in which the contact was formed was "procedurally" unconscionable.[112] Section 3 also clarifies that the enforceability of unfair terms not expressly listed in Section 2 turns on the principles that normally guide courts in deciding whether such terms are enforceable, and that the absence of an unfair term from Section 2 does not create any presumption that such term is *not* unconscionable.

Section 4—Severability. Section 4 prescribes that the inclusion of an unconscionable term in a standard form contracts renders the entire agreement in which it is situated presumptively unenforceable. Courts often conclude that unconscionable terms should be severed from arbitration agreements and the agreements enforced without the offending clause.[113] This approach, however, has the consequence of creating perverse incentives. In the arbitration context, in particular, numerous courts have explained that "courts should not sever unconscionable provisions of arbitration clauses while leaving the rest intact, because doing so creates an incentive to get away with as many 'bad' arbitration provisions as possible."[114] Unless courts completely refuse to enforce arbitration agreements containing illegal terms, the drafters of these contracts will continue to pack agreements with unconscionable terms, like those at issue here. Otherwise, drafters will know that the worst that can happen is that their most abusive terms are stricken, and even then only after a battle through expensive motion practice. To make clear that this is a rule of general applicability, it applies to all unconscionable terms in standard form contracts.

Section 5—UDAP violation. Section 5 provides that the inclusion of the specified terms in a form contract constitutes a violation of the state's general statute prohibiting unfair or deceptive acts or practices ("UDAP" law). Section 5 thereby incorporates the state's UDAP law, including any applicable procedural rules and remedies. Some state laws provide that the inclusion of unconscionable terms not only renders the contract unenforceable in certain contexts, but that it also provides for a cause of action under state law.[115] Explicitly making the inclusion of unconscionable terms in standard form contracts a UDAP violation will, like Section 4, deter businesses from including unconscionable terms to chill claims. To ensure that it has the broad reach notwithstanding potentially contradictory principles under general state UDAP law, Section 5 also allows for the recovery of statutory damages,[116] and expressly allows for claims against brought by employees against employers.[117]

Analysis of Title IV

In practice, arbitration clauses in consumer and employment contracts not only provide an alternative forum for resolving disputes; because of the costs of arbitration, these clauses often prevent consumers and employees from being able to assert their rights in any forum. Some of the aspects of arbitration that are most likely to chill claims are insulated from state regulation by the FAA. For example, the Supreme Court has deemed bilateral dispute resolution to be so fundamental to the ideals of arbitration purportedly embodied in the FAA, that so-called "class action waivers" are effectively protected by the FAA from state-law based challenges.[118]

Many arbitration clauses, however, include terms that not only chill claims but that are inconsistent with the ideals of efficient, speedy, and cheap dispute resolution. Examples are terms calling for excessive costs and fees or requiring the consumer or employee to waive substantive rights or arbitrate in a far-off forum. These types of terms are not protected by the FAA from state-law based challenges and are frequently deemed unenforceable as a matter of state law.[119]

Section 2 of Title IV is merely a codification of common law principles that have already been adopted by courts in a number of states and, therefore, just as these common law rules are not preempted by the FAA, neither is Section 2. This analysis is not affected by the fact that this Title may appear to "target" arbitration in a way that generally applicable common law rules do not. First, these provisions do not speak to *private* dispute resolution in particular. For example, this Title would likely render unconscionable a provision regarding suit in a distant *judicial* forum.

Furthermore, the distinction between the codified rules set out here and the common law principles that courts apply in specific cases does not have any legal relevance. If the FAA preempted legislatures from codifying specific guidance for courts on the enforceability of terms related to arbitration based on general legal principles like unconscionability, it would similarly preempt courts from applying general legal principles in specific cases related to arbitration. As the Supreme Court has recognized, however, *Concepcion* did not overthrow the common law contract defense of unconscionability.[120]

Moreover, not only does this Title not target "fundamental" attributes of arbitration for disfavor, which would be impermissible under *Concepcion*, but it also does not abrogate courts' important role in determining whether—based on the facts of a particular case—certain provisions are unconscionable. In 2013, in *Sonic-Calabasas A, Inc. v. Moreno*,[121] the California Supreme Court concluded that a *per se* rule prohibiting the enforcement of waivers of employees' right to administrative hearings, known as "Berman" hearings, was preempted by the FAA because such a rule interfered with fundamental aspects of arbitration, including the possibility of more expeditious dispute resolution in the absence of a "Berman" hearing. The court explained, however, that the waiver of a "Berman" hearing is still relevant to a general unconscionability analysis:

> [T]he waivability of a Berman hearing in favor of arbitration does not end the unconscionability inquiry. The Berman statutes include various features designed to lower the costs and risks for employees in pursuing wage claims, including procedural informality, assistance of a translator, use of an expert adjudicator who is authorized to help the parties by questioning witnesses and explaining issues and terms, and provisions on fee shifting, mandatory undertaking, and assistance of the Labor Commissioner as counsel to help employees defend and enforce any award on appeal. Waiver of these protections does not necessarily render an arbitration agreement unenforceable, nor does it render an arbitration agreement unconscionable per se. But waiver of these protections in the context of an agreement that does not provide an employee with an accessible and affordable arbitral forum for resolving wage disputes may support a finding of unconscionability. As with any contract, the unconscionability inquiry requires a court to examine the totality of the agreement's substantive terms as well as the circumstances of its formation to determine whether the overall bargain was unreasonably one-sided.[122]

Although its focus on aspects of arbitration that are not "fundamental" brings this Title outside the ambit of FAA preemption on its own, this Title goes one step further in ensuring its viability. Like general rules of unconscionability, the Title instructs courts that certain enumerated terms are presumptively unconscionable. Consistent with the fact-intensive nature of unconscionability analysis, the court should weigh all the facts involved in a case to determine unconscionability but, in enacting this Title, the legislature has determined that the likelihood of these enumerated terms being unconscionable is such that the burden should shift to the drafter to show why in the facts of a case the term is not unconscionable.

This same analysis should apply to Section 4, which creates a presumption that unconscionable terms in standard form contracts are not severable from the remainder of the contract. The United States Supreme Court recently granted *certiorari* in *MHN Gov't Services Inc. v. Zaborowski* to consider whether California has an arbitration-specific severability doctrine, and, if so, whether that doctrine is preempted by the FAA.[123] At this point, however, it is black-letter law that, like unconscionability, severability doctrine is a generally-applicable state law doctrine. It requires courts to examine whether there was a "meeting of the minds" on a cohesive agreement that does not include the unenforceable term.[124] Based on the legislative findings expressed in Section 1, this Title appropriately extends the doctrine to protect against the perverse incentives that severing unconscionable terms sometimes creates for drafters. Section 1 also explains that this presumption is consistent with *general* rules regarding severability because there usually will not have been a genuine meeting of the minds over a dispute-resolution term in a form contract, let alone a term with unconscionable language excised. This Section further insulates itself from preemption both by applying to all form contracts and by creating only a presumption of non-severability and allowing courts to make the final determination based on all of the evidence and the state's "general rules" regarding severability.

Finally, the provision expressly providing that inclusion of an unconscionable term enumerated in this Title constitutes an unfair and deceptive practice does not change the preemption analysis. A number of state laws, regulations, and cases hold that the inclusion of unconscionable terms in standard form contracts is unfair or deceptive. Applying this rule to arbitration clauses does not run afoul of the FAA, because the state law violation follows only from a finding that the provision is unconscionable and unenforceable based on considerations that are not preempted by the FAA.[125]

TITLE V: PROHIBITION OF FORCED ARBITRATION CLAUSES UNDER STATE LAW

Section 1. Findings.

Forced arbitration agreements covering consumers and employees are contrary to the established public policy of this State. Because employees and consumers are forced to assent to these agreements as a condition of being an employee or consumer before any dispute has arisen with the employer or merchant, these agreements do not offer employees and consumers a meaningful choice about how to resolve their disputes with the employer or merchant. In addition, forced arbitration agreements prevent employees and consumers from effectively vindicating their rights under State law. For these reasons, except when inconsistent with federal law, the State prohibits the formation and enforcement of forced arbitration agreements in employment and consumer contracts.

Section 2. Prohibition of arbitration clauses in insurance agreements.

A forced arbitration agreement within or part of any written contract for insurance with a consumer or other written agreement involving the offering of insurance to a consumer is invalid, unenforceable, and void. Any such arbitration agreement shall be considered severable, and all other provisions of the contract for insurance shall remain in effect and given full force.

Section 3. Prohibition of arbitration clauses in employment contracts for workers exempted from the Federal Arbitration Act.
A forced arbitration agreement within or part of any written contract of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce is unenforceable and void. Any such arbitration agreement shall be considered severable, and all other provisions of the employment contract shall remain in effect and given full force.

Section 4. Prohibition of arbitration clauses that are not governed by federal law.
Any forced arbitration agreement, or portion thereof, in an employment or consumer contract is invalid, unenforceable, and void, when the enforceability of such arbitration agreement, or the portion at issue, is governed by State law. Any such arbitration agreement shall be considered severable, and all other provisions of the employment contract shall remain in effect and given full force.

Section 5. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

Notes
Section 2—Prohibition of arbitration clauses in insurance agreements. The federal McCarran-Ferguson Act allows states to regulate arbitration clauses in insurance contracts. Section 2 of this Title is limited to insurance contracts and declares arbitration requirements in such contracts to be void. Unlike Title III, which declares material terms *voidable* if the consumer or employee does not expressly assent to them—because of a concern that declaring all material terms void would have unintended consequences—this section declares arbitration clauses in insurance agreements *void*. It does not alter other terms of insurance agreements.

Section 3—Prohibition of arbitration clauses in employment contracts governing transportation workers. The Federal Arbitration Act includes an express exception for "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce" that the Supreme Court has concluded removes "transportation workers" from the FAA's reach. [126] Title V expressly incorporates the federal legislative language to ensure that arbitration clauses in all contracts that fall within the federal exemption are void.

Section 4—"Catch all" prohibition. Title V also includes a "catch all" provision that renders void any forced arbitration clause in an employment or consumer contract when such arbitration clause is governed by state law and not the FAA. This provision would cover forced arbitration clauses in employment and consumer contracts that do not affect interstate commerce and forced arbitration clauses in employment and consumer contracts in which the parties agree that such arbitration clauses are covered by state and not federal law. It would also apply to the extent that Congress or the Supreme Court excludes other types of employment or consumer contracts from the FAA.

Analysis of Title V
Although state rules that limit the enforceability of arbitration are generally preempted by the Federal Arbitration Act,[127] federal law provides various exceptions to this rule. This Title clarifies that when state and not federal law governs the enforceability of a forced arbitration clause in an employment or consumer contract, that arbitration clause is void as a matter of state law.

First, the federal McCarran-Ferguson Act includes a "reverse preemption" provision that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance… unless such Act specifically relates to the business of insurance."[128] Because the FAA does not specifically relate to insurance, state insurance law can prohibit arbitration agreements in insurance transactions. A number of states either provide that arbitration clauses in insurance agreements are not enforceable or provide that arbitration agreements in certain lines of insurance are unenforceable.[129] Although these regulations would likely be preempted were it not for the McCarran-Ferguson Act, the FAA does not preempt such rules as long as they clearly identify that they are intended to regulate the "business of insurance."[130] Section 2 of this Title specifically addresses the "business of insurance," and thus is not preempted by the FAA.

Second, the FAA itself states that it does not govern "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."[131] The United States Supreme Court has interpreted this language as removing from the FAA's coverage "contracts of employment of transportation workers."[132] Nonetheless, arbitration clauses included in contracts of employment of transportation workers can still be enforceable as a matter of state law.[133] By enacting this Title the state ensures that such agreements are void and unenforceable.

Finally, the FAA does not govern arbitration clauses in contracts that the parties agree are governed exclusively by state law[134] or that do not involve interstate commerce.[135] This Title makes clear that in these circumstances, and any others in which federal law might not apply, forced arbitration clauses in consumer and employment contracts are void and unenforceable.

TITLE VI: DATA DISCLOSURE REQUIREMENTS FOR ARBITRATION ADMINISTRATORS

Section 1. Findings.
Unlike administrative or judicial proceedings, arbitration proceedings regarding consumer and employment claims are not public. The lack of public information regarding these proceedings interferes with the State's ability to monitor arbitration administrators to ensure that they comply with basic principles of fairness and impartiality.

Section 2. Requirements.
(a) Any private company that administers five or more arbitrations a year in this State involving a consumer or employee shall collect and publish the following information about each of its arbitrations for at least five years after the arbitration has completed:

(i) The names of the parties to the arbitration;
(ii) The party that filed the arbitration claim;
(iii) The type of dispute involved, including goods or services, insurance, credit, debt collection, or employment;

(iv) The prevailing party;

(v) Whether the consumer or employee was represented by an attorney;

(vi) The date the company administering the arbitration received the demand for arbitration, the date the arbitrator was appointed, and the date of the arbitration's disposition;

(vii) Whether the arbitration resulted in an in-person hearing;

(viii) Whether the parties provided each other with any pre-hearing discovery;

(ix) The amount of the claim, the amount of the award, and any other relief granted, if any;

(x) The name of the arbitrator, his or her total fee for the case, and the percentage of the arbitrator's fee paid by each party; and

(xi) The arbitrator's professional affiliations.

(b) Information published pursuant to this title must be updated at least quarterly, and made available to the public in a computer-searchable format, which shall be accessible at the website of the private company administering the arbitrations, if any, and on paper upon request.

(c) No private company shall have any liability for collecting, publishing, or distributing the information in accord with this section.

Section 3. Confidentiality.
This Title does not require disclosure of any information other than that set forth in Section 2.

Section 4. Enforcement.
Any private person and any public enforcement agency responsible for enforcing State law under this Title may bring suit for injunctive relief against an entity that violates these provisions, and may recover reasonable attorney fees and other costs if an injunction or equivalent relief is awarded. Injunctive relief is the only relief available in a suit arising from failure to comply with this Title.

Section 5. Severability.
Should a court decide that any provision of this act is unconstitutional, preempted, or otherwise invalid, that provision shall be severed, and such a decision shall not affect the validity of the act other than the part severed.

Notes

Section 2—Requirements. The requirements of this Title are designed to provide the state and the state's residents with an overall picture of how disputes within its borders are resolved by private arbitrators. This Title does not alter rules regarding arbitration agreements between parties or regarding the confirmation of arbitration awards.

Section 3—Confidentiality. Private information about a consumer or employee shall remain confidential unless the parties agree otherwise.

Section 4—Enforcement. This Title allows for *private* enforcement of its requirements. The only remedy available under this Title, however, is injunctive relief, meaning arbitration providers will not be held liable for money damages related to any failure to abide by this Title's disclosure requirements.

Analysis of Title VI

California currently regulates arbitration administrators in a similar fashion to Title VI.[136] Like California law, Title VI requires arbitration administrators (not the individual arbitrators) to disclose information about individual cases and their outcome, how frequently a business uses the same arbitration service provider, how long arbitrations take, how much arbitrators are paid, and who pays them.

This provision would provide useful information to states considering adjusting their policies and enforcement efforts. Indeed, fairly recent events illustrate the importance of state oversight of private arbitration companies. In 2009, the Minnesota attorney general filed a lawsuit against a major national private arbitration provider, the National Arbitration Forum (NAF). The lawsuit arose from the close financial relationship between NAF and a large national debt collection law firm, along with NAF's subsequent administration of thousands of consumer debt collection arbitrations brought by the same law firm. The lawsuit alleged, among other things, that NAF engaged in unfair and deceptive practices by representing to the public that it provided an independent dispute resolution forum, when in fact NAF was financially intertwined with a party that had a substantial interest in many of its arbitrations, and NAF frequently advertised to corporations that it provided a favorable forum for collection arbitrations. The lawsuit resulted in a consent decree in which NAF agreed to terminate administering consumer arbitrations nationwide. Disclosures such as those required by this Title help to expose this type of corruption among arbitration administrators.

California currently regulates arbitration administrators in a similar fashion to Title VI.

Title VI expressly authorizes public enforcement agencies and private parties seeking information under this Title to bring suit seeking injunctive relief.[137] Even though Title VI serves a public purpose, states might not always know whether arbitration providers are actually meeting Title VI's requirements. Therefore, this Title extends enforcement authority to persons such as consumers and employees participating in arbitrations, and journalists or others who interested in accessing data subject to the disclosure requirements of this Title.

The FAA does not preempt reasonable state regulation of arbitration administrators like the American Arbitration Association as long as the regulation does not indirectly limit the enforceability of an arbitration provision. Businesses might argue that this Title interferes with their FAA-protected right to require consumers and employees to resolve disputes through confidential proceedings. However, this Title does not regulate arbitration *agreements*. The parties are permitted to arbitrate before the forum of their choice. Moreover, this requirement does not force the administrator to make public any materials that are the subject of that arbitration, or to otherwise implement procedures that would conflict with the "purposes of the FAA" as understood by the Supreme Court, but rather to provide data on the parties, the arbitrators, and the arbitration fee.

TITLE VII: APPELLATE JURISDICTION

Section 1. No jurisdiction over interlocutory appeals.
Appellate courts shall not have jurisdiction to review a trial court's interlocutory order denying a motion to compel arbitration or otherwise concluding that an arbitration agreement is unenforceable or does not cover a particular claim. Appellate review of the denial of a motion to compel arbitration may be had after a final

judgment has issued. An interlocutory appeal shall be allowed if the trial court orders arbitration and dismisses the suit, or orders arbitration and stays the litigation.

Section 1—No interlocutory appeal. Litigation about the enforceability of arbitration clauses is often expensive and prolonged. This Title provides that parties shall have no right to appeal the denial of a motion to compel arbitration or other order concluding that an arbitration agreement is unenforceable or does not govern a particular dispute or claim until after the court has issued a final judgment in the dispute. In doing so it prevents arbitration agreements from slowing employees' or consumers' efforts to enforce their rights under state law.

The defendant is not similarly prejudiced when an interlocutory appeal is taken from an order staying litigation pending arbitration, because it is the other party that is seeking relief. In addition, in many cases it is not practical for the consumer or employee to proceed through arbitration because of the costs of arbitrating or the inability to bring class or collective claims, so that it is necessary for the consumer or employee to be able to appeal the order on an interlocutory basis.

Analysis of Title VII

The FAA does not preempt state law regarding the procedures for litigating issues related to arbitration.[138] Thus, despite Section 16 of the FAA that allows parties to appeal decisions denying motions to compel arbitration, some states already limit the right of interlocutory appeal in state courts.[139] By limiting the appealability of denials of motions to compel arbitration, states can ensure that employees' and consumers' claims are resolved quickly as opposed to being delayed by prolonged litigation regarding the enforceability of an arbitration clause.

TITLE VIII: PREVENTING RESPONDENTS FROM IMPROPERLY DELAYING THE ARBITRATION PROCEEDING

Section 1. Findings. The United States Supreme Court has held that the Federal Arbitration Act generally protects parties' right to enter into private agreements to resolve their private disputes expeditiously. That goal is frustrated if a party imposes an arbitration requirement on consumers or employees but, then using the procedures of the arbitration administrator chosen by that party, prevents the arbitration proceeding from going forward in an expeditious manner. In particular, when the entity that requires arbitration refuses to pay its required share of the expenses of arbitration, too often the consumer or employee is prevented from going to court and also prevented from having a speedy arbitration hearing. This conduct amounts to a breach of the arbitration agreement and should be grounds for the consumer or employee to bring her claim in court. However, arbitration administrators are often slow to enforce their own rules. This Title regulates administrators to ensure that they arbitrate disputes efficiently and speedily.

The FAA does not preempt state law regarding the procedures for litigating issues related to arbitration.

Section 2. Covered arbitration administrators.

This Title applies to all arbitration administrators that have administrated, in this State, three or more arbitrations brought by a consumer or employee over the past 12 months.

Section 3. Requirements to ensure expeditious dispute resolution.

This section applies if a forced arbitration agreement, whether expressly or through incorporation of the rules of the arbitration administrator, requires that in a case brought by an employer or consumer, the respondent must pay certain fees or costs before the arbitration proceeding can proceed. In that case, if those fees or costs are not paid within 7 days after those fees are due, the arbitration administer must:

(a) Begin administering the arbitration, by scheduling a hearing date, notwithstanding the respondent's failure to pay required fees; or

(b) Within 10 after the fees are due, refuse to administer the arbitration, and provide the consumer or employee with a letter explaining that the administrator will not administrate the arbitration, and expressly stating that the "arbitration forum designated by the parties is unavailable to resolve this dispute."

Section 4. Requirements to prevent pending cases from being improperly suspended.

This section applies if a forced arbitration agreement, whether expressly or through incorporation of the rules of the arbitration administrator, requires that in a case brought by an employer or consumer, the respondent must pay certain fees or costs during the pendency of an arbitration proceeding. In that case, if those fees or costs are not paid within 7 days after the fees are due, the arbitrator must:

(a) Continue the administering the arbitration proceeding notwithstanding the respondent's failure to pay required fees; or

(b) Within 10 days after the fees are due, issue a final award for the consumer or employee that provides all relief requested by the consumer or employee. If the consumer or employee has not expressly set out the amount of monetary damages demanded, the arbitrator may either issue an award on liability alone and allow a court enforcing the award to decide damages or may hold its own hearing on monetary damages within one week following the issuance of the final award concerning liability.

Section 5. Disclosure requirements.

Administrators covered by this Title shall publicly report the following, as applicable, and updated quarterly on the administrators publicly-accessible website for any arbitration demanded by a consumer or employee: when each arbitration demand was made, when each demand for payment of costs and fees is made, the date the respondent paid all fees and costs requested, when a hearing, either live or on the papers, was held, when the award was issued, when the arbitration administrator provided a letter indicating the arbitration would not proceed, and when an arbitration proceeding was terminated for lack of payment and an a resulting award is made to the consumer or employee.

Section 6. Enforcement.

The provisions of this Title shall be enforceable through an action seeking declaratory or injunctive relief by the Attorney General or any employee or consumer aggrieved by an administrator's failure to comply with this Title.

Section 7. Administrator's Right to Collect Fees. Whenever an arbitration agreement or the arbitration administrator's rules incorporated into that agreement require that the respondent pay fees or costs to the arbitrator or arbitration administrator, the arbitrator and administrator are third-party beneficiaries of the agreement to pay fees or costs. If the administrator administers an arbitration and an arbitrator proceeds with an arbitration notwithstanding the respondent's failure to pay fees or costs pursuant to Section 3(a) or 4(a) of this Title, then the administrator may pursue a breach of contract action against the respondent under State law to collect those fees or costs.

Notes

Section 1—Legislative findings. The legislative findings for this Title identify "stalled" arbitration proceedings as one of the most serious impediments many consumers and employees face in achieving redress in individual arbitrations. However, consistent with the focus of this Title, which regulates arbitration administrators and not the respondents in arbitration proceedings, the findings point out that at bottom prolonged dispute resolution in arbitration arises because arbitrators and arbitration providers fail to enforce their own rules.[140]

Section 2—Covered arbitration administrators. Like Title VI, this Title does not cover *every* private arbitration administrator. In this way, the Title avoids the critique that it effectively imposes requirements on private arbitration *agreements*. In theory, there is nothing to prevent a business from designating an arbitration administrator that is not covered by this Title.

Sections 3 & 4—Requirements. Sections 3 and 4 provide arbitration administrators with two different options when a respondent fails to pay fees required by the administrator's rules or demanded by the administrator. First, the administrator may administer the arbitration promptly and in accordance with its normal procedures. Second, under Section 3, the administrator may refuse to administer the arbitration and provide the employee or consumer with a letter stating that the forum is unavailable and thereby entitling the employee or consumer to file her claims in a public forum. Under Section 4, in the event the arbitration proceeding has already initiated, instead of asking the consumer or employee to start all over again in court, the provision provides that an award will be issued in the consumer's or employee's favor if the defendant fails to properly participate in the proceeding. Note that Section 3 addresses the common problem, particularly in AAA arbitrations, of respondents failing to pay or delaying in paying fees required to initiate the arbitration. Section 4 addresses a much less common problem, but a problem that could arise if arbitration administrators sought to evade the requirements of Section 3 by initiating the arbitration but then terminating it while it is pending before the arbitrator because of a failure to pay fees or costs.

Section 5—Disclosure requirements. To ensure that administrators are following the requirements of Sections 3 and 4, and to provide the state with information relevant to enforcement proceedings under Section 6, arbitration administrators are required to provide public disclosures regarding their compliance with this Title.

Section 6—Enforcement. Like Title VI, this Title is enforceable either through a public enforcement action brought by the state or by an aggrieved consumer or employee.

Section 7—Administrator's Right to Collect Fees. In recognition of the financial costs imposed on arbitration administrators that proceed with arbitrations even when the respondent does not pay fees, the Title creates a cause of action for administrators to recover fees. Not only does this section incentivize respondents to pay fees on time, but it also provides further support for the argument that this Title is not preempted. By allowing arbitration providers to recover fees, the Title implicitly signals its approval of arbitration proceedings and provides a mechanism to allow those proceedings to proceed according to the parties' agreement and the ideals of efficient and speedy dispute resolution even when the respondent has not complied with payment terms.

Analysis of Title VIII

This Title avoids any potential conflict with the FAA by regulating arbitration administrators and not arbitration agreements. On its face, a rule targeting employers and other businesses that breach the terms of their arbitration agreements by failing to pay fees in a timely fashion—and thus delaying the arbitration proceeding—would not appear to be preempted by the FAA. After all, this conduct patently contravenes the ideals of "efficient and speedy" dispute resolution protected by the FAA as set out in *Concepcion*.

However, businesses might argue that such a rule would infringe the parties' *federal* right to delegate questions regarding the conduct of the arbitration to the arbitrator.[141] In general, courts hold that even if an arbitration agreement does not expressly delegate this question to the arbitrator, it is presumptively delegated to the arbitrator. Thus, when it is not clear whether a party has actually violated the forum's rules[142] or when it appears that the arbitrator has (or will) come to its own determination of whether the party has violated the rules and what the consequences of that violation should be,[143] the court will generally defer to the arbitrator.

This Title avoids this counterargument entirely because it regulates arbitration administrators to ensure that they enforce their own rules effectively. However, nothing in this Title requires businesses to designate arbitration administrators that are subject to this Title or to specify certain arbitral rules or procedures in the arbitration agreement. Furthermore, nothing in this Title requires arbitration administrators to alter their rules. All that this Title requires is that arbitration providers *enforce* their rules according to their terms.

Furthermore, consistent with the general principle of federal law that arbitrators presumptively have the discretion to rule on matters regarding arbitral procedures, the Title allows the arbitrator either to refuse to administer an arbitration *or* to move forward with the arbitration, and to facilitate the possibility of the latter choice, provides the administrator with a meaningful mechanism to recovering fees. In this way, Title VIII not only fosters arbitration proceedings that are "efficient and speedy,"[144] but also avoids treating arbitration proceedings with disfavor relative to judicial or administrative proceedings.[145]

** David Seligman is a contributing author at the National Consumer Law Center, where he specializes in forced arbitration, and a staff attorney at Towards Justice, where he represents low-wage workers in impact litigation.* *He completed this article with the support of the National Consumer Law Center, a powerful voice for fairness in the marketplace for low-income consumers. For their insight and support, he is grateful to Jon Sheldon and Carolyn Carter—two of the country's most talented and dedicated public interest lawyers. He is also grateful for the insights of Eric Secoy of NCLC; Paul Bland of Public Justice; Jahan Sagafi of Outten & Golden LLP; and Rob Bramson of Bramson, Plutzik, Mahler, and Brikhaeuser. Thanks to Beverlie Sopiep, Jan Kruse, and Svetlana Ladan of NCLC for formatting this model law.*

1 *See, e.g.*, Public Citizen, Righting a Financial Wrong (Feb. 27, 2014), *available at* http://www.citizen.org/documents/righting-a-financial-wrong-forced-arbitration-report.pdf.

2 *See* Jessica Silver-Greenberg & Robert Gebeloff, *Arbitration Everywhere, Stacking the Deck of Justice*, The N.Y. Times, Oct. 31, 2015, *available at* http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html?_r=0.

3 Outlined below.

4 Through the collective bargaining process, unionized workers have the advantage of negotiating over an arbitration agreement.

5 In June 2015, the Yale Law School scholar Judith Resnik summarized the problem:

> The result [of recent Supreme Court decisions] has been the mass production of arbitration clauses without a mass of arbitrations. Although hundreds of millions of consumers and employees are obliged to use arbitration as their remedy, almost none do so—rendering arbitration not a vindication but an unconstitutional evisceration of statutory and common law rights. The diffusion of disputes to a range of private, unknowable alternative adjudicators also violates the constitutional protections accorded to the public—endowed with the right to observe state-empowered decision makers as they impose binding outcomes on disputants. Closed processes preclude the public from assessing the qualities of what gains the force of law and debating what law ought to require. The cumulative effect of the Supreme Court's jurisprudence on arbitration has been to produce an unconstitutional system that undermines both the legitimacy of arbitration and the functions of courts.
> It should be noted that mediation, another form of ADR, differs substantially from arbitration. A mediator attempts to facilitate an agreement between the parties, while an arbitrator actually decides the case. Mediation does not prevent the consumer from bringing an action in court.

Judith Resnik, *Diffusing Disputes: The Public in the Private of Arbitration, the Private in Courts, and the Erasure of Rights*, 124 Yale L.J. 2804 (2015)

6 David Horton & Andrea Cann Chandrasekher, *After the Revolution: An Empirical Study of Consumer Arbitration*, Georgetown L. J. Vol. 104 (forthcoming), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2614773.

7 *Hall Street Assoc. LLC v. Mattel, Inc.*, 552 U.S. 576 (2008).

8 9 U.S.C. § 2.

9 *See generally* Imre Szalai, Outsourcing Justice (2013); *see also* Paul Bland, Public Justice, Important New Book Proves Federal Arbitration Act Badly Distorted by Supreme Court (Mar. 31, 2014), *available at* http://publicjustice.net/blog/important-new-book-proves-federal-arbitration-act-badly-distorted-by-supreme-court (reviewing Professor Szalai's book).

10 15 U.S.C. § 1639c(e).

11 32 C.F.R. § 232.8.

12 Final Action Concerning Review of Interpretations of Magnuson-Moss Warranty Act; Rule Governing Disclosure of Written Consumer Product Warranty Terms and Conditions; Rule Governing Pre-Sale Availability of Written Warranty Terms; Rule Governing Informal Dispute Settlement Procedures; and Guides for the Advertising of Warranties and Guarantees, *available at* https://www.ftc.gov/system/files/documents/federal_register_notices/2015/05/150522mag-mosswarrantyfrn.pdf.

13 Medicare and Medicaid Programs; Reform of Requirements for Long-Term Care Facilities, 80 FR 42168-01

14 *See* Exec. Order No. 13,673 (2014), *available at* http://www.whitehouse.gov/the-press-office/2014/07/31/executive-order-fair-pay-and-safe-workplaces.

15 12 U.S.C. § 5518.

16 CFPB Arbitration Study at §§ 1.4.3 & 1.4.7 (For example, in 2010 and 2011, consumers of credit cards, checking accounts/debit cards, payday loans, prepaid cards, private student loans, and auto loans obtained less than $400,000 in affirmative relief from the American Arbitration Association (AAA), notwithstanding the prevalence of arbitration clauses in these industries. By comparison, between 2008 and 2012, the average annual payout for consumers from class action settlements covering financial services products—in cases where the defendants could not insulate themselves from liability with forced arbitration clauses—was more than $2 billion in cash relief, including fees and expenses, and $600 million in in-kind relief (such as debt forgiveness)).

17 Consumer Financial Protection Bureau, *Small Business Review Panel for Potential Rulemaking on Arbitration Agreements, Outline of Proposals under Consideration and Alternatives Considered*, Oct. 7, 2015, *available at* http://files.consumerfinance.gov/f/201510_cfpb_small-business-review-panel-packet-explaining-the-proposal-under-consideration.pdf ("CFPB Proposal Outline").

18 CFPB Proposal Outline at 17.

19 *Id.* (citing FINRA Rule 2268(f), which states that all agreements shall include a statement that "No person shall bring a putative or certified class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class who has not opted out of the class with respect to any claims encompassed by the putative class action until: (i) the class certification is denied; or (ii) the class is decertified; or (iii) the customer is excluded from the class by the court. Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.").

20 *Id.* at 20.

21 12 U.S.C. § 5519 (excluding most auto dealers from the CFPB's jurisdiction with the exception of dealers that routinely provide their own financing, sometimes known as "buy here pay here" dealers).

22 12 U.S.C. § 5491(a).

23 12 U.S.C. § 5518(d). Additionally, the CFPB has suggested that it may postpone the effective date until 30 days after the final rule is published, meaning that it will not cover arbitration agreements "entered into" until 210 days after publication of the regulation. *See* CFPB Proposal Outline at 22.

24 Letter to Richard Cordray, Director, Consumer Financial Protection Bureau, from sixteen state attorneys general (Nov. 19, 2014), *available at* http://www.attorneygeneral.delaware.gov/documents/20141119-AGs_Ltr_to_CFPB_re_Arb_Clauses_Final.pdf.

25 J. Maria Glover, *The Structural Role of Private Enforcement*, 53 Wm. & Mary L. Rev. 1137, 1155 (2012).

26 Richard B. Stewart & Cass Sunstein, *Public Programs & Private Rights*, 95 Harv. L. Rev. 1193, 1214 (1982) ("Public enforcement is, however, frequently inadequate because of budget constraints."); *see also* Lauren K. Saunders, National Consumer Law Center, Hold Wrongdoers Accountable to the Individuals They Harm, NCLC Issue Brief (Nov. 2009), *available at* http://www.nclc.org/images/pdf/regulatory_reform/issue-hold-wrongdoers-accountable.pdf.

27 National Consumer Law Center, Unfair and Deceptive Acts and Practices § 12.2 (8th ed. 2012), *updated at* www.nclc.org/library.

28 Michael Orey, *Wage Wars*, Bloomberg Businessweek (Sept. 30, 2007), *available at* http://www.businessweek.com/stories/2007-09-30/wage-wars.

29 National Employment Law Project, Winning Wage Justice: An Advocate's Guide to State and City Policies to Fight Wage Theft (Jan. 2011), *available at* http://www.nelp.org/page/-/Justice/2011/WinningWageJustice2011.pdf?nocdn=1.

30 CFPB Arbitration Study at § 9.1 (emphasis added).

31 *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985).

32 CFPB Arbitration Study at § 1.4.3.

33 Consumer Financial Protection Bureau, Arbitration Study Preliminary Results: Section 1028(a) Study Results to Date (Dec. 12, 2013),

available at http://files.consumerfinance.gov/f/201312_cfpb_arbitration-study-preliminary-results.pdf.
34 CFPB Arbitration Study at § 2.5.5.
35 National Association of Consumer Advocates & Public Citizen, Cases That Would Have Been: Three Years After *AT&T v. Concepcion*, Cases of Corporate Wrongdoing Continue to Pile Up (May 1, 2014), *available at* http://www.citizen.org/concepcion-third-anniversary-corporate-wrongdoing-forced-arbitration-report.
36 CFPB Arbitration Study at § 3.1.
37 Haynes v. Logan Furniture Mart, Inc., 503 F.2d 1161, 1165 (7th Cir. 1974) (noting that it is proper for a court, in deciding the "best" available method for prosecution of a claim, to consider the "inability of the poor or uninformed to enforce their rights, and the improbability that large numbers of class members would possess the initiative to litigate individually").
38 *See* Rent-A-Center West, Inc. v. Jackson, 561 U.S. 63 (2010) (parties can delegate questions of validity to the arbitrator); *see also* Duran v. J. Hass Grp., L.L.C., 531 F. Appx. 146, 147 (2d Cir. 2013) (summary order; in case against debt settlement company, compelling New York plaintiff to arbitrate in Arizona her argument that the arbitration clause's requirement that she arbitrate in Arizona was unconscionable).
39 Paul Bland, Public Justice, Bait and Switch (Mar. 24, 2014), *available at* https://www.publicjustice.net/blog/bait-and-switch-many-corporations-promise-to-pay-arbitration-fees-but-don%E2%80%99t.
40 *See* National Consumer Law Center, Consumer Arbitration Agreements Ch. 6 (7th ed. 2015), *updated at* www.nclc.org/library.
41 Steve David Solomon, *Arbitration Clauses Let American Apparel Conceal Misconduct*, The N.Y. Times, July 15, 2014, *available at* http://dealbook.nytimes.com/2014/07/15/arbitration-clauses-let-american-apparel-hide-misconduct/?_php=true&_type=blogs&_r=0.
42 *Id.*
43 Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983); Chelsea Family Pharmacy, P.L.L.C. v. Medco Health Solutions, Inc., 567 F.3d 1191, 1199 (10th Cir. 2009).
44 AT&T Mobility L.L.C v. Concepcion, 131 S. Ct. 1740 (2011).
45 THI of New Mexico at Hobbs Ctr., L.L.C. v. Patton, 741 F.3d 1162, 1169 (10th Cir. 2014); *see generally* AT&T Mobility L.L.C. v. Concepcion, 131 S. Ct. 1740, 1746 (2011).
46 *See, e.g.*, Ferguson v. Corinthian Colleges, Inc., 733 F.3d 928, 934 (9th Cir. 2013).
47 *Concepcion*, 131 S. Ct. at 1749 (internal quotation marks omitted) (quoting H.R. Rep. No. 68-96, at 2 (1924)).
48 *Id.*; Sec. Indus. Ass'n v. Connolly, 883 F.2d 1114, 1117 (1st Cir. 1989) (finding Massachusetts regulations preempted by the FAA because the "[r]egulations not only regulate; they do so in a manner patently inhospitable to arbitration. They (i) bar firms from requiring individuals to enter PDAAs as a nonnegotiable condition precedent to account relationships; (ii) order the prohibition brought "conspicuously" to the attention of prospective customers; and (iii) demand full written disclosure of "the legal effect of the pre-dispute arbitration contract or clause" (internal citations omitted)).
49 The opportunity to "opt out" of an arbitration clause is not a meaningful one. The CFPB has found that "[c]onsumers are generally unaware of any arbitration clause opt-out opportunities they may have been offered." CFPB Arbitration Study at § 1.4.2. Similarly, in assessing whether the presence of an opt-out clause precludes a finding that an arbitration agreement is procedurally unconscionable, many courts have refused to give weight to opt-out provisions which are often burdened by limitations and conditions, or which do not provide consumers with sufficient data to make an informed choice about whether to opt out..
50 Much litigation has resulted from an analogous situation where a plaintiff resists a motion to compel arbitration of a misclassification claim because she argues that the FAA does not apply to her dispute because the arbitration agreement is contained within a "contract of employment of" a transportation worker, which is excluded from the Federal Arbitration Act. 9 U.S.C. § 1; *see also* Title V, *infra.* The definition of employee avoids such unnecessary litigation.
51 PAGA is further described in Professor Janet Cooper Alexander's 2013 article, *To Skin a Cat:* Qui Tam *Actions As a State Legislative Response to Concepcion*, 26 U. Mich. J. L. Reform 1203 (2013), which advocates that states enact a provision similar to the model statute's Title I.
52 J. Randy Beck, *The False Claims Act and the English Eradication of* Qui Tam *Legislation*, 78 N.C. L. Rev. 539, 552 (2000).
53 *See, e.g.*, *Nanavati v. Adecco USA, Inc.,* No. 14-CV-04145-BLF, 2015 WL 1738152, at *8 (N.D. Cal. Apr. 13, 2015) ("As a dispute that is, at its core, between private parties, the terms of their arbitration agreement control.").
54 Notwithstanding the "representative" nature of PAGA actions, they are not "class actions" subject to federal jurisdiction under the Class Action Fairness Act ("CAFA"), 28 U.S.C. § 1332(d)(2)–(A), because, among other things, they do not bind "absent," "represented" employees with respect to their right to seek other remedies available under federal or state law. *See Bauman v. Chase Inv. Services Corp.*, 747 F.3d 1117 (9th Cir. 2014), *cert. denied,* 135 S. Ct. 870 (2014).
55 U.S. ex rel. Summit v. Michael Baker Corp., 40 F. Supp. 2d 772, 774 (E.D. Va. 1999) ("[T]he danger of granting the relator the power to decide settlements in a qui tam case is that the case may present a relator who manipulates the settlements in ways that unfairly enrich them and reduce the benefits of the Government.").
56 31 U.S.C. §§ 3729–3733.
57 Cal. Lab. Code § 2699(a) (West).
58 Iskanian v. CLS Transp. Los Angeles, L.L.C., 206 Cal. App. 4th 949 (2012), *aff'd*, 327 P.3d 129 (Cal. 2014).
59 *See* Section B of the Title I analysis.
60 327 P.3d 129 (Cal. 2014).
61 *See, e.g.*, Chico v. Hilton Worldwide, Inc., 2014 WL 5088240, at *12 (C.D. Cal. Oct. 7, 2014); Ortiz v. Hobby Lobby Stores, Inc., 2014 WL 4961126 (E.D. Cal. Oct. 1, 2014); Fardig v. Hobby Lobby Stores Inc., 2014 WL 2810025 (C.D. Cal. June 13, 2014). *But see* Hernandez v. DMSI Staffing, L.L.C., 2015 WL 458083, at *1 (N.D. Cal. Feb. 3, 2015) (agreeing with *Iskanian*'s approach).
62 CLS Transp. Los Angeles, L.L.C. v. Iskanian, 2015 WL 231976 (U.S. Jan. 20, 2015); *see also* Petition for Writ of *Certiorari*, *CLS Transp. Los Angeles, L.L.C. v. Iskanian,* No. 14-1341 (U.S. Sept. 22, 2014) .
63 Sakkab v. Luxottica Retail N. Am., Inc., 803 F.3d 425 (9th Cir. 2015).
64 *Sakkab*. 803 F.3d at 444 (9th Cir. 2015) (Smith, *J.* dissenting).
65 Iskanian v. CLS Transp. Los Angeles, L.L.C., 327 P.3d 129, 148 (Cal. 2014) (citing Cal. Civ. Code § 3513 (West) ("[A] law established for a public reason cannot be contravened by private agreement.")).
66 *Id.* at 148–152.
67 *Id.* at 150 (internal quotation marks omitted) (quoting 9 U.S.C. § 2).
68 *See, e.g.*, Ferguson v. Corinthian Colleges, Inc., 733 F.3d 928, 936 (9th Cir. 2013) ("States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons." (internal quotation marks omitted)).
69 534 U.S. 279 (2002).
70 *Waffle House*, 534 U.S. at 294.
71 *Iskanian*, 327 P.3d at 150.
72 The California Supreme Court also contended with the argument that PAGA violates state separation-of-powers laws by authorizing "financially interested private citizens to prosecute claims on the state's behalf without governmental supervision." *Iskanian*, 327 P.3d at 153. The Court rejected this argument, reasoning that the rule prohibiting government contingent-fee arrangements with private attorneys in narrow sets of circumstances simply requires government entities to supervise the attorneys they choose to hire to pursue actions. By contrast, a rule disallowing *qui tam* actions would significantly interfere with a legitimate exercise of legislative authority aimed at accomplishing the important

public purpose of augmenting scarce government resources for civil prosecutions. *Id.* at 154.

73 Vermont Agency of Natural Resources v. United States ex rel. Stevens, 529 U.S. 765, 774 (2000).

74 Mikes v. Strauss, 889 F. Supp. 746, 754 (S.D.N.Y. 1995). Many courts hold that employee-whistleblowers' FCA retaliation claims (*i.e.*, claims brought by the employee against the employer for retaliating against the employee for serving as a whistleblower under the FCA) are subject to arbitration clauses in employment agreements. *See, e.g.*, United States ex rel Conyers v. Kellogg, Brown & Root, Inc., No. 412CV04095SLDJEH, 2015 WL 1510544, at *13 (C.D. Ill. Mar. 30, 2015). In contrast to public FCA claims brought on behalf of the federal government, however, these claims are private claims brought by the employee in her individual capacity to redress a private wrong.

75 *Waffle House*, 534 U.S. at 298.

76 *See, e.g.*, Nanavati v. Adecco USA, Inc., No. 14-CV-04145-BLF, 2015 WL 1738152, at *8 (N.D. Cal. Apr. 13, 2015) (citing the absence of these features in PAGA as a reason to conclude that California does not control PAGA litigation).

77 PAGA's requirement that a party be an "aggrieved" employee in order to bring an action is one of the bases upon which the respondent and *amici* urged review by the Supreme Court. Brief of the Employers Group & Cal. Employment Law Council as *Amici Curiae* in Support of the Petition for Writ of *Certiorari*, *CLS Transp. Los Angeles, L.L.C. v. Iskanian,* No. 14-1341 (U.S. Sept. 22, 2014).

78 *See generally* David B. Wilkins*, Rethinking the Public-Private Distinction in Legal Ethics: The Case of "Substitute" Attorneys General*, 2010 Mich. St. L. Rev. 423, 428. Many state courts and legislatures have expressly endorsed this practice. *See id.* at 434–435.

79 *See* Eric Lipton, *Lawyers Create Big Paydays by Coaxing Attorneys General to Sue*, N.Y. Times, Dec. 18, 2014, *available at* http://www.nytimes.com/2014/12/19/us/politics/lawyers-create-big-paydays-by-coaxing-attorneys-general-to-sue-.html?_r=0.

80 *Concepcion*, 131 S. Ct. at 1751.

81 *Sakkab*, 803 F.3d at 436.

82 *See id.* (noting the same differences between PAGA and class claims under Federal Rule of Civil Procedure 23).

83 *Id.* at 446 (Smith, *J.* dissenting).

84 *See, e.g.*, Wisconsin Dep't of Indus., Labor & Human Relations v. Gould Inc., 475 U.S. 282, 290 (1986) (concluding that a state cannot avoid federal labor law preemption merely by virtue of acting pursuant to its spending as opposed to its regulatory powers); *cf. Dolan v. City of Tigard*, 512 U.S. 374, 386 (1994) (explaining that the government can only impose an otherwise unconstitutional condition on the receipt of government funds when there is an "essential nexus" between the government interest in this condition and the government's expense of the funds).

85 White v. Mass. Council of Constr. Employers, 460 U.S. 204 (1983).

86 *See* Exec. Order No. 13,673 (2014), *available at* http://www.whitehouse.gov/the-press-office/2014/07/31/executive-order-fair-pay-and-safe-workplaces.

87 Bldg. & Constr. Trades Dep't, AFL-CIO v. Allbaugh, 295 F.3d 28, 31 (D.C. Cir. 2002).

88 *See generally* Michael Burger, *It Ain't Easy Being Green*, 78 U. Cin. L. Rev. 835 (2010).

89 Hillerby v. Town of Colchester, 167 Vt. 270, 272 (1997) (explaining the doctrine and noting that many states have replaced it with governmental "tort claims" acts).

90 As explained by the Supreme Court, the "market participant" exception to the Dormant Commerce Clause allows for states to "operate freely in the free market." For example, in *White v. Massachusetts Council of Construction Employers, Inc.*, the Supreme Court upheld an executive order of the Mayor of Boston that required all construction projects funded by the city to employ a workforce made up of at least half Boston residents. 460 U.S. 204 (1983). Although the city would otherwise be unable to require private construction firms to hire mainly city residents, the Court reasoned that Boston was free to discriminate against non-residents with regard to the makeup of employees working on projects funded by the city, as such conduct constituted "direct state participation in the market," and amounted, effectively, to a decision on the part of the city regarding the makeup of its own employees. *Id.* at 207 (internal quotation marks omitted).

91 In the labor law context, the seminal case on the issue is Building & Construction Trades Council of Metropolitan District v. Associated Builders & Contractors of Massachusetts/Rhode Island, Inc. ("Boston Harbor"), 507 U.S. 218 (1993), where the Supreme Court concluded that Massachusetts could require contractors working on the Boston Harbor project to enter into pre-recognition labor-management agreements. Although a state requirement that private parties enter into these agreements with each other would clearly be preempted, Massachusetts could enact the rule as a "market participant" because it had a legitimate interest in ensuring labor peace on government construction projects. *Id.* at 230.

Subsequent cases have clarified this exception. In *Chamber of Commerce of U.S. v. Brown*, the Supreme Court confronted a California statute that prohibited employers from using funds received by the government to assist or deter union organizing—a normally common practice in the lead-up to a union certification election. Notwithstanding that the law solely affected the use of government funds, the Court deemed it preempted. To survive preemption under the "market participant" exception, the Court stated, state action had to be "specifically tailored to one particular job," and aimed "to ensure an efficient project that would be completed as quickly and effectively as possible at the lowest cost." 554 U.S. 60, 70 (2008) (internal quotation marks omitted).

The Supreme Court has also examined whether the "market participant" rule protects a state's decision to refuse to do business with companies that have repeatedly violated federal law labor, finding that the provision was preempted because its purpose was to amplify the punishment already provided under federal law for violating the National Labor Relations Act. Wisconsin Dep't of Indus., Labor & Human Relations v. Gould, Inc., 475 U.S. 282 (1986). Nonetheless, the Clean Air Act did not preempt California provisions directing state and local governments to procure vehicles that exceeded its standards. Engine Mfrs. Ass'n v. S. Coast Air Quality Mgmt. Dist., 498 F.3d 1031 (9th Cir. 2007) (California "provisions directing state and local governments to purchase, procure, lease, and contract for use of vehicles meeting certain criteria [exceeding the Clean Air Act] [amounted to] proprietary state action because they essentially reflect[ed] California's own interest in its efficient procurement of needed goods and services"). *See also* Johnson v. Rancho Santiago Cmty. Coll. Dist., 623 F.3d 1011, 1025–1026 (9th Cir. 2010) (school district's "Project Stabilization Agreement" was permissible market participant conduct that, therefore, was not preempted by ERISA or the NLRA).

92 Dan T. Coenen, *Untangling the Market-Participant Exemption to the Dormant Commerce Clause*, 88 Mich. L. Rev. 395, 398 (1989)

93 *Id.*

94 *See, e.g.*, New York Bankers Ass'n, Inc. v. City of New York, 2015 WL 4726880, at *24 (S.D.N.Y. Aug. 7, 2015) ("What is obvious from the text is confirmed by the legislative history. The legislators who sponsored and who spoke in support of this bill did so with one voice: federal and state laws were seen as ineffectual in terms of both the collection of information and the influence over bank conduct regarding community reinvestment in New York City.").

95 Hotel Employees & Restaurant Employees Union Local 57 v. Sage Hospitality Res., L.L.C., 390 F.3d 206, 216 (3d Cir. 2004).

96 Cardinal Towing & Auto Repair, Inc. v. City of Bedford, 180 F.3d 686, 693 (5th Cir. 1999). *See also* Mich. Bldg. & Constr. Trades Council v. Snyder, 729 F.3d 572 (8th Cir. 2013) ("[T]o be proprietary, the government action must be aimed to achieve a proprietary goal and must be limited to the furtherance of that goal.").

97 Echoes of this approach can be traced back to the Supreme Court's decision in *Boston Harbor*. What made that case different from *Gould*, according to the Court, was that the Massachusetts Bay Water Authority required its contractor to enter into a pre-certification agreement "to ensure an efficient project that would be completed as quickly and effectively as possible at the lowest cost," and not to regulate the contractor's conduct outside of the contracting relationship. *Boston Harbor*, 507 U.S. at 232.

98 Bldg. & Constr. Trades Dep't, AFL-CIO v. Allbaugh, 295 F.3d 28, 35 (D.C. Cir. 2002) ("[T]he Government unquestionably is the proprietor of its own funds, and when it acts to ensure the most effective use of those funds, it is acting in a proprietary capacity. Second, that the Government is a lender to or a benefactor of, rather than the owner of, a project is not inconsistent with its acting just as would a private entity; a private lender or benefactor also would be concerned that its financial backing be used efficiently. In sum, the distinction between federally owned and federally funded projects is not relevant here.").

99 Johnson v. Rancho Santiago Cmty. Coll. Dist., 623 F.3d 623 F.3d 1011, 1025 (9th Cir. 2010).

100 *Id. See also* Mich. Bldg. & Constr. Trade Council, 729 F.3d at 580.

101 *Allbaugh*, 295 F.3d at 33 (internal quotation marks and alterations omitted).

102 Jeff Sovern, *Arbitration Clauses Trap Consumers with Fine Print*, Am. Banker, Dec. 2, 2014, *available at* http://www.americanbanker.com/bankthink/arbitration-clauses-trap-consumers-with-fine-print-1071436-1.html.

103 Basulto v. Hialeah Auto*.*, 141 So. 3d 1145 (Fla. 2014) (trial court's fact-bound inquiry finding that the parties never formed a contract because, *inter alia*, neither salespeople nor plaintiff understood arbitration clause was not clearly erroneous); Baker v. Bristol Care, Inc., 2014 WL 4086378 (Mo. Aug. 19, 2014) (concluding, *inter alia*, that unilateral right to amend contract within thirty days rendered contract containing arbitration clause illusory); State ex rel. U-Haul Co. of W. Va. v. Zakaib, 752 S.E.2d 586 (W. Va. 2013) (reference to a contract addendum in a clickwrap agreement was insufficient to bind consumers to such addendum arriving in hard copy in a non-descript envelope).

104 As discussed above and at length in NCLC's *Consumer Arbitration Agreements*, state laws regarding the mechanisms of contract formation generally survive FAA preemption as long as they do not specifically target arbitration. National Consumer Law Center, Consumer Arbitration Agreements Ch. 5 (7th ed. 2015), *updated at* www.nclc.org/library. For example, although a state rule providing that "[n]otice that a contract is subject to arbitration . . . shall be typed in underlined capital letters on the first page of the contract" applies to the question of contract formation, it is preempted by the FAA. Doctor's Associates, Inc. v. Casarotto, 517 U.S. 681 (1996)

105 Altalese v. U.S. Legal Servs. Grp., L.P., 2014 WL 4689318 (N.J. Sept. 23, 2014).

106 Larkin v. New Century Auto Sales Inc., 2014 WL 29119 (E.D. Mich. Jan. 3, 2014).

107 *See, e.g.*, *id*.

108 9 U.S.C. § 2.

109 319 F.3d 1126, 1147 (9th Cir. 2003).

110 *Id.* at 1149.

111 Sakkab v. Luxottica Retail N. Am., Inc., 803 F.3d 425, 432-33 (9th Cir. 2015) (some internal citations omitted).

112 *See, e.g.*, Arthur Alan Leff, *Unconscionability and the Code—the Emperor's New Clause*, 115 U. Pa. L. Rev. 485, 487 (1967) (describing the distinction between procedural and substantive unconscionability); *see also* National Consumer Law Center, Consumer Arbitration Agreements § 6.4 (7th ed. 2015), *updated at* www.nclc.org/library (describing the relationship between procedural and substantive unconscionability).

113 *See* National Consumer Law Center, Consumer Arbitration Agreements § 6.8.3 (7th ed. 2015), *updated at* www.nclc.org/library.

114 Winston v. Academi Training Ctr., Inc., 2013 WL 989999, at *3 (E.D. Va. Mar. 13, 2013).

115 *See generally* National Consumer Law Center, Unfair and Deceptive Acts and Practices Ch. 4 (8th ed. 2012), *updated at* www.nclc.org/library; *see also De la Torre v. CashCall, Inc.,* --- F.Supp.2d ----, 2014 WL 3752796, at *3 (N.D. Cal. July 30, 2014), *vacated on other grounds*, 2014 WL 5390259 (N.D. Cal. Oct. 21, 2014).

116 Felix v. Ganley Chevrolet, Inc., 2015-Ohio-3430, ¶ 31, 2015 WL 5039233 (Ohio Aug. 27, 2015) (concluding that UDAP claims based on unconscionable arbitration clause did not support award of damages to class because plaintiffs could not establish actual damages).

117 Harvard Translations, Inc. v. Heuberger, No. CIV.A. 99-0682F, 1999 WL 967569, at *1 (Mass. Super. Sept. 9, 1999) ("Under Massachusetts case law, disputes between employers and employees are not actionable under [the Commonwealth's UDAP protections].").

118 *Concepcion*, 131 S. Ct. 1749 (2011).

119 For an extensive discussion of the doctrine, see National Consumer Law Center, Consumer Arbitration Agreements Ch. 6 (7th ed. 2015), *updated at* www.nclc.org/library.

120 Marmet Health Care Ctr., Inc. v. Brown, 132 S. Ct. 1201, 1204 (2012) (reaffirming, post-*Concepcion*, the viability of "state common law principles that are not specific to arbitration and pre-empted by the FAA").

121 311 P.3d 184 (Cal. 2013) *cert. denied*, 134 S. Ct. 2724 (2014).

122 *Id.* at 203.

123 *See, e.g.*, MHN Gov't Servs. Inc. v. Zaborowski, Pet. for Writ of *Certiorari*, No. 14-1458 (2015), *available at* http://www.scotusblog.com/wp-content/uploads/2015/08/cert-pet-as-filed.pdf.

124 Cordova v. World Fin. Corp. of N.M., 208 P.3d 901, 911 (N.M. 2009) (recognizing that courts cannot perform "judicial surgery" to excise an unenforceable term). The question of whether an unenforceable term within an arbitration clause is a question of state law that turns on the traditional factors that apply to the question whether an unenforceable term can be severed from an agreement. This question should not be confused, however, with the question whether an arbitration clause is severable from an unenforceable and illegal contract. The United States Supreme Court has concluded that the latter question is one of federal law. *See* Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440 (2006) (arbitration clause is severable from illegal contract such that an attack on the legality of the contract as a whole does not bear on the enforceability of the arbitration clause in particular).

125 National Consumer Law Center, Unfair and Deceptive Acts and Practices Ch. 4 (8th ed. 2012), *updated at* www.nclc.org/library.

126 9 U.S.C. § 1; *see also Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001).

127 *See, e.g.*, Ferguson v. Corinthian Colleges, Inc., 733 F.3d 928, 934 (9th Cir. 2013).

128 15 U.S.C. § 1012(b).

129 *See* National Consumer Law Center, Consumer Arbitration Agreements § 3.3.4 (7th ed. 2015), *updated at* www.nclc.org/library.

130 *See, e.g.*, Standard Sec. Life Ins. Co. of N.Y. v. West, 267 F.3d 821 (8th Cir. 2001) (Missouri statute providing for enforceability of arbitration clauses in written contracts except for contracts of insurance was not preempted by the FAA); *Stephens v. Am. Int'l Ins. Co.*, 66 F.3d 41 (2d Cir. 1995) (FAA did not preempt Kentucky statute limiting enforceability of arbitration clauses in cases related to insurance premium delinquency actions); *Mut. Reinsurance Bureau v. Great Plains Mut. Ins. Co.*, 969 F.2d 931 (10th Cir. 1992) (FAA did not preempt aspect of Kansas Arbitration Act providing that arbitration clauses are enforceable other than those contained in contracts for insurance); Balaban-Zilke v. Cigna Healthcare of Cal., Inc., 2003 WL 21228038 (Cal. Ct. App. May 28, 2003) (FAA did not preempt arbitration-related regulations involving contracts for health care service plans); Allen v. Pacheco, 2003 WL 21310267 (Colo. June 9, 2003) (FAA did not preempt specific disclosure requirements related to arbitration clauses in medical service agreements); Cont'l Ins.

Co. v. Equity Residential Properties Trust, 565 S.E.2d 603 (Ga. App. 2002) (FAA did not preempt Georgia Arbitration Act provision providing for the enforcement of written arbitration clauses except for arbitration clauses in insurance agreements).
131 9 U.S.C. § 1.
132 Circuit City Stores, Inc. v. Adams, 532 U.S. 105 (2001).
133 *See, e.g.*, Palcko v. Airborne Express, Inc., 372 F.3d 588, 597–598 (3d Cir. 2004).
134 *See* Volt Info. Sciences, Inc. v. Bd. of Trustees, 489 U.S. 468 (1989).
135 *See* National Consumer Law Center, Consumer Arbitration Agreements § 3.3.2 (7th ed. 2015), *updated at* www.nclc.org/library.
136 Cal. Code Civ. Proc. §§ 1281.9, 1281.92, 1281.96, 1284.3 (West).
137 Carolyn Said, *Affordable Legal Solution*, San. Fran. Chron., Jan. 12, 2014 (explaining the problems with the absence of such a provision in California's law).
138 *See* Volt Info. Sciences, Inc. v. Bd. of Trustees, 489 U.S. 468 (1989).
139 *See* Wells v. Chevy Chase Bank, 768 A.2d 620, 627 (Md. 2001) (collecting cases and observing that "[m]ost state courts which have faced the issue of whether the FAA prevented appeal of an order compelling arbitration hold that their own procedural rules govern appeals, unless those rules undermine the goals and principles of the FAA, and then those courts find that their procedural rules do not impermissibly undermine the objectives of the FAA"); *see also* National Consumer Law Center, Consumer Arbitration Agreements § 2.6.4 (7th ed. 2015), *updated at* www.nclc.org/library.
140 An attorney who represents consumers bringing claims against predatory auto dealers and lenders recounted the following story about the American Arbitration Association's (AAA) failure to follow its own rules requiring the business to pay fees in a timely manner and refusing to administer an arbitration if the arbitration clause is not registered with AAA. *See* American Arbitration Association, Consumer Arbitration Rules, R-12, *available at* https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTAGE2021425&revision=latestreleased.

> We filed a YoYo car sale case against a car dealer where dealer kept the down payment and repo'd the car. Car dealer hires a known automobile dealer defense firm who for the first time provides my client with a copy the arbitration agreement she signed right before discovery is due. I don't think we can win against it, so I call the other attorney and we agree to file a joint motion to stay the case compel arbitration to save time rather than waiting two months for a hearing date that I know I will lose. It is with AAA, so I file under the consumer rules. AAA takes approximately 90 days before contacting the dealer. Car dealer has not had the arbitration agreement previously approved with AAA and does not pay the fees so case gets dismissed—another couple of months. We file a motion with the Court to lift the stay and deem arbitration waived. Court sets it for a hearing a month and a half out. Shortly before hearing, dealer pays the $250.00 to get AAA to approve the Arbitration and gets a letter from them saying they will now agree to hear cases involving the dealer. Court denies our motion and makes us start over from the beginning after almost a Year has passed!

Email to David Seligman, Oct. 29, 2015 (on file with author).
141 Rent-A-Center, West, Inc. v. Jackson, 561 U.S. 63 (2010).
142 *See* Pro Tech Indus., Inc. v. URS Corp., 377 F.3d 868, 872 (8th Cir. 2004) (whether party waived right to arbitrate by making an untimely request for arbitration under the arbitration agreement was for the arbitrator to decide, because "arbitrators are the experts about the meaning of their own rules, and are comparatively better able to interpret and apply them than courts"); RMES Communications, Inc. v. Qwest Bus. Gov't Services, Inc., 2006 WL 1183173 (D. Colo. May 2, 2006) (whether party's pre-litigation activity waived right to arbitrate was for arbitrator to decide); Omar v. Ralphs Grocery Co., 13 Cal. Rptr. 3d 562, 568 (Ct. App. 2004) ("[W]here the delay is unrelated to the litigation process, it is improper for the judge to decide this issue." (citation omitted)).
143 Lifescan, Inc. v. Premier Diabetic Services, Inc., 363 F.3d 1010 (9th Cir. 2004).
144 Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213, 221 (1985).
145 AT&T Mobility L.L.C v. Concepcion, 131 S. Ct. 1740 (2011).

APPENDIX
MODEL TEXT WITHOUT COMMENTARY

NATIONAL CONSUMER LAW CENTER'S MODEL STATE CONSUMER & EMPLOYEE JUSTICE ENFORCEMENT ACT

DEFINITION OF TERMS

[*Note*: States will likely need to define other terms used throughout the Act (including, for example, "consumer"), but because many states already include such definitions in their employee and consumer protection statutes, the Model Act does not provide such definitions here. Furthermore, some terms used throughout the Act will be inappropriate for certain states' statutory schemes. As just one example, the term "civil penalties" might not be appropriate in some states that impose "fines" or "sanctions."]

Forced arbitration agreement is an agreement to subject disputes between the parties to a binding dispute resolution procedure separate from federal or state judicial or administrative process if such agreement (1) is a condition of entering into a relationship with the party that presented the agreement or is presented in such a way that a reasonable person would consider it to be a condition of entering into a relationship with the party that presented it; and (2) was not negotiated by a labor union through collective bargaining; pursuant to this definition, for a consumer and employment contract an arbitration agreement is a "condition of entering into a relationship" with a business if the business retaliates against the consumer or employee for failing to assent to the agreement or if the consumer or employee reasonably fears that the business would retaliate against the consumer or employee for failing to assent to the agreement. The right to "opt-out" of the agreement at a later time does not affect or alter the agreement's status as a "forced arbitration agreement."

Employee is, for the purpose of this Act, any person employed by another as defined by state law, and any person who is not classified by a business as an employee but who claims to be an employee and whose claims against the purported employer relate to this alleged misclassification.

TITLE I: DELEGATION OF STATE ENFORCEMENT AUTHORITY

Section 1. Findings.
Limits on the availability of public enforcement resources have deleterious effects on the marketplace by allowing abuses targeting consumers and workers to persist unprosecuted. To ensure the robust enforcement of [*designated State consumer and worker protection statutes*], while simultaneously minimizing the outlay of scarce State funds, this Title provides for private attorneys general to represent the State's enforcement interests in certain contexts in which the State does not have the means to enforce fully state consumer and worker protections.

Section 2. Civil penalties.
Unless State law provides a different amount as the civil penalty recoverable by the State for violations of [*designated State consumer and worker protection statutes*], a person who commits a violation of such State consumer or worker protection laws shall be subject to a civil penalty not to exceed $5,000 per violation.

Section 3. Private attorney general suits:

- **(a)** A person may initiate on behalf of the State an action alleging violations of [*designated State consumer and worker protection statutes*] to recover civil penalties on behalf of the State and to seek injunctive, declaratory, or other equitable relief that the State would itself be entitled to seek;
- **(b)** In initiating an action under this Title, a person may allege multiple violations that have affected different consumers or employees, as long as those violations are of a sufficiently similar kind that they can be efficiently managed in a single action;
- **(c)** For the purpose of encouraging the enforcement of public protections, a court may award a person who initiates a claim under this Title an incentive award of up to twenty-five (25) percent of the total monetary recovery if that person pursues the action to final judgment as the prevailing party, or up to ten (10) percent of the total recovery if the state intervenes in the action and pursues it to final judgment as the prevailing party, including after settlement. In deciding an appropriate incentive award, a court shall consider the complexity of the case, the resources dedicated to prosecuting the case, whether the private attorney general obtained equitable relief on behalf of the state, and the extent of such relief, and the importance of the case as measured by the extent of actual damages caused by the wrongdoing to consumers or employees; and
- **(d)** When a private attorney general or the State prevails in an action originally brought under this Title, the private attorney general and the State each shall be entitled to attorney fees and costs, as reasonable based on their participation in the action.

Section 4. State's opportunity to intervene and proceed with the action.
A person initiating an action under this Title shall serve a copy of the complaint and a letter describing the action on the State Attorney General, at which point the action shall be stayed for thirty (30) days. The State may intervene in the action and proceed with any and all claims in the action:

- **(a)** As of right within the thirty-day stay; or
- **(b)** For good cause, as determined by the court, after the expiration of the thirty-day stay.

Section 5. Discovery.
Whether or not the State proceeds with the action, upon a showing by the State that certain actions of discovery by the person initiating the action would interfere with the State's investigation or prosecution of a criminal or civil matter arising out of the same facts, the court

may stay such discovery for a period of not more than 60 days. Such a showing shall be conducted *in camera*. The court may extend the 60-day period upon a further showing in camera that the State has pursued the criminal or civil investigation or proceedings with reasonable diligence and any proposed discovery in the action will interfere with the ongoing criminal or civil investigation or proceedings.

Section 6. Prohibition of duplicative actions.
No action may be brought by a private party acting pursuant to this Title for any violations already alleged as the basis for an action brought by the State, or by another private party pursuant to this Title, and no action may be brought by the State for any violations already alleged as the basis for an action brought by a private party pursuant to this Title. Furthermore, when a person initiates an action under this Title, no person other than the State may intervene or bring a related action under this Title based on the facts underlying the pending action.

Section 7. Settlement.
The court in which the action is filed shall review and approve any proposed settlement of an action brought under this Title to ensure that the settlement provisions are reasonable in light of State law. The court shall also ensure that any incentive fees and attorney fees or costs included in a settlement are reasonable and that the private attorney general does not recover, as an incentive payment, more than twenty-five (25) percent of the recovery remitted to the State under the proposed settlement. The proposed settlement shall be submitted to the State Attorney General at the same time that it is submitted to the court. If the State Attorney General opposes the settlement and expresses such opposition by filing a motion with the Court, the Court must decline approval of the settlement.

Section 8. Limitations on State actions initiated by a private party.

- **(a)** The State may dismiss any action in which it decides to intervene under Section 4 of this Title notwithstanding the objections of the person who initiated the action.
- **(b)** The State may settle any action in which it decides to intervene under Section 4 of this Title notwithstanding the objections of the person who initiated the action.

Section 9. Res judicata.
Notwithstanding any other provision of law, an action initiated by a private person under this Title shall not bar that person or any other individual from filing a private action based on the same nucleus of operative facts, nor shall a prior private action based on the same nucleus of operative facts bar an action under this Title.

Section 10. Relationship to forced arbitration.
Actions under this Title are prosecuted on behalf of the State and not an individual, and forced arbitration agreements between private parties do not apply to actions under this Title. No contract shall waive or limit a private party's right to act as a private attorney general under this Title by waiving that party's right to bring such an action in a public forum or by preventing the party from being able to bring an action alleging multiple violations committed against multiple consumers or employees pursuant to Section 3(b) of this Title.

Section 11. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

TITLE II: CONDITIONS ON PERSONS DOING BUSINESS WITH THE STATE

Section 1. Findings.
To ensure that the State spends its limited funds in the most efficient manner possible, this Title prohibits the State from doing business with persons that form or enforce forced arbitration agreements with their consumers or employees. The secret nature of forced arbitration agreements between persons doing business with the State and their consumers or employees undermines the efficient management of State funds in the following ways:

- **(a)** It prevents the State from learning whether goods or services provided by persons doing business with the State are the subject of consumer grievances concerning the quality of the good or service or whether the employees producing such goods or providing such services complain of unfair and illegal treatment that might interfere with the quality of the good or service;
- **(b)** It obscures the extent to which persons doing business with the State violate the legal rights of their consumers or employees, and therefore whether such persons are breaching their obligations to the State or concealing from public scrutiny conduct that interferes with the quality of a good or service provided to the State; and
- **(c)** It obscures the extent to which persons doing business with the State might be destabilized by the person's conduct as to consumers or its employees—such destabilization increases the likelihood that such person will defraud the State or be unable to perform under a contract with the State.

Section 2. Definition of "doing business with the State."
A person "does business with the State" when it or any of its subsidiaries or parent entities receives State funds exceeding $100,000 in exchange for goods or services provided to the State or a third party. Persons "doing business with the State" include but are not limited to persons performing public work on State contracts, merchants of goods or services purchased by the State, and persons providing services to third parties in exchange for funds provided directly from the State.

Section 3. Prohibition against the State doing business with persons that form or enforce forced arbitration agreements.
(a) The State shall not do business with any person or any of its parent entities or subsidiaries if that person includes forced arbitration clauses in any of its contracts with consumers or employees, unless one-hundred-eighty (180) days before doing business with the State, the person or its parent entity or subsidiary provides reasonable notice to its consumers or employees that it will cease enforcing arbitration clauses in consumer or employment contracts if such clauses exist in consumer or employment contracts.
(b) The State shall not do business with any person or any of its parent entities or subsidiaries if that person or any of its parent entities or subsidiaries enforces forced arbitration agreements against any of its employees or consumers.

Section 4. Enforcement.
(a) Before doing business with any person, the State agency representing the State in the business relationship shall confirm that such person, its parent entities, and its subsidiaries do not form or enforce forced arbitration agreements with consumers or employees and shall ensure, when appropriate, that a contract between the State and the person includes a provision prohibiting that person, its parent entities, and its subsidiaries from forming or enforcing forced arbitration agreements. Under this provision, a person or its parent entities or subsidiaries forms forced arbitration clauses in its contracts with consumers or employees if current contracts with consumers or employees include forced arbitration clauses, unless, one-hundred-eighty (180) days before doing business with the State, the person or its parent entity or subsidiary provides reasonable notice to its consumers or employees that it will cease enforcing arbitration clauses in consumer or employment contracts.
(b) If the State Attorney General, after giving a person doing business with the State notice and an opportunity to be heard, concludes that such person has violated the provisions of Section 3, the State Attorney General shall notify all State agencies doing business with the person about the violation and can seek actual damages owed to the State caused by such violation.
(c) If a State agency receives notice from the State Attorney General that a person with whom the agency does business has violated the provisions of Section 3, the agency shall terminate its business dealings with such person as soon as practical.

Section 5. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

TITLE III: CLEAR NOTICE AND SINGLE DOCUMENT RULE

Section 1. Findings.
Obscure and overly complex language in consumer and employment contracts interferes with employees' and consumers' ability to provide meaningful assent to their consumer and employment contracts. To ensure that private parties comprehend the material terms of the consumer and employment contracts into which they enter, this Title requires that merchants and employers in designated forms of contracts adequately disclose terms and condition.

Section 2. Coverage.
This Title applies to contracts of the categories set out in Section 3 formed after this Title's effective date that meet any one of the following three criteria:
(a) An employment or consumer contract not written in plain language that an average consumer or employee would understand;
(b) An employment or consumer contract not written in the language in which the transaction was conducted, unless it can be proven that fewer than ten percent (10%) of the entity's transactions are conducted in that language; or
(c) If a consumer contract, all of the material terms are not found in a single document.

Section 3. Categories of contracts covered.
[*TO BE FILLED IN BY EACH STATE*]

Section 4. Rights when a covered contract is non-conforming.
A consumer or employee may seek a court order reforming any contract covered by Section 2. Such reformed agreement shall reflect the understanding of the parties, and the court may exclude terms not written in plain English, not written in the language in which the transaction was conducted, or found in a separate document.

Section 5. Pre-existing rules.
This Title shall be applied in conjunction with pre-existing rules regarding contract formation, including rules regarding reasonable notice and the conduct a consumer or employee must manifest in order to assent to an agreement.

TITLE IV: UNCONSCIONABLE TERMS IN STANDARD FORM CONTRACTS

Section 1. Findings.
The inclusion of unconscionable terms in standard form contracts regarding dispute resolution is unfair not only because any resulting dispute resolution proceeding is unfair to the party forced to agree to the unconscionable terms, but also because the unconscionable terms discourage valid claims. Furthermore, when the provisions are challenged, courts may simply strike the unconscionable terms but enforce the remainder of the agreement regarding dispute resolution. As a result, businesses have little incentive not to include these terms. Furthermore, because this Title governs form contracts, it is unlikely that there is any meeting of the minds over a dispute-resolution agreement that does not include severed unconscionable terms.

Section 2. Unconscionable terms.
There is a rebuttable presumption that the following contractual terms are substantively unconscionable when included in a standard form contract to which only one of the parties to the contract is an individual and that individual does not draft the contract:
(a) A requirement that resolution of legal claims take place in an inconvenient venue. An inconvenient venue is defined for State law claims as a place other than the county where the individual resides or the contract was consummated, and for federal law claims as a place other than the federal judicial district where the individual resides or the contract was consummated;
(b) A waiver of the individual's right to assert claims or seek remedies provided by State or federal statute;
(c) A waiver of the individual's right to seek punitive damages as provided by law;
(d) A requirement that the individual bring an action prior to the expiration of the applicable statute of limitations;
(e) A requirement that the individual pay fees and costs to bring a legal claim substantially in excess of the fees and costs that this State's courts require to bring such a State law claim or that federal courts require to bring such a federal law claim.

Section 3. Relation to common law and the Uniform Commercial Code.
In determining whether the terms described in Section 2 are unenforceable, a court shall consider the principles that normally guide courts in this State in determining whether unconscionable terms are enforceable. Additionally, the common law and Uniform Commercial Code shall guide courts in determining the enforceability of unfair terms not specifically identified in Section 2.

Section 4. Severability.
There is a rebuttable presumption that unconscionable terms in form contracts are not severable from the agreements in which they are situated, thus rendering the entire agreement unenforceable. In determining whether this presumption has been rebutted courts should consider general state law principles regarding the severability of unenforceable terms.

Section 5. Unfair and deceptive act and practice.
It is an unfair and deceptive practice in violation of [*the State deceptive practices statute*] to include one of the presumptively-unconscionable terms identified in Section 2 in a standard form contract to which only one of the parties to the contract is an individual and that individual does not draft the contact. Notwithstanding any other state laws to the contrary, a party who prevails in a claim under this Section shall be entitled to $1,000 in statutory damages per violation. Additionally, such an action may be maintained by an employee against her employer whether or not [*the State deceptive practices statute*] otherwise allows for such claims.

TITLE V: PROHIBITION OF FORCED ARBITRATION CLAUSES UNDER STATE LAW

Section 1. Findings.
Forced arbitration agreements covering consumers and employees are contrary to the established public policy of this State. Because employees and consumers are forced to assent to these agreements as a condition of being an employee or consumer before any dispute has arisen with the employer or merchant, these agreements do not offer employees and consumers a meaningful choice about how to resolve their disputes with the employer or merchant. In addition, forced arbitration agreements prevent employees and consumers from effectively vindicating their rights under State law. For these reasons, except when inconsistent with federal law, the State prohibits the formation and enforcement of forced arbitration agreements in employment and consumer contracts.

Section 2. Prohibition of arbitration clauses in insurance agreements.
A forced arbitration agreement within or part of any written contract for insurance with a consumer or other written agreement involving the offering of insurance to a consumer is invalid, unenforceable, and void. Any such arbitration agreement shall be considered severable, and all other provisions of the contract for insurance shall remain in effect and given full force.

Section 3. Prohibition of arbitration clauses in employment contracts for workers exempted from the Federal Arbitration Act.
A forced arbitration agreement within or part of any written contract of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce is unenforceable and void. Any such arbitration agreement shall be considered severable, and all other provisions of the employment contract shall remain in effect and given full force.

Section 4. Prohibition of arbitration clauses that are not governed by federal law.
Any forced arbitration agreement, or portion thereof, in an employment or consumer contract is invalid, unenforceable, and void, when the enforceability of such arbitration agreement, or the portion at issue, is governed by State law. Any such arbitration agreement shall be considered severable, and all other provisions of the employment contract shall remain in effect and given full force.

Section 5. Severability.
If any provision of this Title or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the Title that can be given effect without the invalid provision or application, and to this end the provisions of this Title are declared to be severable.

TITLE VI: DATA DISCLOSURE REQUIREMENTS FOR ARBITRATION ADMINISTRATORS

Section 1. Findings.
Unlike administrative or judicial proceedings, arbitration proceedings regarding consumer and employment claims are not public. The lack of public information regarding these proceedings interferes with the State's ability to monitor arbitration administrators to ensure that they comply with basic principles of fairness and impartiality.

Section 2. Requirements.

(a) Any private company that administers five or more arbitrations a year in this State involving a consumer or employee shall collect and publish the following information about each of its arbitrations for at least five years after the arbitration has completed:

- **(i)** The names of the parties to the arbitration;
- **(ii)** The party that filed the arbitration claim;
- **(iii)** The type of dispute involved, including goods or services, insurance, credit, debt collection, or employment;
- **(iv)** The prevailing party;
- **(v)** Whether the consumer or employee was represented by an attorney;
- **(vi)** The date the company administering the arbitration received the demand for arbitration, the date the arbitrator was appoint ed, and the date of the arbitration's disposition;
- **(vii)** Whether the arbitration resulted in an in-person hearing;
- **(viii)** Whether the parties provided each other with any pre-hearing discovery;
- **(ix)** The amount of the claim, the amount of the award, and any other relief granted, if any;
- **(x)** The name of the arbitrator, his or her total fee for the case, and the percentage of the arbitrator's fee paid by each party; and
- **(xi)** The arbitrator's professional affiliations.

(b) Information published pursuant to this title must be updated at least quarterly, and made available to the public in a computer-searchable format, which shall be accessible at the website of the private company administering the arbitrations, if any, and on paper upon request.

(c) No private company shall have any liability for collecting, publishing, or distributing the information in accord with this section.

Section 3. Confidentiality.

This Title does not require disclosure of any information other than that set forth in Section 2.

Section 4. Enforcement.

Any private person and any public enforcement agency responsible for enforcing State law under this Title may bring suit for injunctive relief against an entity that violates these provisions, and may recover reasonable attorney fees and other costs if an injunction or equivalent relief is awarded. Injunctive relief is the only relief available in a suit arising from failure to comply with this Title.

Section 5. Severability.

Should a court decide that any provision of this act is unconstitutional, preempted, or otherwise invalid, that provision shall be severed, and such a decision shall not affect the validity of the act other than the part severed.

TITLE VII: APPELLATE JURISDICTION

Section 1. No jurisdiction over interlocutory appeals.

Appellate courts shall not have jurisdiction to review a trial court's interlocutory order denying a motion to compel arbitration or otherwise concluding that an arbitration agreement is unenforceable or does not cover a particular claim. Appellate review of the denial of a motion to compel arbitration may be had after a final judgment has issued. An interlocutory appeal shall be allowed if the trial court orders arbitration and dismisses the suit, or orders arbitration and stays the litigation.

TITLE VIII: PREVENTING RESPONDENTS FROM IMPROPERLY DELAYING THE ARBITRATION PROCEEDING

Section 1. Findings. The United States Supreme Court has held that the Federal Arbitration Act generally protects parties' right to enter into private agreements to resolve their private disputes expeditiously. That goal is frustrated if a party imposes an arbitration requirement on consumers or employees but, then using the procedures of the arbitration administrator chosen by that party, prevents the arbitration proceeding from going forward in an expeditious manner. In particular, when the entity that requires arbitration refuses to pay its required share of the expenses of arbitration, too often the consumer or employee is prevented from going to court and also prevented from having a speedy arbitration hearing. This conduct amounts to a breach of the arbitration agreement and should be grounds for the consumer or employee to bring her claim in court. However, arbitration administrators are often slow to enforce their own rules. This Title regulates administrators to ensure that they arbitrate disputes efficiently and speedily.

Section 2. Covered arbitration administrators.

This Title applies to all arbitration administrators that have administrated, in this State, three or more arbitrations brought by a consumer or employee over the past 12 months.

Section 3. Requirements to ensure expeditious dispute resolution.

This section applies if a forced arbitration agreement, whether expressly or through incorporation of the rules of the arbitration administrator, requires that in a case brought by an employer or consumer, the respondent must pay certain fees or costs before the arbitration proceeding can proceed. In that case, if those fees or costs are not paid within 7 days after those fees are due, the arbitration administer must:

(a) Begin administering the arbitration, by scheduling a hearing date, notwithstanding the respondent's failure to pay required fees; or

(b) Within 10 after the fees are due, refuse to administer the arbitration, and provide the consumer or employee with a letter explaining that the administrator will not administrate the arbitration, and expressly stating that the "arbitration forum designated by the parties is unavailable to resolve this dispute."

Section 4. Requirements to prevent pending cases from being improperly suspended.
This section applies if a forced arbitration agreement, whether expressly or through incorporation of the rules of the arbitration administrator, requires that in a case brought by an employer or consumer, the respondent must pay certain fees or costs during the pendency of an arbitration proceeding. In that case, if those fees or costs are not paid within 7 days after the fees are due, the arbitrator must:

- **(a)** Continue the administering the arbitration proceeding notwithstanding the respondent's failure to pay required fees; or
- **(b)** Within 10 days after the fees are due, issue a final award for the consumer or employee that provides all relief requested by the consumer or employee. If the consumer or employee has not expressly set out the amount of monetary damages demanded, the arbitrator may either issue an award on liability alone and allow a court enforcing the award to decide damages or may hold its own hearing on monetary damages within one week following the issuance of the final award concerning liability.

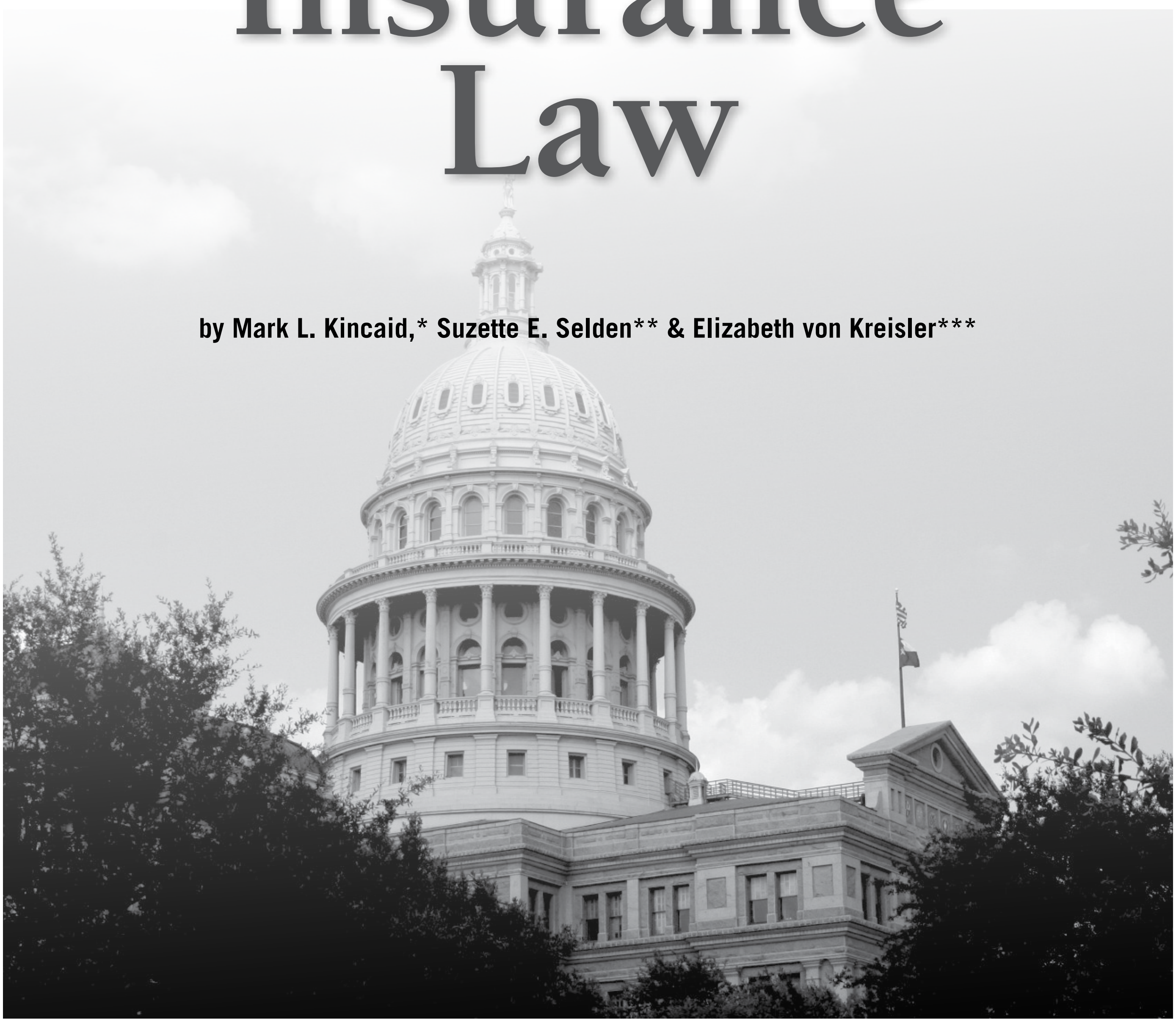
Section 5. Disclosure requirements.
Administrators covered by this Title shall publicly report the following, as applicable, and updated quarterly on the administrators publicly-accessible website for any arbitration demanded by a consumer or employee: when each arbitration demand was made, when each demand for payment of costs and fees is made, the date the respondent paid all fees and costs requested, when a hearing, either live or on the papers, was held, when the award was issued, when the arbitration administrator provided a letter indicating the arbitration would not proceed, and when an arbitration proceeding was terminated for lack of payment and an a resulting award is made to the consumer or employee.

Section 6. Enforcement.
The provisions of this Title shall be enforceable through an action seeking declaratory or injunctive relief by the Attorney General or any employee or consumer aggrieved by an administrator's failure to comply with this Title.

Section 7. Administrator's Right to Collect Fees.
Whenever an arbitration agreement or the arbitration administrator's rules incorporated into that agreement require that the respondent pay fees or costs to the arbitrator or arbitration administrator, the arbitrator and administrator are third-party beneficiaries of the agreement to pay fees or costs. If the administrator administers an arbitration and an arbitrator proceeds with an arbitration notwithstanding the respondent's failure to pay fees or costs pursuant to Section 3(a) or 4(a) of this Title, then the administrator may pursue a breach of contract action against the respondent under State law to collect those fees or costs.

Annual Survey of Texas Insurance Law

by Mark L. Kincaid,* Suzette E. Selden** & Elizabeth von Kreisler***



I. INTRODUCTION

The most significant event in Texas insurance law this past year was legislative. The bills ultimately died, but they would have drastically changed the unfair insurance practice statute and prompt payment of claims act as they apply to property damage claims. At the urging of insurance companies and "tort reform" lobbyists, the Texas Legislature considered a pair of bills that would have: (1) limited recovery for property damage claims; (2) allowed insurers to force suits into federal court; (3) immunized insurance company adjusters from liability for unfairly low estimates and other misconduct, while criminalizing excessive estimates by policyholders and their public adjusters; (4) required policyholders to document every detail of their damages as a prerequisite to filing suit; and (5) shortened limitations to one year. Senate Bill 1628 by Sen. Larry Taylor[1] and House Bill 3646 by Rep. John Smithee[2] were offered in response to perceived abuses arising from hailstorm claims, but both bills proposed changes that would have affected all property damage claims. The bills died after substantial opposition from businesses and others. SB 1628 passed the Senate but died in the House. HB 3646 died in committee.[3]

There were several significant developments in case law. Texas state and federal courts decided about 100 insurance cases this year, with several significant decisions. Perhaps the most significant decision is yet to come when the supreme court will decide whether policy benefits are "actual damages" recoverable for unfair insurance practices. To resolve a split in authorities, the Fifth Circuit certified the following question to the Texas Supreme Court:

> Whether, to maintain a cause of action under Chapter 541 of the Texas Insurance Code against an insurer that wrongfully withheld policy benefits, an insured must allege and prove an injury independent from denial policy benefits?

In re Deepwater Horizon, No. 14-31321, 2015 WL 7421978, at *10 (5th Cir. Nov. 19, 2015).

The Texas Supreme Court construed an ambiguous commercial property provision on calculating policy limits in favor of the commercial property insured in *RSUI Indem. Co. v. Lynd Co.*, 466 S.W.3d 113 (Tex. 2015). Conversely, the court held that an unambiguous anti-concurrent causation provision barred a hurricane damage claim in *JAW The Pointe, L.L.C. v. Lexington Ins. Co.*, 460 S.W.3d 597 (Tex. 2015).

The court also held that defendants and insurers can seek declaratory judgments on liability coverage, but plaintiffs cannot. *In re Essex Ins. Co.*, 450 S.W.3d 524 (Tex. 2014).

In a pair of decisions, the Fifth Circuit recognized the expansive scope of the remedies for violating the Prompt Payment of Claims Act. In *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Insurance Co.*, 801 F.3d 512 (5th Cir. 2015), the court held that the penalty deadline started once the policyholder gave the insurer most, but not all, of the requested information. In *Cox Operating, L.L.C. v. St. Paul Surplus Lines Insurance Co.*, 795 F.3d 496 (5th Cir. 2015), the fifth circuit held that violating any of the statutory deadlines for acknowledging, investigating, and accepting or rejecting a claim would trigger the 18 percent penalty, meaning the penalty applies to all deadlines, not just the payment deadline.

The Fifth Circuit clarified that attorney's fees can be awarded as a contingent fee percentage, in *Mid-Continent Cas. Co. v. Kipp Flores Architects, L.L.C.*, 602 Fed. App'x 985, 999-1000 (5th Cir. 2015).

With mixed results, a number of courts wrestled with issues regarding the extent to which appraisal exempts an insurer from liability for breach of contract, unfair insurance practices, and prompt payment violations. In a perennial contest, in suits where adjusters were named as defendants, insurers continued to seek removal based on improper joinder, and insureds continued to seek remands. The sides tied 3-3 this year.

II. FIRST PARTY INSURANCE POLICIES & PROVSIONS

A. Automobile

An injured man recovered policy limits from the party who hit him, then sued his own insurer, asserting breach of contract and extra-contractual claims after his insurer did not pay his UM/UIM benefits. The insurer moved to sever and abate the extra-contractual claims until the breach of contract claim was resolved. The trial court ordered the extra-contractual claims severed but denied abatement. The insurer sought mandamus relief, which the appellate court granted. The court held that the insurer should not be required to conduct discovery and prepare for trial on severed extra-contractual claims that could be rendered moot. The court stated that the lack of a settlement offer did not prevent the court abating the extra-contractual claims. *In re Farmers Tex. Co. Mut. Ins. Co.*, No. 03-15-00527-CV, 2015 WL 5781170, (Tex. App.—Austin Sept. 30, 2015, orig. proceeding).

B. Homeowners

Water damage to homeowners' wooden floors was not a covered loss. *Tsai v. Liberty Mut. Ins. Co.*, No. 01-14-00677-CV, 2015 WL 6550769 (Tex. App.—Houston [1st Dist.] Oct. 29, 2015, no pet. h.). The flooring was damaged by water migration from planters on a neighbor's property. The insurer denied the claim on grounds that the policy excluded damage from "surface water" entering the home at ground level. The insureds argued that the water ceased to be "surface" water when it migrated beneath their floors. The court disagreed. An engineering report showed that, after falling on the planters, the water pooled underneath a surface layer of mulch before being released. The floors were at or slightly below the level of the mulch. The water that reached the insureds' home was not absorbed by land and thus was excluded as "surface water."

In a divided opinion, a court held that a residential fence was an "other structure" subject to a 10% coverage limit, instead of being a structure attached to the dwelling, subject to the full policy limit. *Nassar v. Liberty Mut. Fire Ins. Co.*, No. 14-14-00277-CV, 2015 WL 5727667 (Tex. App.—Houston [14th Dist.] Sept. 29, 2015, no pet.). The policy covered:

> (1) The dwelling on the residence premises shown on the declarations page including structures attached to the dwelling.

(2) Other structures on the residence premises set apart from the dwelling by clear space. This includes structures connected to the dwelling by only a fence, utility line, or similar connection. The total limit of liability for other structures is the limit of liability shown on the declarations page or 10% of Coverage A (Dwelling) limit of liability, whichever is greater.

The parties agreed that the fence was damaged. The disagreement was whether it fit in coverage (1) or coverage (2). The majority held that the fence had to be considered an "other structure" subject to the lower limit. The majority reasoned that including the fence in (1) as a "structure attached to the dwelling" would make the fence a part of the dwelling and everything attached to the fence would also be part of the dwelling, which would negate (2). One justice dissented. The policy did not define "structures." The fences were clearly "attached to the dwelling." Considering the fence a "structure attached to the dwelling" would not make it part of the dwelling, contrary to the majority's analysis.

After an insured died, the estate's legal representative sued his insurance company for failing to pay for personal property stolen from the home after the insured's death. The court held that the policy did not cover the property after the insured's death, as it only covered, "personal property owned, worn or used by an insured while on the residence premises." The representative also sued the insurance agent, arguing that if the policy did not cover the loss, the agent was at fault. The court held the representative did not present any evidence that he notified the agent of the death before the loss occurred. *Spurlock v. Beacon Lloyds Ins. Co.*, No. 11-12-00357-CV, 2015 WL 581682 (Tex. App.—Eastland Jan. 29, 2015, pet. denied).

Texas state and federal courts decided about 100 insurance cases this year, with several significant decisions. Perhaps the most significant decision is yet to come.

A policy exclusion and limitation for water that "backs up through sewers or drains from outside the dwelling's plumbing system" applied where sewage flooded a home due to the concurrent failure of a check valve at the street and a quick disconnect at the dwelling system. *Durrett v. Nationwide Prop. & Cas. Ins. Co.*, No. A-14-CA-167-SS, 2015 WL 1564783 (W.D. Tex. April 7, 2015).

C. Commercial Property

An insurance policy was ambiguous and would be construed in favor of coverage where it allowed the insurer to choose the lower of three values, but was not clear whether the insurer could choose a value for each property or was limited to choosing only once for an occurrence that affected several properties. *RSUI Indem. Co. v. Lynd Co.*, 466 S.W.3d 113 (Tex. 2015). The insured had commercial properties insured by RSUI. Fifteen properties were damaged by Hurricane Rita, which the parties agreed was a single "occurrence." The disagreement was how to measure the insurer's amount due. The policy provided that the insurer's liability would be limited to the least of the following, in any one occurrence: (a) the actual adjusted amount of the loss; (b) 115% of the individually-stated value for each scheduled item of property; or (c) the Limit of Liability as shown on the policy. Lynd argued that the insurer had to choose one limit to apply to all the properties. The insurer argued that it could choose the lowest limit for each property, resulting in a lower total payment. After the trial court agreed with the insurer, and a divided court of appeals agreed with the insured, a majority of the Texas Supreme Court found the language was subject to more than one reasonable construction, was therefore ambiguous, and would be construed in favor of the insured.

An anti-concurrent-causation provision excluded the cost of rebuilding to comply with an ordinance, made necessary by damage caused by both covered wind and excluded flooding. *JAW The Pointe, L.L.C. v. Lexington Ins. Co.*, 460 S.W.3d 597 (Tex. 2015). The apartment complex was damaged by both wind and flooding from Hurricane Ike. A city ordinance required that the property be rebuilt to code because of the substantial damage, and that would require demolition and rebuilding to reach a higher elevation. The supreme court held there was no coverage where it was undisputed that both wind and flooding damaged the property. The policy contained an anti-concurrent-causation clause that excluded any loss resulting directly or indirectly from an excluded cause, such as flooding, regardless of any other cause or event that contributed to the loss. The court rejected the insured's argument that there should be coverage under the common law concurrent causation doctrines, because the wind damage, which was covered, was separate and independent and was sufficient to trigger the ordinance, resulting in the increased repair cost. The court rejected this argument, finding that the policy language controlled in place of the common law doctrine.

Delaying notice of a loss for nearly two years prejudiced the insurer and resulted in no coverage. *Alaniz v. Sirius Int'l Ins. Corp.*, No. 15-40497, 2015 WL 5316565 (5th Cir. Sep. 14, 2015) (per curiam). A hailstorm damaged an insured's property. Although the insured knew about the storm for over a year, he did not realize that his property was damaged. After learning of the damage, the insured delayed another five months before filing a claim. The insurer denied the claim on grounds that he did not provide prompt notice. The court agreed. The insured's delay was not reasonable, even if the delay was measured following the insured's awareness of facts suggesting hail damage. Further, the delay prejudiced the insurer because there was continued deterioration of the property due to water damage, which could have been partially avoided. The deterioration prejudiced the insurer's ability to investigate the extent of the damage from the hailstorm.

A court held that a policy covered only the actual cash value of the insured's property damage and thus barred the trial court from considering the jury's finding on replacement cost. *Davis v. Nat'l Lloyds Ins. Co.*, No. 01-14-00278-CV, 2015 WL 6081411 (Tex. App.—Houston [1st Dist.] Oct. 13, 2015, no pet. h.).

A policy deductible provision was unambiguous and meant 5% of the sum of the insurable values of each damaged property. *Saratoga Res., Inc. v. Am. Int'l Grp., Inc.*, No. H.-14-2270, 2015 WL 1602130 (S.D. Tex. May 21, 2015). A policy insured various oil and gas properties owned by the insured. These properties were damaged by Hurricane Isaac. The insurer and the insured disagreed how the deductible should be calculated. The policy stated that the deductible was "5% of Total Insurable Values at the time and place of the loss … If two or more deductible amounts apply to a single occurrence, the total to be deducted shall not exceed the largest deductible applicable unless otherwise stated[.]" The insured argued that this meant the deductible should be calculated to be 5% of the value of the property with the highest total insured value, whereas the insurer argued this meant the deductible was 5% of the total insurable values of all damage properties, added together. The court agreed with the insurer. The policy was not ambiguous. Only one interpretation gave meaning to all parts. The words "total" and "values" indicated that more than one value was to be included in the calculation.

A court concluded that an insured's claim for commercial property damage was excluded by water and earth movement exclusions. *Bilotto v. Allied Prop. & Cas. Ins. Co.*, 79 F. Supp. 3d 660 (S.D. Tex. 2015). When the insured purchased the property, the building already had cracks. A year later, the insured hired a foundation company that found damage and suggested that a plumbing leak might be to blame. The insured then filed a claim. The insurer advised the insured to retain a plumbing company, which found several plumbing leaks. The insurer then hired an engineering company, which observed much damage to the building. Both the plumbing and engineering companies determined that the damage was caused partly by three plumbing leaks under the property. The engineering company identified other causes as soil movement, foundation design, and material quality. After the insurer denied coverage, the insured hired an engineering expert, who testified that there were two causes of damage, one of which was the slope of the asphalt parking lot, which caused drainage problems, resulting in earth movement under the foundation. The insured argued there was no evidence that the leaks were continuous over a fourteen-day period, as required for the water exclusion to apply. While there was no soil or geotechnical testing done to determine the duration of the leaks, the court concluded that no such testing was required. The cracks existed when the insured bought the building a year before he filed the claim. Also, the insured's expert's testimony regarding the drainage issues was some evidence of continued or repeated leakage of moisture over a period of more than fourteen days. The court further held that, even if the water exclusion did not apply, the earth movement exclusion did, based on the experts' testimony. Finally, the court held that the anti-concurrent causation clause excluded all coverage, even if the damage fell within certain exclusions and outside others.

D. Life Insurance

Police were called to a home where a man was attempting suicide. The man approached the police with a gun in his hand, so they shot him dead. His beneficiaries tried to collect the life insurance proceeds. The insurer refused to pay, stating that the death was not accidental, since the insured put himself in a position where he should have known serious injury or death would occur. The appeals court affirmed summary judgment for the insurer. *Rice v. ReliaStar Life Ins. Co.*, 770 F.3d 1122 (5th Cir. 2014).

A life insurer that paid disputed proceeds into the court's registry but made a sizeable computation error in the amount of interest could correct that error, where the insurer had not violated the prompt payment of claim statute. *Penn Mut. Life Ins. Co. v. Stewart*, No. H-14-2976, 2015 WL 5795636 (S.D. Tex. Oct. 2, 2015).

A trial court denied an insurer's motion for judgment on the pleadings in *Slack v. Prudential Ins. Co. of Am.*, No. 6:14-CV-576, 2015 WL 5604678 (E.D. Tex. Sep. 22, 2015). The plaintiff alleged that her husband purchased a life insurance policy naming her as the beneficiary and that the insurer unilaterally, and over the agent's objection, used the policy's cash value and paid premiums to purchase a different type of policy than the one the plaintiff and her husband were told they had. The insurer argued that the plaintiff lacked standing to bring her DTPA and Insurance Code claims. The court found that plaintiff was a "consumer" entitled to bring the DTPA claim because she was a third party beneficiary of the life insurance policy. It did not matter that the plaintiff was not involved with the policy until after the alleged wrongdoing occurred. The plaintiff also had standing under the Insurance Code as a beneficiary of the policy.

E. Health

The defendant in *United States v. Collins*, 774 F.3d 256 (5th Cir. 2014), set up fake personal injury claims to defraud insurance companies. When charged with conspiracy to commit healthcare fraud, the defendant argued that the insurers he defrauded did not meet the statutory definition of "health care benefit program," as they were automobile insurers. The court held that, to the extent automobile insurers pay for medical treatment, they are health care benefit programs under the healthcare fraud statute, 18 U.S.C. § 1347(a).

F. Worker's Compensation

In *In re Crawford & Co.*, 458 S.W.3d 920 (Tex. 2015), the supreme court extended its holding in *Ruttiger* in. In *Texas Mut. Ins. Co. v. Ruttiger*, 381 S.W.3d 430 (Tex. 2012), the court held that statutory and common law claims related to claims handling by a workers' compensation insurer fell within the exclusive jurisdiction of the workers' compensation division. In contrast, *Ruttiger* held that statutory claims for misrepresentation were not within the exclusive jurisdiction.

Johnson and his wife sued his workers' compensation insurer, claims handling company, and claims adjuster for various acts including negligence; gross negligence; negligent, fraudulent, and intentional misrepresentations; fraud; fraudulent nondisclosure; fraudulent inducement; intentional infliction of emotional distress; malicious prosecution; conspiracy; breach of contract; quantum meruit; and breach of the common law duty of good faith and fair dealing. The court held that all of the claims that related to claims handling were within the exclusive jurisdiction of the workers' compensation division and therefore the trial court lacked jurisdiction.

The court then held that all the claims related to misrepresentation were also within the exclusive jurisdiction of the workers' compensation division, because all of the alleged misrepresentations were made in the context of handling the claim for benefits. The court likewise held that the claim for malicious prosecution arose out of claims handling and also was within the workers' compensation division's exclusive jurisdiction. Finally, the court held that, assuming the wife had standing to assert any claims, those claims also were within the exclusive jurisdiction of the division. The court granted the petition for writ of mandamus compelling the trial court to dismiss the case in its entirety.

G. Title

A title insurer did not breach its contract by failing to cover a claim of right of first refusal, where that right was expressly excepted from coverage. *IQ Holdings, Inc. v. Stewart Title Guar. Co.*, 451 S.W.3d 861 (Tex. App.—Houston [1st Dist.] 2014, no pet.).

H. Surplus Lines Insurance

A commercial property surplus lines insurer could enforce a forum selection clause in its contract, where the policy was procured by a licensed surplus lines agent from an eligible surplus lines insurer as defined by Chapter 981 of the Texas Insurance Code. *Chandler Mgmt. Corp. v. First Specialty Ins. Corp.*, 452 S.W.3d 887 (Tex. App.—Dallas 2014, pet. filed). The court held that the insurer carried its burden of proving every fact essential to the surplus lines insurer exception. The insurer presented evidence that the policy was issued by an eligible surplus lines agent, even though the agent did business under a different name. The insured also did not object to the trial court taking judicial notice of records from the website of the Texas Department of Insurance showing the insurer was an eligible surplus lines insurer.

Construing the statute to allow recovery of policy benefits as part of actual damages is an application that is consistent with the statutory purpose of prohibiting unfair insurance practices.

The insured argued that the policy did not meet certain technical requirements and that the insurer failed to show that the full amount of insurance could not be obtained from an authorized insurer, instead of a surplus lines insurer, as required by section 981.004(a). The *Chandler* court noted several instances where the insurance policy did not comply with Chapter 981. The court also noted that the statute provides that violations do not affect the enforceability of insurance policies unless the violations are "material and intentional." The court held that the record contained no evidence that any violation, even if material, was intentional. The court also held that violations could be punished by sanctions from TDI, but that did not affect the insurer's status as an eligible surplus lines insurer and therefore did not prohibit the insurer from enforcing the forum selection clause in the policy.

A notice provision in a definition of a coverage term was a condition precedent that the insurer waived when it denied the insured's claim. *Cox Operating, L.L.C. v. St. Paul Surplus Lines Ins.,* 795 F.3d 496 (5th Cir. 2015). An insured spent millions of dollars cleaning up pollution after Hurricane Katrina damaged its oil and gas facilities. It sought coverage under its liability policy, which provided coverage for "pollution clean up costs," defined as any expense for pollution work that "is reported to us within one year of the ending date of that pollution work." The insured submitted various invoices for its claim. The insurer paid a portion of the claim but denied coverage for any additional amounts. The insurer filed suit seeking a declaration that it was not liable for the rest because those amounts were submitted more than a year after the clean up was finished. The Fifth Circuit held that, although the reporting requirement was imbedded in the definition of the coverage term, it was a waivable condition precedent. The court reasoned that the parties' objective intent, and not just the location of the notice provision in the policy, determined whether it could be waived. The policy also included the reporting requirement in a separate provision that was stated in conditional terms. This created an ambiguity as to whether the reporting requirement was definitional in the scope of coverage or whether it was a waivable condition precedent. The court interpreted this ambiguity in favor of the insured. Additionally, the reporting requirement here was a cost-reporting requirement, not an incident-reporting requirement, which made it different from other cases involving claims-made policies because it did not restrict the insurer's liability to an immediately ascertainable time frame. The court also found it unimaginable that the parties would have intended the reporting requirement to be nonwaivable. When the insurer denied the claims, the insured's clean up work was ongoing. It did not make sense that the insured would have to continue reporting after the denial.

I. Other Policies

The term "theft" in a commercial crime insurance policy did not include forgery, in the absence of an unlawful taking. *Tesoro Refining & Mktg. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 96 F. Supp. 3d 638 (W.D. Tex. 2015). A company sought coverage for losses from its employee's alleged forgery of line of credit documents that suggested a customer was adequately collateralized. The insured sought coverage under the employee theft provision, which stated, that "theft shall also include forgery." The policy defined "theft" as "the unlawful taking of property to the deprivation of the insured." The court concluded that the definition covered losses from "unlawful takings" by employees by forgery, but not every loss from forgery. The insured's proposed interpretation — that a forgery always constitutes a theft — was unreasonable. The court further held that the employee's conduct did not amount to an "unlawful taking." The insured continued to sell fuel on credit to the customer based on the forged documents, but the employee did not seize, take possession of, or otherwise exercise control over the insured's fuel.

III. FIRST PARTY THEORIES OF LIABILITY

A. Unfair Insurance Practices, Deceptive Trade Practices & Unconscionable Conduct

The question whether policy benefits are part of "actual damages" or whether the insured must prove an "independent injury" will soon be decided by the Texas Supreme Court. Actually, the issue will be re-decided, because the court already made it clear that policy benefits are actual damages, and in fact may be damages as a matter of law, in *Vail v. Texas Farm Bur. Mut. Ins. Co.*, 754 S.W.2d 129, 136 (Tex. 1988).

In *Vail* the insurer made the same argument – that policy benefits were damages for breach of contract and were not "actual damages" for unfair settlement practices. The supreme court expressly rejected this argument, saying, "We hold that an insurer's refusal to pay the insured's claim causes damages as a matter of law in at least the amount of the policy benefits wrongfully withheld."

Despite this clear decision, a line of mostly federal cases has developed holding that an insured has to prove an "independent injury" to recover. The Fifth Circuit has stated that "[t]here can be no recovery for extra-contractual damages for mishandling claims unless the complained of actions or omissions caused injury independent of those that would have resulted from wrongful denial of policy benefits." *Great Am. Ins. Co. v. AFS/IBEX Fin. Services, Inc.*, 612 F.3d 800, 808 (5th Cir. 2010) (*quoting Parkans Int'l LLC v. Zurich Ins. Co.,* 299 F.3d 514, 519 (5th Cir.2002)).

These cases misapply a holding from *Republic Ins. Co.*

v. Stoker, 903 S.W.2d 338 (Tex. 1995), where the supreme court found no coverage for the claim and held that the lack of coverage precluded liability based on allegations that the insurer improperly failed to pay policy benefits. That holding makes perfect sense. If the insurer does not owe the claim, it cannot be liable for unreasonably failing to pay the claim. The *Stoker* court recognized that even when the insurer does not owe the claim, it could be liable if, in the course of handling the claim, the insurer committed an extreme act that caused an "independent injury." *See also First Tex. Sav. Ass'n v. Reliance Ins. Co.*, 950 F.2d 1171 (5th Cir. 1992). An independent injury is required when the insurer *does not* owe the claim, but when the insurer *does* owe the claim, the wrongfully withheld benefits are part of the injury.

In addition to contradicting *Vail*, those cases misapply the plain language of the statute, which allows recovery of "actual damages." Tex. Ins. Code § 541.151. "Actual damages means those recoverable at common law." *Brown v. Am. Transfer & Storage Co.*, 601 S.W.2d 931, 939 (Tex. 1980); *State Farm Life Ins. Co. v. Beaston*, 907 S.W.2d 430, 435 (Tex. 1995). Contract benefits certainly are damages recoverable at common law and are therefore part of "actual damages."

These misguided cases add words to the statute and ignore the mandate of liberal construction in section 541.008, which requires that courts give the statute "its most comprehensive application possible without doing any violence to its terms." *Kennedy v. Sale,* 689 S.W.2d 890, 892 (Tex.1985) (quoting *Cameron v. Terrell & Garrett, Inc.,* 618 S.W.2d 535, 541 (Tex.1981)). Construing the statute to allow recovery of policy benefits as part of actual damages is an application that is consistent with the statutory purpose of prohibiting unfair insurance practices.

Finally, these cases create the absurd result that a statute that prohibits unfair claim settlement practices and provides a remedy for those unfair claim practices doesn't allow the injured insured to recover the claim. How does that make sense?

Nevertheless, federal courts feel bound by the Fifth Circuit's erroneous holding. In *Lyda Swinerton Builders, Inc. v. Oklahoma Sur. Co.*, No. 4:12-CV-1759, 2015 WL 6164087 (S.D. Tex. July 30, 2015), the court required evidence of an independent injury. The court in *Lyda Swinerton Builders* recognized the very thoughtful decision in *In re Oil Spill by the Oil Rig "Deepwater Horizon,"* No. 12-311, 2014 WL 5524268, *15-16 (E.D. La. Oct. 21, 2014), where another court felt bound to reach the same conclusion but expressed concern that the Fifth Circuit was wrong in light of *Vail*. (Citing Mark L. Kincaid & Christopher W. Martin, *Texas Practice Guide: Insurance Litigation* § 16:27 (West 2015)).

In the appeal of the *Deepwater Horizon* decision, the Fifth Circuit took the opportunity to fix this mess by certifying the following question to the Texas Supreme Court:

> Whether, to maintain a cause of action under Chapter 541 of the Texas Insurance Code against an insurer that wrongfully withheld policy benefits, an insured must allege and prove an injury independent from denial policy benefits?

In re Deepwater Horizon, No. 14-31321, 2015 WL 7421978, *10 (5th Cir. Nov. 19, 2015).

In another case, the Fifth Circuit affirmed dismissal of an insured's bad faith claims based on post-litigation conduct by the insurer. *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*¸ 801 F.3d 512 (5th Cir. 2015). The court stated that the test is whether there is any reasonable basis for denying the claim, and evidence of a bona fide coverage dispute does not show bad faith. The district court excluded evidence of the insurer's post-litigation conduct in filing a summary judgment motion the insured contended the insurer knew was meritless.

The decision in *Weiser-Brown* is correct, but is expressed in language that may lead to error in other cases. The court muddles the issue by continuing to refer to the "no reasonable basis" test, which was correct for the common law duty of good faith and fair dealing until the decision in *Universe Life v. Giles* in 1997. At that point, the Texas Supreme Court replaced the common law "no reasonable basis" standard with the statutory standard imposing liability on an insurer that fails to act in good faith to effectuate a prompt, fair, and equitable settlement once liability is reasonable clear. *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 55-56 (Tex. 1997). In *Weiser-Brown* relying on the outdated phrasing made no difference. The evidence showed the insurer had a reasonable basis for denying the claim, because there was uncertainty about whether a covered loss occurred. That would negate liability under either the common law or statutory standards.

Further, the *Weiser-Brown* court affirmed the exclusion of post-litigation conduct, but not because it was post-litigation. Some insurers argue that only information at the time of the claim denial matters, relying on older common law cases. That argument may make sense under the older common law language, because the focus was on whether there was a reasonable basis to deny the claim. That invited focusing on the evidence the insurer had at the time the claim was denied.

In contrast, the statute imposes liability for "failing to attempt in good faith to effectuate a prompt, fair, and equitable settlement of … a claim with respect to which the insurer's liability *has become* reasonably clear." § 541.060 (a)(2)(A) (emphasis added). The "*has become*" language denotes a moving target that allows consideration of any point when the insurer's liability "*becomes*" reasonably clear. Thus, for example, an insurer's liability may not be reasonably clear in a case where it has a reasonable basis to suspect arson, but then may become clear if someone else admits to setting the fire. While the insurer might be reasonable in denying the claim before it receives that information, it would be unreasonable to continue denying the claim afterwards. Post-litigation conduct may be relevant if it shows the insurer's liability "*has become*" reasonably clear. In *Weiser-Brown* there was no such evidence. The court found that the evidence did not show that the insurer's liability ever became reasonably clear, before the court ruled. The evidence showed there was a serious dispute about whether there was a covered claim, which the jury resolved. The evidence wasn't excluded because it was post-litigation; it was excluded because it didn't show bad faith.

The *Weiser-Brown* opinion also discussed the exclusion of "expert" testimony on bad faith and affirmed for reasons discussed *post*. The Fifth Circuit did not exclude the evidence because it was post-litigation. The court analyzed the admissibility of the evidence under the rule allowing exclusion of even relevant evidence that poses the risk of undue prejudice or confusion. This presupposes that the evidence was relevant and could be admissible but was excluded for countervailing reasons.

After finding no coverage, the court in *Nassar v. Liberty Mut. Fire Ins. Co.*, No. 14-14-00277-CV, 2015 WL 5727667 (Tex. App.—Houston [14th Dist.] Sept. 29, 2015, pet. filed), concluded there was no extra-contractual liability for failing to pay a claim that was not covered. The court further held there was no basis to recover for misrepresentations based on general statements by the insurer that "our trained professionals are committed to providing you with a complete protection plan that is tailored to your lifestyle as well as your budget."

After finding an appraisal award under a homeowner's insurance policy was valid, the court considered the impact of that finding on the insured's claims for unfair insurance practices in *Cantu v. Southern Ins. Co.*, No. 03-14-00533-CV, 2015 WL

5096858 (Tex. App.—Austin Aug. 25, 2015, no pet.). The insurer argued that the appraisal award meant it had met its contractual obligations, precluding the insured's bad faith claims. The court held that once the insurer showed compliance with the appraisal award, the burden shifted to the insured to produce evidence creating a fact issue on her bad faith claims. The court agreed with the insured that the appraisal award would not necessarily bar her extra-contractual claims for pre-appraisal conduct. However, the court found no summary judgment evidence of any pre-appraisal conduct that would support her claim for bad faith, much less any evidence of "extreme" behavior.

One point from *Cantu* deserves clarification. The court correctly recognized that an appraisal award does not necessarily preclude a finding of bad faith. That result necessarily follows from the fact that Chapter 541 prohibits failing to act in good faith to settle once liability is reasonably clear. Any time an insurance company invokes appraisal, its liability for some amount is reasonably clear. The statute requires consideration of whether the insurer did or did not act in good faith to effectuate a prompt settlement. In some cases the evidence will show that the insurer behaved reasonably, invoked appraisal, and then paid the claim. In such a case there would be no liability for bad faith – not because of the appraisal award, but because of the lack of evidence of bad faith. In other circumstances, there may be significant evidence of bad faith where the insurance company fails to make any offer, makes an unreasonably low offer that is contradicted by the appraisal award, or engages in other conduct that satisfies the statutory standard of failing to act in good faith to effectuate a prompt, fair, and equitable settlement. The framework recognized by the court in *Cantu* allows for this consideration.

The court relied on the statement in the supreme court's decision in *Progressive County Mutual Ins. Co. v. Boyd*, 177 S.W.3d 919, 922 (Tex. 2005), that "We have left open the possibility that an insurer's denial of a claim it was not obligated to pay might nevertheless be in bad faith if its conduct was extreme and produced damages unrelated to and independent of the policy claim." That statement is correct in the context of a claim that is not owed. It recognizes that, even though the insurer does not owe the claim, it might otherwise cause damages. That reasoning has no application in a case where the insurer does owe the claim, such as where there is an appraisal award that the insurer has paid. All that should be required is evidence that meets that statutory standard of failing to act in good faith to settle once liability is reasonably clear. The court correctly recognized that an appraisal award does not necessarily preclude a bad faith claim, but it did so using a standard that may be inappropriate in another case.

An insured sued his insurer to recover insurance benefits after a home robbery. The trial court granted summary judgment in favor of the insurer, holding that the insured failed to state a claim. The appeals court reversed, holding that the insured stated a claim: he alleged that he paid his premium in full, that his insurer terminated him before the expiration of the policy period, and that the insurer told him he would receive a refund of any unearned premiums paid but never received a refund. *Chambers v. Am. Hallmark Ins. Co.*, 465 S.W.3d 389 (Tex. App.—Corpus Christi 2015, no pet.).

An insurer's timely payment of an appraisal award barred recovery for unfair insurance practice claims based on failure to pay the claim prior to the award, but did not entitle the insurer to summary judgment on other claims based on misrepresentation. *Graber v. State Farm Lloyds*, No. 3:13-CV-2671-B, 2015 WL 3755030 (N.D. Tex. June 15, 2015).

An employer could not state claims for misrepresentation based on a misrepresentation that occupational accident policies were like worker's compensation policies, where the employer expressly acknowledged on accepting the policy that it was not a worker's compensation policy. *Glenn v. L. Ray Calhoun & Co.*, 83 F. Supp. 3d 733, 749-50 (W.D. Tex. 2015).

In *Amarillo Hospitality Tenant, L.L.C. v. Massachusetts Bay Ins. Co.*, No. 2:14-CV-00143-J, 2015 WL 1954053 (N.D. Tex. April 29, 2015), the insured sued for unfair insurance practices after the insurer refused to pay to repair a hotel roof. The insured argued that a hailstorm caused damage to the roof, while the insurer argued that the damage was not caused by the storm. The court held that the fact that one of the insurer's vice presidents did not speak with the hotel owner did not suggest that the insurer did not attempt to know all the conditions of the claim. Moreover, there was no evidence that the insurer ignored information provided by other engineers and estimators. Because the insured failed to provide its own engineering report, there was nothing in the record to contradict the insurer's engineer. Summary judgment was granted for the insurer.

The Fifth Circuit held that violating any of the deadlines under the prompt payment of claims statute will trigger a penalty, not just failure to pay the claim.

B. Prompt Payment of Claims

The Fifth Circuit held that violating any of the deadlines under the prompt payment of claims statute will trigger a penalty, not just failure to pay the claim. *Cox Operating, L.L.C. v. St. Paul Surplus Lines Ins. Co.*, 795 F.3d 496 (5th Cir. 2015). The court based this holding on the plain language of the penalty provision, which provides that any violation will trigger a penalty. Reading it otherwise would render many of the deadlines meaningless. The court also relied on the statute's liberal construction mandate.

In *Cox*, the insurer failed to commence its investigation within the required thirty-day deadline under section 542.005. The district court began the accrual of the penalty sixty days after the date of claim, reasoning that the insurer had received everything it required – notice of the claim – by that date and failed to pay thereafter. The district court ended the penalty on the date of judgment. The Fifth Circuit affirmed, suggesting that the proper accrual date would have been the date of the violation – thirty days after the claim – based on the insurer's failure to commence its investigation. Because no party challenged the starting date, the Fifth Circuit did not rule on it. Similarly, because the insured did not challenge the date that interest stopped accruing, the Fifth Circuit did not address that, but did note that interest accrues until the earlier of the date judgment is rendered or the date the insurer takes the action it failed to take earlier.

The *Cox* decision raises some interesting points. First, the district court's award could have been supported as a violation by failing to pay within sixty days, not just a failure to commence its investigation, considering that the district court treated the failure to request additional information as indicating that the notice of the claim was sufficient. Thus, the insurer failed to pay within sixty days of that date, which triggered a violation.

Second, the court continues in what is an error in determining the ending date for penalties. The court got it half right – the ending date should be the date the insurer complies with whichever deadline it violated. If the insurer is late acknowledging a claim, the penalty should run from the due date until the date of compliance. If the insurer is late in requesting information, the penalty should run from the due date until the date of the insurer's late request. Of course, in that situation, it may be better to argue that the late request is ineffective to stop other deadlines requiring payment. When the violation is a failure to pay, the penalty should continue *until payment*, and should not end on the date of judgment.

There is no rational basis nor any basis in the language of the statute for stopping the penalty on the date of judgment, when the violation is a failure to pay. The insured remains unpaid on the date of judgment. The insurer has been penalized during the time it may have been challenging the claim in good faith. Why does it make sense to stop the penalty once the insurer's liability is recognized by a judgment? It doesn't.

It does make sense to stop other penalties accruing on the date of judgment, because by that point the insurer can no longer comply, but when the violation is a failure to pay, it makes no sense to stop the penalty unless and until the insurer pays. This is consistent with the liberal construction mandate of the statute, which has as its purpose encouraging the prompt payment of claims. Continuing to accrue the penalty certainly encourages an insurer that has been found liable to pay that claim much more so than ending the penalty does.

As in *Cox*, a number of decisions say that the penalty ends on the date of judgment, but they do not analyze the issue and explain why. Once a court does, they should hold that the penalty continues until the claim is paid. *See* Mark L. Kincaid & Christopher W. Martin, *Texas Practice Guide: Insurance Litigation* § 17:31 (West 2015) (available on Westlaw as TXPG-INS).

In another significant decision, the Fifth Circuit held that prompt payment penalties began after the insurer received most, but not all, of the items the insurer requested. *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*¸ 801 F.3d 512 (5th Cir. 2015). After the insured submitted a claim for loss of control of an oil well, the insurer requested seventeen items. The court found that by a certain date the insured had provided most of the information, but not everything. Nevertheless, the district court and Fifth Circuit both held that the insurer's penalty for failing to pay started on the date the insurer received most of the information. In the most extensive opinion to address the issue to date, the court discussed the meaning of the language in section 542.056 requiring payment by the fifteenth business day after the insurer receives "all items, statements, and forms required by the insurer to secure final proof of loss." The court cited but did not necessarily embrace the reasoning in several other decisions that the information required is not everything necessary to show the extent of the loss but only information necessary to show the insured in fact suffered a loss. In this case, the court affirmed as the trigger the date when the insurer received a substantial amount of the requested information, because the insurer never indicated afterwards that it needed more information (until suit was filed), and the remaining information did not go to the issue of whether there was a loss. Further, the insurer denied the claim, indicating that it had sufficient information. Even the insurer acknowledged that the insured is not required to comply with all document requests. The court concluded that an insurer cannot avoid liability "by pointing after-the-fact to missing information, the absence of which did not affect the insurer's decision." *Id.* at *10.

The Fifth Circuit held that an insurer cannot be liable under the prompt payment of claims act unless it is also liable under the insurance contract. *Tremago, L.P. v. Euler-Hermes American Credit Indem. Co.*, 602 Fed. App'x 981 (5th Cir. 2015) (per curiam). This holding is unremarkable and is supported by a number of other decisions that have said the same thing. However, it bears noting that none of these cases ever considered arguments why it may be consistent with the statutory purpose and language to impose liability on an insurer that violates deadlines, even if it ultimately does not owe the claim. The statute provides that non-liability is a defense to a penalty for failing to pay, of course. That suggests that non-liability for the claim isn't necessarily a defense for liability for failing to timely acknowledge the claim, failing to accept or reject the claim, or failing to state reasons for rejecting the claim, which are required under other provisions. Admittedly, it seems odd to penalize an insurer on a claim it does not owe, but the statute has deadlines for promptly handling even claims that are properly rejected. Requiring that the insurer owe the claim before any liability attaches undermines these deadlines by removing any possible penalty when the claim is not covered. For a fuller discussion of this issue *see* Mark L. Kincaid & Christopher W. Martin, *Texas Practice Guide: Insurance Litigation* § 17:43

(West 2015) (available on Westlaw as TXPG-INS).

An insurer's timely payment of an appraisal award did not serve as a defense to the insurer's liability for prompt payment of claims violations. *Graber v. State Farm Lloyds*, No. 3:13-CV-2671-B, 2015 WL 3755030 (N.D. Tex. June 15, 2015). Noting a line of lower court cases recognizing such a defense, the *Graber* court held that such a holding is not supported by the text of the statute and is in conflict with Texas Supreme Court and Fifth Circuit decisions. The court reasoned that this was a form of "good faith" defense precluded by the Fifth Circuit's decision in *Higginbotham v. State Farm Mut. Auto Ins. Co.*, 103 F.3d 456 (5th Cir. 1997), and other cases. Further, where the insurer promptly paid part of the claim but not the balance, until after the appraisal award, allowing a penalty on the unpaid portion was consistent with the Texas Supreme Court's decision in *Republic Underwriter's Ins. Co. v. Mex-Tex, Inc.*, 150 S.W.3d 423, 427-428 (Tex. 2004).

A federal court decided that to recover penalties and attorney's fees for failure to pay defense costs, the insured must incur and submit to the insurer bills for those costs. *Lyda Swinerton Builders, Inc. v. Okla. Sur. Co.*, No. 4:12-CV-1759, 2015 WL 6164087 (S.D. Tex. July 30, 2015). The court joined the prior decision in *Trammell Crow Residential Co. v. Virginia Sur. Co.*, 643 F. Supp. 2d 844, 859 (N.D. Tex. 2008), which held: "*Lamar Homes*[*, Inc. v. Mid-Continent Cas. Co.*, 242 S.W.3d 1, 20 (Tex. 2007)] is best understood as holding that an insurer becomes liable under the statute when it wrongfully rejects its defense obligations, but that attorney's fees cannot be awarded, and prejudgment interest does not begin accruing, until the insured actually incurs the defense cost."

A company submitted a claim to its insurer after some of the beef it shipped arrived in a spoiled condition. After the insurer failed to pay, the insured sued for failing to promptly accept or deny the claim. The court granted the insurer's motion to dismiss, because the statute does not apply to marine insurance contracts. *Beef Source Int'l, L.L.C. v. Certain Underwriters at Lloyds London Subscribing to Certificate No. B0723144A11-008,* No. 2:14-CV-104-J, 2015 WL 5666716 (N.D. Tex. Sept. 24, 2015).

A hotel owner sued its insurer for the breach of duty of good faith and fair dealing and violations of the prompt-payment statute for failing to pay a claim for business interruption when the hotel's air conditioner broke. The court found that the claim for business interruption was never submitted before bringing suit. Therefore, the court held the insurer did not violate its duty of good faith and fair dealing or violate the prompt-payment statute. *Metro Hospitality Partners, Ltd. v. Lexington Ins. Co.*, 84 F. Supp. 3d 553 (S.D. Tex. 2015).

A liability insurer's breach of its duty to defend by unreasonably delaying accepting the defense also violated the prompt payment of claims act. *Yowell v. Seneca Specialty Ins. Co.*, No. 4:15CV80-LG-CMC, 2015 WL 4575450 (E.D. Tex. July 28, 2015).

C. Breach of the Duty of Good Faith and Fair Dealing

In an unpublished opinion, the Fifth Circuit held that summary judgment on a bad faith claim was proper where the insured failed to cite evidence that the insurer had no reasonable basis to deny the claim. *Tremago, L.P. v. Euler-Hermes American Credit Indem. Co.*, 602 Fed. App'x 981 (5th Cir. 2015) (per curiam) (citing *Lyons v. Millers Cas. Ins. Co.*, 866 S.W.2d 597, 600 (Tex. 1993). Given that this is an unpublished opinion, it should not matter that the court cited to the outdated common law standard for breach of the duty of good faith and fair dealing, which was replaced by the statutory standard "failing to act in good faith to settle once liability is reasonably clear" in *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 55-56 (Tex. 1997).

A homeowner's insurer's payment of an appraisal award relieved it of liability for breach of the common law duty of good faith and fair dealing. *Graber v. State Farm Lloyds*, No. 3:13-CV-2671-B, 2015 WL 3755030 (N.D. Tex. June 15, 2015).

A widow sued a mortgage lender and a life insurance company after her claim for life insurance benefits was denied. *Ingram v. Beneficial Fin., Inc.*, No. 3:13-CV-4037-L, 2015 WL 1443110 (N.D. Tex. Mar. 30, 2015). The widow and her husband had obtained a home equity loan from the lender and also applied for life insurance to pay off the loan in the event of the husband's death. The husband was notified by letter that his application for insurance was denied and that a refund check for the initial premium would be mailed. The husband died. When the widow inquired about the insurance proceeds, she was told there was no policy. She sued the lender and the insurer on various grounds, including breach of the duty of good faith and fair dealing. The district court dismissed all of the widow's claims on summary judgment. The claims against the lender under the Insurance Code could not be sustained, because there was no evidence that the lender was engaged in the business of insurance. Also, the widow's claims for breach of contract and breach of the duty of good faith and fair dealing could not be maintained. No policy was ever issued, and the widow's evidence that she did not receive the denial letter or the check was insufficient to raise a fact issue regarding the existence of a valid policy or a special relationship.

D. Negligence

The Fifth Circuit held summary judgment was proper on an insured's negligence claim, because there was no authority for the proposition that insurance companies have a duty to draft a policy that contemplates all of the risks that the insured or a third-party beneficiary believes the policy should cover. *Tremago, L.P. v. Euler-Hermes Am. Credit Indem. Co.*, 602 Fed. App'x 981 (5th Cir. 2015) (per curiam).

E. ERISA

An insurer abused its discretion by determining that an employee was not totally disabled, where the insurer did not produce evidence supporting its conclusion that alternate positions were available in which the employee could earn substantially the same salary as his previous occupation. *George v. Reliance Standard Life Ins. Co.*, 776 F.3d 349 (5th Cir. 2015). The court further held that an exclusion for disability "caused by or contributed to by mental or nervous disorders" did not apply where the physical disability was sufficient, even without any mental disorder.

A beneficiary of an ERISA plan sought declaratory judgment that she was not required to reimburse the plan's payment of her medical expenses from proceeds of a medical malpractice suit. She argued that there was no plan document, which was true. However, the court found that the summary plan description could be the plan document, and the SPD allowed for reimbursement. If the court held otherwise, it would not be equitable, because the beneficiary would receive payment for her medical expenses under the SPD, but then would not be required to reimburse the plan under the same document. The court stated that the plaintiff could not obtain the benefit as a covered person and not also comply with her obligations. *Rhea v. Alan Ritchey, Inc. Welfare Benefit Plan*, 85 F. Supp. 3d 870 (E.D. Tex. 2015).

F. Breach of Fiduciary Duty

A court rejected an insured's argument that the insurer was liable for a breach of fiduciary duty by failing to act in the utmost good faith and not exercising the most scrupulous honesty, based on a complaint that the insurer failed to provide coverage for a fence attached to the insured's house. *Nassar v. Liberty Mut. Fire Ins. Co.*, No. 14-14-00277-CV, 2015 WL 5727667 (Tex. App.—Houston [14th Dist.] Sept. 29, 2015, pet. filed). The court found no formal fiduciary relationship and no basis to impose an informal fiduciary relationship.

A title insurance company as escrow agent, did not breach any fiduciary duty to the buyer. As escrow agent that duty consists of a duty of loyalty, the duty to make full disclosure, and the duty to exercise a high degree of care to conserve money and pay it only to those entitled to receive it. The authority and duty of the title company as escrow agent were limited and did not extend to investigation of the title. *IQ Holdings, Inc. v. Stewart Title Guar. Co.*, 451 S.W.3d 861 (Tex. App.—Houston [1st Dist.] 2014, no pet.).

IV. AGENTS, AGENCY, AND VICARIOUS LIABILITY

A. Individual Liability of Agents, Adjusters, and Others

A reinsurer sued an automobile insurer, its managing general agent, and the individuals who owned the MGA for breach of fiduciary duties. The owners of the MGA and insurer had transferred over $50 million of premiums to themselves rather than keeping the money in reserve, which ended up requiring the reinsurer to pay claims it otherwise would not have. The court held that a managing general agent holds money on behalf of an insured or insurer in a fiduciary capacity, even if the premium funds had not yet been transferred to the trust account. Therefore, a fiduciary duty was owed by the insurer, MGA, and owners of the MGA to the reinsurer. *Lincoln Gen. Ins. Co. v. U.S. Auto Ins. Servs.*, 787 F.3d 716 (5th Cir. 2015).

B. Insurer's Vicarious Liability for Agent's Conduct

An insurer was not vicariously liable for the conduct of an agent in selling an accident policy where the summary judgment evidence from both the insurer and agent stated that he was not an employee, agent, or representative of the insurer and had no affiliation with the insurer, and the plaintiff offered no contrary evidence. *Glenn v. L. Ray Calhoun & Co.*, 83 F. Supp. 3d 733, 749 (W.D. Tex. 2015).

V. THIRD PARTY INSURANCE POLICIES & PROVISIONS

A. Commercial Automobile Liability Insurance

A commercial auto insurer had no duty to pay a loss involving a vehicle that was not listed as a covered auto, and there was no evidence that the vehicle was used as a temporary substitute for a covered auto. *Canal Ins. Co. v. XMEX Transp., L.L.C.*, No. EP-13-CV-156-KC, 2015 WL 5010381 (W.D. Tex. Aug. 21, 2015). This finding of no coverage under the policy did not resolve whether there was coverage under the MCS-90 endorsement. In the underlying lawsuit, the jury found one decedent was an employee and the other was not. The court held that this determination did not decide liability under the MCS-90, because "employee" is defined differently under state law and federal law. Under state law, the distinction between employee and independent contractor matters, but it does not under federal law. The court deferred resolution of this issue until appeals in the underlying state court case were resolved.

A driver doesn't "loan" her car to a repair shop when it is left for repairs. Further, it is reasonable to construe the policy so that working on the brakes does not count as "operating" the vehicle.

B. Homeowners Liability Insurance

A court of appeals found no coverage for injuries when a car being worked on fell on the plaintiff. The insured's mother drove her car to the insured's house and left it for him to replace the brakes. The insured had the car jacked up, and his friend was helping, when the jack "gave way" and the vehicle suddenly fell on top of and injured the friend. The homeowner's insurer refused to defend or indemnify, relying on an exclusion for "bodily injury … arising out of the ownership, maintenance, operation, use, loading or unloading of … motor … vehicles …; which are owned or operated by or rented or loaned to an Insured." After the friend obtained a judgment against the insured, the insured assigned his claims to the plaintiff in return for a covenant not to execute. The court of appeals held that the trial court properly rendered summary judgment finding no coverage. The parties agreed that the bodily injuries arose out of the maintenance of a motor vehicle. The dispute was the last clause – whether the vehicle was "owned or operated by or rented or loaned to an Insured." The court concluded that the words owned, loan, and operated all indicated that the insured exercised control of the vehicle. The court concluded that the exclusion applied because "[t]he insured was performing customary acts of maintenance and handling on the motor vehicle loaned to him by his mother when the accident occurred which was a normal operation of the vehicle." *Fusaro v. Trinity Universal Ins. Co.*, 466 S.W.3d 927 (Tex. App.—Dallas 2015, no pet.).

It appears the *Fusaro* court got it wrong. According to the court, the mother left the car with the insured to replace the brakes. It is reasonable to construe the word "loan" to not include leaving a car for repairs. A driver doesn't "loan" her car to a repair shop when it is left for repairs. Further, it is reasonable to construe the policy so that working on the brakes does not count as "operating" the vehicle. One operates a vehicle by driving it, not by hoisting it on a jack where it is undriveable. The court should have found the words did not apply or at least were ambiguous and could reasonably be construed not to apply.

C. Commercial General Liability Insurance

Agreeing with the "overwhelming majority of jurisdictions to have considered the issue," the supreme court concluded that a demand by the Environmental Protection Agency under the federal Comprehensive Environmental Response, Compensation, Liability Act of 1980 is a "suit" within the meaning of the CGL policies' duty to defend. *McGinnis Industr. Maint. Corp. v. Phoenix Ins. Co.*, No. 14-0465, 2015 WL 4080146 (Tex. June 26, 2015). The insured received a "potential responsible party" demand letter from the EPA offering the insured the opportunity to enter into negotiations regarding cleaning up a toxic waste site where the insured had dumped pollutants. The insured requested a defense, which its insurers refused based on their contention that the demand letter was not a "suit" within the meaning of the policy. Answering a certified question from the Fifth Circuit, the Texas Supreme Court concluded that, based on the particular facts of CERCLA, a demand letter from the EPA did qualify as a "suit." First, the court noted that historically the EPA had to file suit in the usual sense to force compliance, but after enactment of CERLA in 1980 the EPA's demand letter served many of the functions previously requiring an actual suit. Second, the court noted that it was well-settled that CERLA cleanup costs are "damages" within the meaning of a CGL policy. Thus, it would lead to odd results if the court recognized a duty to pay for the damages, but no duty to defend the proceeding that would lead to the insured being required to pay. Finally, the court noted that the large majority of courts considering this issue ruled this way, so joining the majority promoted uniformity.

Announcing what may be great news for policyholders, the dissent by four justices wrote: "If you do not like your insurance policy, the Supreme Court of Texas can now change it for you." The dissenters objected that the demand letter was not within the understood meaning of "suit" at the time the policies were issued and that the insurers did not agree to defend the "functional equivalent of a suit."

The Texas Supreme Court held that an oilfield developer was not covered as an "additional insured" for subsurface pollution caused by the explosion of the Deepwater Horizon drilling rig. *In re Deepwater Horizon*, 470 S.W.3d 452 (Tex. 2015). The rig owner, Transocean, agreed to indemnify the developer, BP, for above surface pollution, and BP agreed to indemnify Transocean for subsurface pollution. In addition, Transocean agreed to name BP as an additional insured "in each of [Transocean's] policies, except Workers' Compensation for liabilities assumed by [Transocean] under the terms of [the Drilling] Contract." Looking only to Transocean's insurance policies, there was nothing to limit BP's coverage for subsurface pollution. However, if the drilling contract was considered, it would limit BP's coverage, because Transocean did not agree to indemnify BP for subsurface pollution. The court concluded that the insurance policy necessarily incorporated the provisions of the drilling contract, because the only way that BP was an additional insured was by virtue of policy language referring to liability under an "insured contract." The court reasoned that this necessarily required reference to the contract to determine the scope of the obligations.

The court further rejected BP's argument that the limitation only applied to workers' compensation policies, because this interpretation would be inconsistent with other policy provisions. In contrast, the court agreed with Transocean's interpretation that workers' compensation policies were excepted from the requirement of additional insured status, and additional insured status was limited to liabilities assumed under the drilling contract.

Because an insured did not meet its burden of showing that defective bolts supplied by a vendor caused "property damage" within the meaning of the policy, the insurer had no duty to indemnify. *Am. Home Assur. Co. v. Oceaneering Int'l, Inc.*, 609 F. App'x 171 (5th Cir. 2015) (per curiam). The underlying claim involved the failure of bolts in the construction of a riser system for a floating spar oil production facility in the Gulf of Mexico. When the bolts failed, Chevron sued several parties for its damages incurred repairing the spar, including the insured, which was found liable for indemnification of one of the other defendants. Coverage existed for "property damage." The insured argued that the two underlying suits had determined that the loss was for property damage. First, the insured pointed to a conclusion that Chevron did not suffer "economic loss" but instead showed damage to the spar. The Fifth Circuit held that this conclusion was not binding in the coverage dispute, because it was made in a separate action and was not the law of the case and because the words "property damage" in the prior opinion were not made in the context of the policy but in the context of whether attorney's fees were available. Second, the insured then argued that another prior opinion finding its duty to indemnify the other defendant was binding because it was based on the agreement between the insured and Chevron, which obligated the insured to "to be liable to and hold INDEMNITEES harmless for any loss of or damage to the property of [Chevron]." The court disagreed, finding that the prior opinion never addressed whether the bolts caused property damage to the spar.

The Fifth Circuit reversed a summary judgment for an insurer, and instead found that no exclusion applied and that the insurer owed a duty to indemnify homeowners for expenses they incurred in correcting defective construction work performed by the insured developer. *Crownover v. Mid-Continent Cas. Co.*, 772 F.3d 197 (5th Cir. 2014). The homeowners had previously obtained an arbitration award against the insured developer, but it went into bankruptcy, which limited the homeowners' recovery to what they could obtain from the insurer. The question was whether the developer's contractual obligation to repair its work was an "assumption of liability" beyond the developer's liability under general Texas law, thereby triggering the "contractual-liability exclusion" in its liability policy. Following *Gilbert Tex. Construction, L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118 (Tex. 2010), and *Ewing Construction Co. v. Amerisure Ins. Co.*, 420 S.W.3d 30 (Tex. 2014), the Fifth Circuit concluded that the contractual-liability exclusion did not apply. In *Gilbert*, the Texas Supreme Court held that a contractual-liability exclusion applied because the insured had "assumed" liability by taking on liability in its contract that it would not otherwise have had under the law, namely by agreeing to repair or pay for damage to property adjacent to the construction site. In *Ewing*, the Texas Supreme Court held that a contractual-liability exclusion did not apply because the insured's agreement to construct tennis courts in a "good and workmanlike manner" did not enlarge its obligations beyond any general common-law duty it might have, namely the duty to comply with the contract's terms and exercise ordinary care in doing so. Applying these precedents, the Fifth Circuit found that the contractual-liability exclusion did not apply. The fact that the obligation was contained in a contract was not sufficient to make the exclusion applicable. The question is whether the provision reflected an expansion of liability. The court noted that "there is no doubt that the general law provides a duty to repair" work that is not carried out in a good an workmanlike manner and that, consequently, the fact that the contract obligation was framed in terms of a duty to repair as opposed to a duty to construct made no difference. The remedy would be the same. The insurer failed to meet its burden of showing that the insured's duty to repair nonconforming work under the contract increased the insured's liability. The insurer was thus liable.

A judgment creditor's failure to segregate covered and non-covered damages was fatal to recovery from the judgment debtor's insurer. *Dallas Nat'l Ins. Co. v. Calitex Corp.*, 458 S.W.3d 210 (Tex. App.—Dallas 2015, pet. filed). A plaintiff project owner obtained a judgment against an insured builder for construction defects. The plaintiff then sued the insured's commercial general liability insurer to recover the underlying judgment. However, the court concluded that the "business risk exclusion" applied to at least some of the damages included in the judgment. The evidence at trial showed that at least some of the water leak damage occurred while the construction was ongoing and the builder was "performing operations." Because the insurer met its burden to show the exclusion applied to some of the damages proved in the underlying suit, the burden shift to the plaintiff to segregate covered and non-covered damages. The plaintiff presented evidence of different types of damages but did not show which of those were incurred while the insured builder was "performing operations" and which were incurred after. Having failed to segregate covered and non-covered damages, the plaintiff could not recover anything.

In *Companion Prop. & Cas. Ins. Co. v. Opheim*, 92 F. Supp. 3d 539 (N.D. Tex. 2015), the contractor's insurer sought a declaration that it had no duty to indemnify the contractor for damages awarded to a homeowner. One of the subcontractors took off the roof in a way that caused damage to other parts of the home. The policy stated that the insurance did not apply to property damage "arising out of … any roofing." The court held that, because the facts indicated that the damages were "causally related" to "roofing operations," the exclusion applied.

D. Personal Injury & Advertising Injury Liability Insurance

A complaint did not state a claim for "trade dress" infringement where the complaint that a competitor's map was confusingly similar was not based on its look and feel but instead was based on misleading statements. The insurer therefore had no duty to defend under the advertising injury coverage. *Test Masters Edu. Servs, Inc. v. State Farm Lloyds*, 791 F.3d 561 (5th Cir. 2015).

Hallmark, a homebuilder, infringed the copyright of an architecture firm, KFA, by obtaining a license to use eleven designs to build eleven homes but then building hundreds of copies based on the original plans without paying for additional licenses. The Fifth Circuit held this loss was covered as an "advertising injury" under the builder's policy. *Mid-Continent Cas. Co. v. Kipp Flores Architects, L.L.C.*, 602 Fed. App'x 985 (5th Cir. 2015). The Fifth Circuit held that coverage could be found for "advertising injury" under the policy even though the underlying judgment did not use those words. The court reasoned that the underlying litigation establishing the insured's liability often does not address the specific facts essential to decide coverage. Nevertheless, the court in the coverage action can make findings on the additional facts necessary to establish coverage. Coverage in this case depended on whether the infringing houses were "advertisements." The policy generally excluded copyright infringement, but the exclusion did not apply to infringement in the insured's "advertisement." The evidence supported a finding that the homes built by Hallmark were how it advertised its services. The homes built by Hallmark were its primary form of marketing. The court found no basis to construe the term "advertisement" narrowly. The policy defined advertisement as "a notice that is broadcast or published to the general public or specific market segments about your goods, products or services for the purpose of attracting customers or supporters." The court noted that under Texas law "advertisement" is given an expansive definition. The infringing homes were therefore advertisements within the exception, and the builder's liability was covered.

The court also held that the claim was not barred under the concurrent causation doctrine. Hallmark was liable for all the damages based on its infringement of KFA's copyright by building the additional homes without additional licenses. The fact that Hallmark may also have been liable for other breaches did not establish concurrent causation. All the damages were caused by the covered loss, and the court found that was a separate and independent cause that was covered. *Mid-Continent Cas. Co. v. Kipp Flores Architects, L.L.C.*, 602 Fed. App'x 985 (5th Cir. 2015).

The court also rejected the insurer's argument that the breach of contact exclusion applied. The contract between Hallmark and KFA provided that if Hallmark did not pay for additional licenses, then its license lapsed and was void; therefore, at the time Hallmark committed its copyright infringement, there was no contract in force to breach.

The court rejected the insurer's argument that the loss was excluded as a prior publication. There was no evidence that any infringing house was built before the insurer's first policy year. For the same reason, the court concluded that it made no difference when during the five consecutive policy years the infringement occurred, since none of them occurred before the first year or after the last year. No matter when the losses occurred, they would be covered by the insurer. The insured was therefore entitled to be indemnified.

E. Employer's Liability

An employee was fatally electrocuted while working around an energized power line. The facts showed that the foreman violated safety procedures by sending the crew near this line. The employer settled a lawsuit brought by the deceased employee's family and then sought indemnification. The policy covered "bodily injury by accident." The court agreed that the death was reasonably expected and not an "accident" and therefore there was no duty to indemnify. *Liberty Ins. Corp. v. Dixie Electric, L.L.C.*, No. 3:14-CV-0757-L, 2015 WL 1443161 (N.D. Tex. March 31, 2015).

F. Errors & Omissions

An exclusion for claims made against any insured by a person or entity that succeeds to the interest of the insured did not bar a claim by the insured's assignee. *Primo v. Great Am. Ins. Co.*, 455 S.W.3d 714 (Tex. App.—Houston [14th Dist.] 2015, no pet.). Primo was insured under an errors and omissions policy issued to Briar Green Condominiums, of which he was an officer and director. Briar Green asserted a claim against its fidelity insurer for $115,000 it asserted Primo had taken from its account. After the fidelity insurer paid that claim, Briar Green then assigned to the fidelity insurer, Travelers, all of its claims and rights against Primo. Travelers in turn sued Primo who tendered that claim to Great American for defense and indemnity. Great American denied the claim under the "insured versus insured" exclusion, which excluded liability for suits "made against any Insured … by, or for the benefit of, or at the behest of … any person or entity which succeeds to the interest of [Briar Green]."

The court of appeals held that Travelers was an assignee of Briar Green's rights, but that did not make it a successor in interest. The case law on successor in interest includes a party that acquires the other party's rights and responsibilities. While Travelers acquired Briar Green's rights under the policy, it did not acquire any of Briar Green's responsibilities. Further, the policy did not define successors in interest and the term was at least ambiguous regarding whether it included or did not include an assignee. Therefore, the court of appeals concluded that the trial court erred in rendering summary judgment for Great American based on the exclusion.

G. Excess Liability Insurance

An insured's settlement with a primary insurer for less than its policy limits did not exhaust the primary coverage, even where the insured offered to make up the difference, so that the excess insurer's obligation to pay was not triggered. *Martin Res. Mgmt. Corp. v. AXIS Ins. Co.*, 803 F.3d 766 (5th Cir. 2015). The AXIS policy stated that, "The Insurance afforded under this Policy shall apply only after all applicable Underlying Insurance … has been exhausted by actual payment under such Underlying Insurance[.]" The court found the language requiring actual payment under the underlying insurance meant the payment had to come from the insurer and could not be provided by the insured. The underlying limit was $10 million, and the insured settled with the primary insurer for $6 million. The court concluded that the underlying limit had not been exhausted.

The insured also relied on another provision in the excess policy providing that "If any Underlying Insurer fails to make payments under [its] Underlying Insurance for any reason whatsoever … then the Insureds shall be deemed to have retained any such amounts which are not so paid." The insured argued that this supported a reading that if the primary insurer failed to pay for any reason, then the gap could be treated as the insured's retention. The court concluded that, because the insured agreed to absolve the primary insurer for less than its policy limits, the insured was foreclosed from arguing that the primary insurer failed in its obligation to make full payment under the primary policy.

A disputed indemnity obligation did not qualify as "other insurance" and thus did not defer the excess insurer's obligation to pay its policy benefits. *In re Deepwater Horizon*, 470 S.W.3d 452 (Tex. 2015). The "other insurance" clause provided that if other insurance "applies" to the loss, then the policy would be in excess of such other insurance. "Other insurance" was defined to include any type of "indemnification." However, the company that arguably agreed to indemnify the insured was refusing such indemnity. The court rejected the insurer's argument that indemnity that potentially applies was covered and instead held that only indemnity that "actually and presently" applies qualified as "other insurance." The insurer therefore constructively breached its contract by refusing to pay.

H. Other Policies

The assignee of an oil and gas lease was entitled to coverage under a well-control policy. *St. Paul Fire & Marine Ins. Co. v. Petroplex Energy, Inc.*, No. 11-13-00104-CV, 2015 WL 5173035 (Tex. App.—Eastland Aug. 31, 2015, pet. filed). The assignee sued the insurer to recover expenses, damages, and costs resulting from a well blowout. The insurer denied coverage on grounds that: (1) the assignee was not the working interest owner of the well and thus was not an insured; and (2) that the well was not insured under the policy because it was not "producing" but instead was in a "workover," which was an increased hazard requiring extra premiums. The assignee argued that it owned 100% of the well and that the well was insured. The court agreed with the assignee. First, the assignee was the working interest owner of the well and the insured. The assignors testified that they intended for the assignment to transfer the entire interest to the assignee. Further, the fact that other parties initially paid for the expenses related to the blowout did not alter the fact that the assignee was the 100% owner. There was nothing to contradict the assignee's claim that it would ultimately be charged with those expenses when there was a true-up of accounts with the assignor. Second, the well was covered under the policy. It was an insured well at the inception of the policy, and there were no circumstances that caused the well to drop out of coverage when it blew out. The policy provided a rate for the well and an after-the-fact, quarterly true-up to account for any changes in the status of an insured well.

VI. DUTIES OF LIABILITY INSURERS

A. Duty to Defend

An insurer under a banker's professional liability policy had a duty to defend a bank that was sued in a class action for various deceitful practices motivated by the bank's desire to generate additional overdraft fees. *First Cmty. Bancshares v. St. Paul Mercury Ins. Co.*, 593 Fed. App'x 286 (5th Cir. 2014) (per curiam). Although the policy excluded claims "based upon, arising out of or attributable to any dispute involving fees or charges for an Insured's services," the court held that the claims were not solely claims for return of the improperly obtained fees.

An insurer under a banker's professional liability policy had a duty to defend a bank that was sued in a class action for various deceitful practices motivated by the bank's desire to generate additional overdraft fees.

An insured prison operator sought a declaratory judgment that the insurer had a duty to defend and indemnify under CGL and CUL policies for an underlying civil rights action. The civil rights suit involved the operator failing to provide necessary medical treatment to an inmate. The court held that the "medical services" exclusion in the CGL policy and the "professional liability" exclusion to the CUL policy applied, because as the loss arose from the failure to provide medical aid and professional services. Therefore, the insurer did not have a duty to defend or indemnify the operator. *LCS Corr. Servs., Inc. v. Lexington Ins. Co.*, 800 F.3d 664 (5th Cir. 2015).

In *Colony Insurance Co. v. Price*, No. 14-10317, 2015 WL 603218 (5th Cir. Feb. 12, 2015) (per curiam), an insurer sought a declaration that it owed no duty to defend its insured in an underlying suit arising from the beating death of a nightclub patron caused by club personnel. The underlying suit alleged claims of negligence and false imprisonment relating to the patron's treatment and claims of conspiracy and fraudulent transfer relating to the defendants' asset-hiding scheme in response to imminent litigation. The petition did not clarify why certain of the defendants (the "Price defendants") would be liable, since they consisted of two entities not in existence at the time of the death and the attorney of one of the other defendants. The petition simply alleged a vicarious liability theory with respect to the Price defendants. The insurer sought a declaration that it had no duty to defend the Price defendants because none of them were insureds or additional insureds. The policy named a single insured, as well as several additional insureds, including "employees" of the nightclub. The court agreed with the insurer. The Price defendants were not named insureds. They were also not additional insureds as "employees." The underlying petition never alleged that the Price defendants were employees of the insured, but rather suggested that the named insured was the employee of the Price defendants.

In *Texas Farm Bureau Underwriters v. Graham*, 450 S.W.3d 919 (Tex. App.—Texarkana 2015, pet. denied), the court held that an insurer owed no duty to defend a suit regarding a fatal shooting because the shooting, as alleged, was not an accident. The insured shot and killed a burglar in his house. He successfully defended the resulting wrongful death suit and then sought his defense costs from his homeowner's insurer. The court refused to consider any extrinsic evidence. The policy covered injury caused by an "occurrence" defined to be "an accident," and excluded coverage for injury "caused intentionally" by the insured. In the petition, the plaintiffs omitted the fact that the victim was committing burglary when he was shot, instead stating that the plaintiffs "had no way of knowing why" he was killed, and further stating that the insured had the "intent and purpose of bringing about the death of" the victim. The plaintiffs pled that the insured committed "a violent assault and battery" and, alternatively, that the insured was "negligent and grossly negligent" in causing the victim's death. The insured argued that the petition's negligence causes of action and statement that there is "no way of knowing why [the victim] was killed" brought the pleading within coverage. The court disagreed, finding that there were no facts in the petition alleging that the shooting was anything other than intentional. In applying the eight corners rule, the focus is on the facts alleged, not the causes of action or legal theories asserted. The negligence cause of action was thus insufficient to establish a duty to defend. The plaintiffs pled specific facts showing that the insured engaged in intentional conduct — he requested a weapon, took it, and shot the victim at close range. An intentional act can still be considered an accident when its effects are not the intended or expected result. However, that was not the situation here. The insurer had no duty to defend.

An insurer breached its duty to defend by delaying an unreasonable amount of time and could not cure that breach by belatedly offering a defense. The court found that the unexplained delay of 140 days after the insured demanded a defense was unreasonable. *Yowell v. Seneca Specialty Ins. Co.*, No. 4:15CV80-LG-CMC, 2015 WL 4575450 (E.D. Tex. July 28, 2015). The court further held that by breaching its duty to defend the insurer waived its right to control the insured's defense. The insured was free to utilize the attorney of its choice in the defense of the underlying lawsuit.

The *Yowell* court rejected the insured's assertion that the insurer could not contest the reasonableness and necessity of the insured's attorney's fees. While one district court decision supports this argument, the Fifth Circuit reached the opposite conclusion and held that attorney's fees that are recoverable as damages for breach of the duty to defend must be reasonable and necessary. *Am. Home Assur. Co. v. United Space Alliance, L.L.C.*, 378 F.3d 482, 490 (5th Cir. 2004).

Where the petition in an underlying litigation did not clearly state when the insured defendant first got notice, it triggered a duty to defend under two adjacent insurers' claims-made policies. When construing the petition in favor of the insured with respect to the later insurer, it could reasonably be read to first give notice during that period. Conversely, when reading the policy favorably to the insured against the prior insurer, the complaint could be read as potentially alleging notice of the claim during that period. Thus, both insurers had to defend. *Corinth Investors Holdings, L.L.C. v. Evanston Ins. Co.*, No. 4:13-CV-682, 2015 WL 1321616 (E.D. Tex. March 24, 2015).

In reaching its decision, the court in *Corinth Investors* relied on the eight corners rule, comparing the allegations in the complaint to the coverage provisions in the petition, but the court also considered the return of service as an "intrinsic extension of the original petition and one of the 'pleadings' that the Court may consider."

In another case, a court granted a motion to strike a declaration discussing the insured's vehicles, insurance policies, and reasons for purchasing an umbrella policy. The court agreed that it could not consider the declaration under the eight corners rule when determining the duty to defend. *Hudson Specialty Ins. Co. v. Bland*, No. H-14-1231, 2015 WL 1841180 (S.D. Tex. April 22, 2015).

A pollution exclusion barred coverage so that an insurer had no duty to defend its insured in litigation arising from injuries allegedly caused by a product manufactured by the insured. *Evanston Ins. Co. v. Lapolla Indus., Inc.*, 93 F. Supp. 3d 606 (S.D. Tex. 2015). The insured manufactured foam insulation, which was installed in a home. The homeowners filed a products liability suit against the insured after the insulation caused them respiratory distress that forced them to move out. The policy excluded coverage for injury or property damage caused by the release of pollutants, which were defined as any "irritant or contaminant," including things like "vapor" and "fumes." The plaintiffs' allegations that the insulation was present only in one part of the house and that the bodily harm occurred when vapors migrated to the rooms where they were staying undermined the insured's attempt to distinguish between exposure to vapors versus exposure to the insulation itself. Extrinsic evidence that the plaintiffs had contact with the insulation itself could not be considered. The pollution exclusion applied.

A professional liability insurer had a duty to defend a law firm sued for breach of fiduciary duty in a fee dispute, because the fee dispute, while not a "professional service" did arise out of the rendering of professional services.

An insurer had no duty to defend its insured against allegations that the insured attempted to mislead competitors and contracting bodies on the scope of its patent, because those allegations did not fall within coverage for advertising injury. *Uretek (USA), Inc. v. Cont'l Cas. Co.*, 92 F. Supp. 3d 589 (S.D. Tex. 2015). In a suit with its competitor, an insured was accused of knowingly misrepresenting to competitors and customers that certain road repair and maintenance contracts were covered by the insured's patent. The insured had liability insurance that covered "personal and advertising injury," defined to include disparagement of another's goods or services, use of another's advertising idea, or infringing on another's copyright. The court held there was no coverage, because deceptive statements regarding the scope of the insured's patent could not be construed as disparagement of a competitor's services.

A maritime insurer had a duty to defend an insured oil and gas company in an underlying suit brought by the United States concerning the discharge of pollutants from the insured's offshore platform. *Tow v. Water Quality Ins. Syndicate*, 531 B.R. 694 (S.D. Tex. Bankr. 2015). The underlying suit alleged "willful misconduct" that would be excluded under the policy. However, the underlying suit also alleged negligent conduct that was covered by the policy, which triggered the insurer's duty to defend.

A professional liability insurer had a duty to defend a law firm sued for breach of fiduciary duty in a fee dispute, because the fee dispute, while not a "professional service," did arise out of the rendering of professional services. Without the attorney-client relationship, there could be no breach of fiduciary duty claim. *Shamoun & Norman, L.L.P. v. Ironshore Indem., Inc.*, 56 F. Supp. 3d 840 (N.D. Tex. 2014).

VII. THIRD PARTY THEORIES OF LIABILITY

A. *Stowers* Duty & Negligent Failure to Settle

A plaintiff's *Stowers* demand was a counteroffer that rejected the insurer's prior offer, so that the plaintiff could not later revive that offer and accept it. *Davis v. Tex. Farm Bureau Ins.*, 470 S.W.3d 97 (Tex. App.—Houston [1st. Dist.] 2015, no pet.). The court found no evidence that when the insurer made its offer it intended for it to remain open despite the plaintiff's counteroffer in the *Stowers* demand. Therefore, the plaintiff had no claim for breach of contract.

The plaintiff also had no claim for promissory estoppel. First, there was no evidence that the insurer promised anything. The court reasoned that the insurer had offered $12,000 and inquired whether the plaintiff would take it. There likewise was no evidence that it was foreseeable that plaintiff would rely on the continuation of the offer, because the counteroffer rejected it. Finally, the court held there was no evidence that the plaintiff's reliance on any promise was reasonable, because the offer was made by an adversary.

B. Unfair Insurance Practices

An insurance broker sued a competitor alleging that it monopolized trade in the market for selling professional liability insurance to veterinarians. The court held that the competitor's refusal to work with insurers who would insure the appellant's clients was not a boycott because at least two firms must exclude another to constitute a boycott and in this case there was only one party allegedly excluding the insurance broker. For these same reasons, the Fifth Circuit held that the competitor did not commit unfair insurance practices. *Sanger Ins. Co. v. HUB Int'l, Ltd.*, 802 F.3d 732 (5th Cir. 2015).

After finding no coverage, a court then considered whether the trial court erred in rendering summary judgment on the unfair insurance claims. *Fusaro v. Trinity Universal Ins. Co.*, 466 S.W.3d 927 (Tex. App.—Dallas 2015, no pet.). One problem was that the plaintiff amended his petition after the motion for summary judgment was filed. Normally it would be error to grant summary judgment when that issue had not been raised. The court found any error was harmless as to unfair insurance practice claims that depended on coverage, because the court found there was no coverage. However, the court held that the trial court did err by granting summary judgment on unfair insurance practice claims that related to misrepresentations apart from coverage. Based on the record, the court of appeals could not determine whether those claims were valid or not and reversed and remanded to the trial court.

An injured third party lacked standing to sue the other driver's insurer for unfair settlement practices. *Ramirez v. First*

Liberty Ins. Corp., 458 S.W.3d 568 (Tex. App.—El Paso 2014, no pet.). Further, the injured third party could not sue for misrepresentations where there was no evidence that the insurer misrepresented anything regarding his claim.

C. Breach of the Duty of Good Faith and Fair Dealing

After finding an insurer had a duty to defend, the court nevertheless held there would be no breach of the duty of good faith and fair dealing, because the coverage dispute was a bona fide disagreement. *First Cmty. Bancshares v. St. Paul Mercury Ins. Co.*, 593 Fed. App'x 286 (5th Cir. 2014) (per curiam). The court thus did not reach the question whether there was a duty of good faith and fair dealing in the context of breach of the duty to defend.

It is interesting that the court bothered to address this issue, considering the district court held there was no breach of the duty of good faith and fair dealing cause of action for breach of the duty to defend. The Texas Supreme Court held in *Maryland Insurance Co. v. Head Industrial Coating & Services, Inc.*, 938 S.W.2d 27 (Tex. 1996), that there is no duty of good faith and fair dealing in the context of a liability policy. It is also curious that parties continue to allege this cause of action.

An injured third party lacked standing to sue the other driver's insurer for breach of the implied covenant of good faith and fair dealing. *Ramirez v. First Liberty Ins. Corp.*, 458 S.W.3d 568 (Tex. App.—El Paso 2014, no pet.). The court could have added that the insured also cannot sue for breach of that duty under a liability policy.

D. Other Theories

The insured under a CGL policy brought a claim for fraud against its insurer and agent when the insurer failed to pay a claim brought against the insured for the faulty construction of a retaining wall. The appellate court upheld the trial court's summary judgment for the insurer and agent, stating the "your work" exclusion applied because the insured built the retaining wall. *Vela v. Calvin Specialty Ins. Co.*, No. 13-13-00475-CV, 2015 WL 1743455 (Tex. App.—Corpus Christi April 16, 2015, pet. filed).

E. Suits by third parties

A medical device company entered into an agreement under which an insurer agreed to pay the company for properly submitted claims for "covered services rendered to subscribers." The insurer terminated the agreement, and this suit followed. The appeals court held that the district court did not err when it dismissed the company's third-party beneficiary claim, as there was no support for the proposition that healthcare providers are third-party beneficiaries of their patients' health-insurance contracts. However, the appeals court remanded to allow the company to cure the deficiency by pleading that it received assignments from its patients. *Electrostim Medical Servs., Inc. v. Health Care Serv. Corp.*, 614 Fed. App'x 731 (5th Cir. 2015).

Tesoro Corporation and Tesoro Refining filed suit against Tesoro Corporation's insurer for breach of contract and unfair insurance practices related to payment of environmental liabilities incurred by Tesoro Refining. The policy only named Tesoro Corporation as an insured and did not name Tesoro Refining. However, Tesoro Refining argued that the previous owner of the company agreed to procure insurance for the benefit of Tesoro Refining but failed to do so. The court held there is nothing in the case law to suggest that a promise made by a party no longer named on the insurance policy can dictate payment of the insurance proceeds. *Charts Specialty Ins. Co. v. Tesoro Corp.*, Nos. 5:11-CV-927-DAE; 5:12-CV-256-DAE, 2015 WL 4154136 (W.D. July 10, 2015).

A commercial property owner and its insured tenant sued the insurer over the denial of adequate reimbursement for hurricane damage. *United Neurology, P.A. v. Harford Lloyd's Ins. Co.*, No. H-10-4248, 2015 WL 1470296 (S.D. Tex. Mar. 31, 2015). The court held that the property owner was not an intended third-party beneficiary and thus lacked standing to sue for breach of contract.

A medical service provider obtained an assignment of rights and lien from its patient, and filed a UCC financing statement reflecting the assignment. After receiving treatment, the patient settled with the automobile insurer of the driver that had caused her injuries. The patient did not pay the provider, which then sued the automobile insurer for violating UCC section 9.406. That statute says that a debtor cannot discharge its obligation by paying the assignor after receiving notice of the assignment. The court held that the patient's assignment of rights to the provider and the filing of a UCC financing statement did not give the provider a direct action against the insurer for the patient's treatment. Texas is not a direct action state. Without a judgment or agreement that the insured had a legal obligation to pay damages to the injured party, the patient did not have direct rights against the insurer to assign to the provider. Moreover, the UCC does not apply to "an assignment of a claim arising in tort, other than a commercial tort claim," and the claims at issue were for personal injury. Consequently, the provider had no direct right of action against the insurer on which to base its suit. *Pain Control Inst., Inc. v. GEICO Gen. Ins. Co.*, 447 S.W.3d 893 (Tex. App.—Dallas 2014, pet. filed).

An injured third party could not sue the other driver's insurer for negligent misrepresentation, where there was no evidence that the insurer misrepresented anything regarding the claim or that it represented anything to guide him in his business. *Ramirez v. First Liberty Ins. Corp.*, 458 S.W.3d 568 (Tex. App.—El Paso 2014, no pet.).

VIII. DAMAGES & OTHER ELEMENTS OF RECOVERY

A. Attorney's Fees

An insurer that breached its contract was liable as a matter of law for attorney's fees, and the insured did not waive its claim for fees by failing to brief it in its motion for summary judgment, at which time the claim would have been premature. *In re Deepwater Horizon*, No. 14-31321, 2015 WL 7421978 (5th Cir. Nov. 19, 2015).

The Fifth Circuit held that under Texas law a plaintiff may recover an otherwise reasonable contingent fee, without applying the lodestar method, which multiplies a reasonable rate by a reasonable number of hours. *Mid-Continent Cas. Co. v. Kipp Flores Architects, L.L.C.*, 602 Fed. App'x 985, 999-1000 (5th Cir. 2015). The court noted a number of prior decisions where the Fifth Circuit and Texas courts have awarded fees calculated on a percentage fee basis based on evidence that fee was usual or customary. The court concluded that lodestar evidence is not required for contingency fee awards but is required if a claimant wants to go above the contingency fee calculation. For example, lodestar evidence was required in a case where the judgment awarded no monetary relief other than attorney's fees, because there was nothing for the contingency fee to apply to.

Although this is an unpublished opinion by the Fifth Circuit, this holding on attorney's fees clarifies an important issue that has recently come into question in some quarters. The court did make one common math error, however. The court stated that the net fee of $1 million was 33% of the judgment, compared to the underlying judgment of $3 million. In fact, a $1 million fee is only 25% of a judgment for $3 million in damages.

If the contingent fee is 33% of the recovery, then with $3 million in damages the fee would be $1.5 million dollars, which would be 33% of the total recovery of $4.5 million.

After an insurance coverage case went to trial and resulted in a judgment in favor of the insured and its attorneys (who were also parties), the prevailing parties moved for attorney's fees on a contingent basis or, alternatively, on an enhanced lodestar model. *OneBeacon Ins. Co. v. T. Wade Welch & Assocs.*, No. H-11-3061, 2015 WL 5021954 (S.D. Tex. Aug. 24, 2015, no pet.). The court applied the lodestar method, finding that the prevailing party had provided evidence of the lodestar amount and that the lodestar method provided the court with flexibility to consider the contingency contract when considering the overall reasonableness of the rate. In applying the lodestar factors, the court found that the case was complex and, given that complexity, it was reasonable for two lawyers to both perform certain activities. The court did, however, reduce one attorney's rate by 5% because he billed in quarter-hour increments. In considering the contingency nature of the case, the court refused to apply a multiplier to the base lodestar for the law firm's representation of itself in the suit, because the firm could not have a contingency agreement with itself. However, the court allowed an adjustment to the lodestar base for the fees for representing the insured.

An insurer that breached its duty to defend by unreasonably delaying was liable for the insured's attorney's fees incurred in defending the suit and was liable for the insured's attorney's fees incurred in pursuing the claim against the insurer. However, because there were competing affidavits on the reasonableness of the fees, there was a fact issue on the amounts, which precluded summary judgment. *Yowell v. Seneca Specialty Ins. Co.*, No. 4:15CV80-LG-CMC, 2015 WL 4575450 (E.D. Tex. July 28, 2015).

A liability insurer that agreed to pay the same lawyer to defend who was already pursuing the insured's affirmative claims was not required to pay any portion of the attorney's fees incurred in pursuing the affirmative claims. The court recognized that when a suit alleges covered and non-covered claims, the insurer must defend all, but that did not mean that the insurer had to pay fees for the affirmative claims. The court found that the work done on the affirmative and defensive claims could be segregated and had been by the lawyer. *Charla G. Aldous, P.C. v. Darwin Nat'l Assur. Co.*, 92 F. Supp. 3d 555 (N.D. Tex. 2015).

The court further held that judicial estoppel barred the insured from arguing that the amount of defensive attorney's fees disputed by the insurer was different from the amount of fees the plaintiff recovered in litigation against a third party. The court found that the insured could not take inconsistent positions, having prevailed in the first proceeding.

Finally, the court held that the insurer could assert the equitable claim of money had and received to recoup from the insured overpayments it had made for defense costs.

B. Costs

An insurer that prevailed in a coverage suit was entitled to all, not just a portion, of its costs. *Schreiber v. State Farm Lloyds*, No. 14-14-00010-CV, 2015 WL 4546131 (Tex. App.—Houston [1st Dist.] July 28, 2015, pet. filed). An insured sued her homeowner's insurer following a fire loss. The insurer prevailed on its arson defense, and the trial court rendered judgment in its favor. However, the trial court only awarded the insurer a small portion of its costs in the judgment, without specifying reasons for the reduction. The court of appeals found this was error and modified the judgment to include all of the insurer's costs. Although Tex. R. Civ. Proc. 131 gives the trial court discretion to not award all of the taxable court costs, that rule requires the court to state good cause on the record for doing so. That was not the case here. Although Tex. Civ. Prac. & Rem. Code § 31.007(b) states that a court "may include" all costs in an order, it does not change the Rule 131 requirement that the trial court award all taxable court costs to the prevailing party.

C. One Satisfaction Rule

A jury's finding that there was no double recovery of damages from one insurer that had been paid by another insurer was supported by evidence that the prior insurer did not specifically allocate its payment to any particular damages and the total damages exceeded the amount paid. *Cox Operating, L.L.C. v. St. Paul Surplus Lines Ins. Co.*, 795 F.3d 496 (5th Cir. 2015).

IX. DEFENSES & COUNTERCLAIMS

A. Arson

A court found the evidence supported a finding of arson, where there was evidence that the fire was incendiary and both insureds had a motive to set the fire and either an opportunity or other circumstances linking them to the fire. *Weidner v. Nationwide Prop. & Cas. Ins. Co.*, 74 F. Supp. 3d 814 (E.D. Tex. 2014). The court concluded that there was evidence that the husband set the fire but that the wife did not; therefore, the husband's recovery would be precluded by the intentional acts exclusion, but the wife would be entitled to recover her half of the benefits for her community interest. However, the court then analyzed coverage under the "concealment and fraud" exclusion and found that barred coverage as to both insureds.

B. Fortuity Doctrine

A claim was barred by the fortuity doctrine where the employer did not add the employee to the required list submitted to the insurer until after the employee was injured. The court reasoned that the employer should not be allowed to buy insurance after-the-fact to cover a known loss. *Glenn v. L. Ray Calhoun & Co.*, 83 F. Supp. 3d 733, 744 (W.D. Tex. 2015).

C. Forum Selection Clause

A surplus lines insurer could enforce a forum selection clause requiring suit be brought in New York where there was no evidence that doing so would deprive the insured of the ability to present evidence and the insured never objected to the clause in the policy until the insurer sought to enforce it. *Chandler Mgmt. Corp. v. First Specialty Ins. Corp.*, 452 S.W.3d 887 (Tex. App.—Dallas 2014, pet. filed). The court also held that enforcement of the clause was not against public policy. The insurance adjusting company and adjuster also could enforce the forum selection clause, even though they were not parties to the contract, where the insured's claims against them for unfair settlement practices and misrepresentations all related to enforcement of benefits under the contract.

D. Limitations

An insured homeowner received payment from his insurer for damage caused to his home during a hailstorm. After payment, the insurer closed the claim. Almost two years later, the insured hired a public adjuster who sent a letter to the insurer asking for a re-inspection. The insured eventually filed suit for breach of contract and unfair insurance practices after communications with the insurer failed. The court held that the cause of action accrues, at the latest, upon issuance of a final letter and closing of the claim file. Any request by the plaintiff to reopen the claim does not toll or extend the limitations period following a claims decision. Because suit was filed two years after the closing of the claim file, the case was dismissed. *Chapa v. Allstate Tex. Lloyds*, No. 7:15-CV-30, 2015 WL 3833074 (S.D. Tex. June 22, 2015).

Limitations barred misrepresentation claims by an employer based on the defendant's failure to explain that the occupational accident policies were not the same as worker's compensation, where the employer had received policies clearly disclosing that they were not worker's compensation policies. *Glenn v. L. Ray Calhoun & Co.*, 83 F. Supp. 3d 733, 746-47 (W.D. Tex. 2015).

E. Misrepresentation or Fraud by Insured

Misrepresentations by husband and wife insureds would not allow the insurer to avoid liability under the concealment and fraud exclusion, where the insurer did not show it relied on them or even believed them. However, the husband's misrepresentation about his knowledge of the fire, which the court found resulted from the husband's arson, would bar recovery as to both the husband and the wife. *Weidner v. Nationwide Prop. & Cas. Ins. Co.*, 74 F. Supp. 3d 814 (E.D. Tex. 2014).

An investigation bars reliance only when it is not hindered or prevented from being complete by any act of the other party.

A homeowner's fraudulent claim for meals as additional living expenses resulting from a water damage claim voided the policy and excused the insurer from any liability under the contract and for any liability for consequential damages or extra-contractual claims. *Igwe v. Safeco Ins. Co. of Indiana*, No. A-14-CV-587 LY, 2015 WL 6506391 (W.D. Tex. Oct. 27, 2015). The insured submitted claims for meals for himself, his wife, and their two children for many months while he was out of the house, even though his wife and children were not with him and did not consume any of those meals.

Fulgham submitted false hailstorm claims to an insurer and was found guilty of defrauding the insurer out of $899,000. The court of appeals held there was sufficient evidence that the insurer relied on misrepresentations by Fulgham in the claims process regarding repair work and other issues. The court also rejected his argument that the insurer could not rely on any representations where it conducted its own investigation. An investigation bars reliance only when it is not hindered or prevented from being complete by any act of the other party. In this case, there was substantial evidence that Fulgham made misrepresentations and hindered the insurer's investigation. *Fulgham v. Allied Prop. & Ins. Co.*, No. 05-14-00189-CV, 2015 WL 3413525 (Tex. App.—Dallas May 28, 2015, pet. filed).

The court rejected Fulgham's argument that the insurer failed to comply with Tex. Ins. Code sections 705.003 and 705.005 by failing to give notice that it refused to be bound by the policy and by failing to show that its reliance on misrepresentation caused it to lose a valid defense. The court held that these statutory requirements apply when the insurer relies on misrepresentation as a defense. Here the insurer relied on Fulgham's misrepresentations to support its affirmative claim for fraud.

F. Notice

A one year reporting requirement for pollution cleanup cost was a condition precedent that was waived by the insurer's denial of the claim, not a coverage provision that could not be waived. *Cox Operating, L.L.C. v. St. Paul Surplus Lines Ins. Co.*, 795 F.3d 496 (5th Cir. 2015). The Fifth Circuit held that, although the reporting requirement was imbedded in the definition of the coverage term, it was really a waivable condition precedent. The court reasoned that the parties' objective intent, not just the location of the notice provision, determined whether it could be waived. The policy also included the reporting requirement in a separate provision that was stated in conditional terms. This created an ambiguity as to whether the reporting requirement was defined in the scope of coverage or whether it was a waivable condition precedent. The court interpreted this ambiguity in favor of the insured. Additionally, the reporting requirement was a cost-reporting requirement, not an incident-reporting requirement, which distinguished other cases involving claims-made policies. The clause did not restrict the insurer's liability to an immediately ascertainable time frame. The court also found it unimaginable that the parties would have intended the reporting requirement to be non-waivable. When the insurer denied the claims, the insured's cleanup work was ongoing. It did not make sense that the insured would have to continue reporting after the denial.

In another case, the Fifth Circuit held that notice to the agent was not notice to the excess insurer and that the insurer was prejudiced where it did not receive direct notice until after a jury verdict against its insured. *Berkley Reg'l Ins. Co. v. Philadelphia Indem. Ins. Co.*, 600 Fed. App'x 230 (5th Cir. 2015) (per curiam). The court held that the broker was the insurer's agent under an agreement that expressly made the broker the insurer's agent, even though there was an intermediary broker between the two. However, the court found that the agency agreement did not give the broker express or implied authority to accept notice of claims. Therefore, the court concluded that notice to the agent did not satisfy the policy's requirement that the insured give notice of claims promptly to the excess insurer.

The *Berkley* court reaffirmed its prior holding in an earlier appeal that the insurer was prejudiced as a matter of law where it did not receive notice until after the verdict. The court found the insurer was prejudiced when it lost valuable rights including the right to have a seat at the mediation table and the ability to do any investigation or conduct its own analysis of the case, and the ability to join in the primary insurer's evaluation. The court rejected the argument that the excess insurer's ability to participate in the appeal showed a lack of prejudice. *Berkley Reg'l Ins. Co. v. Philadelphia Indem. Ins. Co.*, 690 F.3d 342 (5th Cir. 2012).

The court's holding that notice to the agent was not notice to the insurer is flatly contradicted by its holding in *Minter v.*

Great American Ins. Co. of New York, 423 F.3d 460, 472 (5th Cir. 2005). There, the court said, "It is a fundamental rule of agency law that notice to the agent constitutes notice to the principal. … accordingly, Great American's lack-of-notice defense fails as a matter of law." *See also Grissom v. Watson*, 704 S.W.2d 325, 327 (Tex. 1986)(quoting *Irvine v. Grady*, 85 Tex. 120, 19 S.W. 1028) (1892)).

Oddly, two of the judges were the same on both panels, yet the *Berkley* decision does not cite the *Minter* decision. In the future when these cases collide, *Minter* should win. It is a published decision, while *Berkley* is unpublished. Fifth Circuit Rule 47.5 provides that unpublished opinions are not precedent except under limited circumstances set forth in the rule. *Berkley,* 600 Fed. App'x 230, 231 n.*.

The court reasoned that appraisal is intended to take place before suit is filed and that a party must demand an appraisal promptly after the parties reach an impasse in their negotiations.

G. Preemption

FEMA preempts claims concerning an insurer's conduct after a flood policy is issued, but not claims concerning the issuance itself. *Spong v. Fidelity Nat'l Prop. & Cas. Ins. Co.*, 787 F.3d 296 (5th Cir. 2015). Insured property owners sued their flood insurer under various theories after their home was destroyed by Hurricane Ike. The policy was issued under the National Flood Insurance Program. The insurer argued that the policy was void from inception because the property was ineligible for flood insurance under the NFIP because it was located in a flood zone. The insurer also argued that the insured's claims were preempted by federal law. The Fifth Circuit held that the insured's state law claims were not preempted to the extent that they are insurance procurement claims, but claims that pertained to or arose from claims-handling after the policy issued were preempted.

The Fifth Circuit found that FEMA's pronouncements that it intended for federal preemption to apply to the issuance of policies were not binding on the court without any further action by Congress. Thus, the court was bound by its precedent *Campo v. Allstate Ins. Co.*, in which it held that FEMA did not preempt claims relating to the procurement of flood insurance policies.

Nevertheless, the court concluded that some of the insured's state tort claims failed as a matter of law. In particular, the insureds alleged that, by issuing and renewing the policy, the insurer misrepresented whether the property was eligible for federal flood insurance. The court held that the insureds could not reasonably rely on the insurer to make that determination for them and could not reasonably rely on the issuance of a policy as a representation that their property was not in the uninsurable zone. Further, FEMA's determination after Ike that the property was within the uninsurable zone was not within the insurer's control, and the insurer had a duty to the federal government not to use government funds to pay the insureds' claims after FEMA made its determination.

H. Waiver

Where an excess insurer constructively breached its contract by refusing to pay, relying inappropriately on an "other insurance" clause, the insurer waived any subrogation rights under the policy. *In re Deepwater Horizon*, 470 S.W.3d 452 (Tex. 2015).

X. PRACTICE & PROCEDURE

A. Appraisal

An appraisal award was not rendered without authority and substantially complied with the contract provision requiring an itemized award in *Cantu v. Southern Ins. Co.*, No. 03-14-00533-CV, 2015 WL 5096858 (Tex. App.—Austin Aug. 25, 2015, no pet.). Cantu suffered a fire loss and filed suit against her insurer. The insurer then invoked appraisal under the policy. Cantu later objected to the award in a separate proceeding on two grounds: that the trial court lacked authority to replace the initial umpire; and the award did not substantially comply with the contract because it was not an "itemized decision." The court first held that it did not have jurisdiction to consider her challenge, because the challenge to the replacement umpire was not raised in the original suit. However, the court went on to hold that even if it did consider the issue it would find that the trial court had authority to replace the umpire.

The court also rejected Cantu's argument that the award was not an itemized decision. While the award did not list amounts for each specific item, it did list separate amounts for the types of coverage – dwelling, personal property, additional living expense, and damage from testing – and broke those up by replacement cost, depreciation, and actual cash value. The court found this was sufficiently itemized and was substantial compliance with the contract.

The court held that the insurer waived any right to seek appraisal in *In re Guideone Nat'l Ins. Co.*, No. 05-15-00981-CV, 2015 WL 5050233 (Tex. App.—Dallas Aug. 27, 2015, orig. proceeding [mand. pending]). The insurer denied the claim, tendered payment for another claim in an amount the insured found unsatisfactory, and then waited six months after suit was filed before demanding appraisal under a provision that gave only the insurer the right to demand appraisal. The court reasoned that appraisal is intended to take place before suit is filed and that a party must demand an appraisal promptly after the parties reach an impasse in their negotiations. An impasse exists when there is a mutual understanding that neither party will negotiate further and that further negotiations are futile. The court concluded that there was no suggestion that the insurer believed further negotiations would be productive; therefore, it waived appraisal by its delay. The court noted that during the time the insurer delayed, the insured was required to incur the cost of hiring experts to assess and value damages for litigation, thereby reducing or eliminating entirely the efficiencies appraisal is intended to provide. The court of appeals concluded that the trial court did not abuse its discretion by declining to require the parties to go to appraisal. As of October 28, 2015, an application for writ of mandamus was pending in the Texas Supreme Court.

The court in *In re Guideone* also addressed the insurance company's argument that it could not waive the right to appraisal, because the policy contained a clause stating that no provision of policy could be waived except by a written endorsement issued by the insurance company. The court held that the terms of the contract weren't altered. Instead, the insurer simply chose not to take advantage of the provision allowing it to invoke appraisal.

In another case involving Guideone, the Amarillo court reached the opposite conclusion. *In re Guideone Nat'l Ins. Co.*, No. 07-15-00281-CV, 2015 WL 5766496 (Tex. App.—Amarillo

Sept. 29, 2015, orig. proceeding). The court found under the same policy language that the insurer could not waive its right to appraisal even though, when asked to submit to appraisal by the insured, the insurer declined but then later changed its mind. The court held that finding a waiver would require it to ignore the language of the contract. The court also rejected the insured's argument that a one-way appraisal clause that allowed only the insured to invoke it was void as against public policy.

It seems the Dallas court's analysis of Guideone's policy is more compelling. Neither court was required to ignore the appraisal clause or the non-waiver provision. As the first court construed it, the appraisal clause gave the insurer the right to choose appraisal. When Guideone chose not to accept appraisal, despite being invited to, that conduct should be considered a waiver of that provision in the contract. As the first court put it, that did not change the term in the contract; it merely demonstrated that the insurer exercised its choice and did not choose appraisal. Taking the second court's analysis literally goes too far. Under the second court's analysis Guideone could invoke appraisal at any point in the litigation – even after judgment – because the non-waiver clause meant it could never waive it without the court having to ignore the contract provision. At some point, a party by its conduct can waive the protections of a contract, even though the court honors the language of that contract.

Another court found it was an abuse of discretion not to order appraisal even though appraisal was not demanded by the insurer until after suit was filed and after the parties had hired experts, exchanged discovery, and mediated, in *In re Century Sur. Co.*, No. 07-15-00386, 2015 WL 6689532 (Tex. App.—Amarillo Nov. 2, 2015, org. proceeding [mand. pending]). The court considered whether the insured showed prejudice by the insurer's delay in invoking appraisal and concluded that the insured had not. Because the appraisal clause could be invoked by either party, the court concluded that the insured could have avoided any prejudice from the insurer's delay by simply invoking appraisal itself. The court distinguished the Dallas *In re Guideone* decision on the basis that in that case only the insurer could invoke appraisal so when it did not, the insured had no choice but to pursue litigation.

Another court found no waiver of appraisal even though the insurer invoked appraisal after litigation ensued and the insurer was successful in its motion for summary judgment on one of the claims. The court found the record supported the insurer's assertion that was when the parties reached the point of impasse. *Nassar v. Liberty Mut. Fire Ins. Co.*, No. 14-14-00277-CV, 2015 WL 5727667 (Tex. App.—Houston [14th Dist.] Sept. 29, 2015, pet. filed).

The *Nassar* court also found no evidence of fraud to vitiate the appraisal award, based on the difference in values between the insurer's estimate offered at mediation and the lower estimate offered at appraisal.

Finally, the *Nassar* court rejected the insured's argument that the award was invalid because the appraisers exceeded the scope of their authority by considering causation. The court relied on the supreme court's decision in *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 891 (Tex. 2009), where the court said, "Indeed, appraisers must always consider causation, at least as an initial matter."

Similarly in *In re Ooida Risk Retention Relators Group, Inc.*, 2015 WL 5223512 (Tex. App.—Fort Worth, Sept. 4, 2015, orig. proceeding), the court found no waiver of appraisal and no prejudice. In that case a truck belonging to Wells was damaged. The insurer offered $21,000, and the parties continued to negotiate. Eventually, Wells filed suit, but the parties continued to negotiate. In the meantime, the insurer had destroyed the truck based on the assertion by Wells that he did not want to keep it for salvage. The court held that the mere filing of suit did not indicate waiver, because it did not show the parties had reached an impasse. They continued to negotiate. Further, when the insurer invoked appraisal after suit was filed, Wells participated in the process for more than a year before raising the waiver argument.

The *Ooida* court also found no evidence that Wells was prejudiced by the delay. There was no showing that the destruction of the truck affected the appraisal process, and that occurred before that parties reached an impasse. A party must show prejudice based on delay after the point of impasse. Wells did not offer any other evidence of harm caused by any delay after the point of impasse.

A court found a policy was ambiguous regarding when payment was required so that the insurer was not entitled to summary judgment on its claim that it timely paid an appraisal award. The policy could be read to require payment within fifteen business days after notice by the insurer or within five business days after performance by the plaintiff. *Cody v. Am. Bankers Ins. Co of Florida*, No. 2:14-CV-00187-J, 2015 WL 6460007 (N.D. Tex. Oct. 21, 2015). The court erroneously held that interpretation of this ambiguous provision was an issue of fact, instead of construing it in favor of the insured as a matter of law.

After an insured and insurer could not agree on the price to repair the insured's damaged roof, the insurer invoked the appraisal clause. An appraisal award resulted in the insurer owing six times what the insurer initially paid to the insured. The insurer paid the appraisal award, and then the insured sued the insurer for breach of contract and unfair insurance practices. The court granted the insurer's motion for summary judgment, holding that there was no breach of contract as the insured accepted payment of the appraisal award. The court stated that generally an insured is precluded from maintaining a bad faith claim where his breach of contract claim fails, and that the insured's payment of legal fees and appraisal expenses did not suffice to show an independent injury. Moreover, the court stated that full and timely payment of the arbitration award precluded an award for penalties under the prompt payment provisions of the Insurance Code. *Barry v. Allstate Tex. Lloyds*, No. 4:14-CV-00870, 2015 WL 1470429 (S.D. Tex. March 31, 2015).

Another federal court felt compelled to add in dicta that compliance with the appraisal process and prompt payment of the award means that an insurer cannot be in breach of the contract and cannot be liable for prompt payment penalties or statutory or common law bad faith damages. *Igwe v. Safeco Ins. Co. of Indiana*, No. A-14-CV-587 LY, 2015 WL 6506391 (W.D. Tex. Oct. 27, 2015).

An insured tenant sued the insurer on a claim arising from the insurer's denial of adequate reimbursement for hurricane damage to the property. The court held that the insured was estopped from claiming that the insurer breached the contract due to the insurer's payment of the appraisal award. The insured's refusal to accept the payment tendered did not matter. The insurer's payment of the appraisal award also nullified the insured's extra-contractual claims, prompt payment claims, and claims under section 541. *United Neurology, P.A. v. Harford Lloyd's Ins. Co.*, No. H-10-4248, 2015 WL 1470296 (S.D. Tex. Mar. 31, 2015).

An insurer was entitled to summary judgment on the insureds' breach of contract claim where the insurer promptly paid an appraisal award. The court held that it is "well-settled under Texas law that the insurer 'may not use the fact that the appraisal award was different than the amount originally paid as evidence of breach of contact.'" The court held that the insureds were estopped from relying on the appraisal award to demonstrate that the insurer breached the policy when it initially assessed payment for an amount less than the appraisal award. *Graber v. State Farm*

Lloyds, No. 3:13-CV-2671-B, 2015 WL 3755030 (N.D. Tex. June 15, 2015).

B. Arbitration

The Texas Supreme Court held that federal law preempts and therefore allows enforcement of an arbitration clause between a nursing home and its patient. The court rejected the argument that the arbitration clause was invalid under Tex. Civ. Prac. & Rem. Code § 74.151, because that was not a "law regulating the business of insurance" saved by the McCarran – Ferguson Act. *Fredericksburg Care Co. v. Perez*, 461 S.W.3d 513 (Tex. 2015). A patient entered into an arbitration agreement with a nursing home. The agreement would be void under state law, because section 74.451 required a conspicuous notice and a signature by the patient's lawyer. In contrast, the arbitration agreement would be valid under federal law, which does not contain these requirements. The court first concluded that federal law would apply because the patient received Medicare payments, thus implicating interstate commerce. The court then considered whether under federal law the Texas statute was saved from preemption as a "law regulating the business of insurance." The court considered that chapter 74 as a whole was not a law regulating the business of insurance. While the statute imposed limitations on medical malpractice tort claims, reduction of insurance premiums was only a hoped-for result, not the direct result. The specific provision at issue also did not regulate the relationship between insured and insurer. The court concluded that the exception under federal law did not apply and, therefore, the arbitration clause was valid and enforceable.

A trial court abused its discretion by not severing unfair settlement claims from a breach of contract claim under an uninsured motorist's policy.

C. Declaratory Judgment

The Texas Supreme Court held that a plaintiff could not sue for a declaratory judgment establishing the tort defendant's coverage under a liability policy. *In re Essex Ins. Co.*, 450 S.W.3d 524 (Tex. 2014). The supreme court agreed that the rule barring any direct action against an insurer also barred the plaintiff's attempt to get declaratory relief on coverage. The court rejected the plaintiff's argument that prior decisions by the court held that parties can seek a declaratory judgment regarding an insurer's duty to indemnify even before the insured defendant's liability has been determined. The court pointed out that prior cases had only allowed declaratory relief sought by the defendant or the defendant's insurer, but not by the plaintiff. The court reasoned that allowing a plaintiff to seek declaratory relief against the defendant's insurer would create a conflict of interests for the insurer between its duty to defend its insured and its effort to negate coverage in the declaratory judgment suit and would necessarily require admission of evidence of liability insurance in violation of Tex. R. Evid. 411. The court therefore granted mandamus relief.

The problem with the court's analysis is the plaintiff did exactly what the court told parties to do in *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696 (Tex. 1996). There, the current chief justice wrote for a unanimous court encouraging defendants, insurers, and plaintiffs to seek declaratory relief determining the duty to indemnify, even before the underlying liability was established. The unanimous opinion states:

> Disputes between *I* and *D* can often be expeditiously resolved in an action for declaratory judgment while *P's* claim is pending. … We recognize that prosecution of a declaratory judgment may be burdensome to *D*, but often *I* will assume the burden of having the issues resolved. *A plaintiff who thinks a defendant should be covered by insurance may be willing to await or even assist in obtaining an adjudication of the insurer's responsibility.*

Id. at 714. (emphasis added). If the court has reconsidered this dicta, it should say so, and not pretend it does not exist.

Further, the reasons the court gives for precluding a declaratory judgment suit by a plaintiff, while it is allowed by a defendant or insurer, make no sense. The court says that the *plaintiff's* suit is barred because it creates a conflict of interests for the insurer. But that is true whenever an insurers is allowed to seek declaratory relief on its duty to indemnify. That certainly creates just as much of a conflict between the insurer's duty to defend the insured and its effort to avoid coverage.

D. Choice of Law

In *Zurich American Ins. Co. v. Cabot Oil & Gas Corp.*, No. 4:14-CV-2735, 2015 WL 5604068 (S.D. Tex. Sept. 23, 2015), an employee of an insured company was injured on the job by a ruptured separator on an oil well. The employee received worker's compensation benefits from his employer's insurer. He then filed a personal injury suit against his employer in West Virginia. The insurer then filed suit in Texas for declaratory judgment that the policy did not cover the claims in the underlying suit. The court held that West Virginia law applied in making the determination on the insurer's motion for summary judgment, because the policy contained a specific provision for insured risks in West Virginia – that the policy does not cover "bodily injury intentionally caused … by your deliberate intention as that term is defined…." in a West Virginia statute. The court granted the insurer's motion for summary judgment, finding the acts by the employer were intentional under the statute.

E. Jurisdiction

A district court determined that it had personal jurisdiction over a flooring manufacturer in a declaratory judgment action brought by a liability insurer against the manufacturer. *Maxum Indem. Co. v. BRW Floors, Inc.*, No. 5:15-CV-00167-RCL, 2015 WL 5881584 (W.D. Tex. Oct. 7, 2015). The manufacturer was impleaded into the underlying suit by the insured, which prompted the manufacturer to seek defense and indemnity from the insurer. The manufacturer did not challenge personal jurisdiction in the underlying suit. The manufacturer was not a resident of Texas, not licensed in Texas, and had no office, assets, or agent in Texas. But the district court concluded that it had personal jurisdiction over the manufacturer because it intentionally marketed and distributed products in Texas. It was thus foreseeable that the manufacturer "may be required to litigate claims arising from both the product and the contract insuring the product in the states where it purposefully directs and sells that product." Further, the manufacturer engaged in conduct in Texas for which it sought indemnification and defense under the insurance agreement.

F. Severance & Separate Trials

A trial court abused its discretion by not severing unfair settlement claims from a breach of contract claim under an uninsured motorist's policy, but did not abuse its discretion by declining to sever misrepresentation claims. *In re Allstate Cnty. Mut. Ins. Co.*, 447 S.W.3d 497 (Tex. App.—Houston [1st Dist.] 2014, no pet.). The court of appeals concluded that the claims for unfair settlement would be rendered moot if the plaintiffs could not establish their claim for breach of contract. Further, the court held that requiring the insurer to provide broad discovery on its claims handling, to be admitted into the breach of contract case, would be manifestly unjust. Finally, the court concluded that severance of the plaintiff's unfair settlement claims from the breach of contract claim would not prejudice the parties' rights.

In contrast, the court found no abuse of discretion by not severing the misrepresentation claims from the claim for breach of contract. The plaintiffs alleged in the alternative that, if there was no coverage under the policy, then the insurance agent, agency, and Allstate were liable for misrepresenting coverage. The court held that this contention would not be rendered moot by a finding of no breach of contract, and the insurer did not demonstrate how it would be prejudiced by being required to prepare for and litigate both causes of action.

G. Discovery

A trial court did not abuse its discretion by ordering State Farm to produce discovery in native or near-native form. State Farm failed to produce evidence showing the specific undue burden of producing the electronically stored information in that format. The plaintiffs produced evidence that State Farm already provided the data in native and near-native format to itself and defense counsel, but offered downgraded information to plaintiffs for discovery and litigation. The "reasonably useable" alternative State Farm offered was incomplete and lacked essential information. *In re State Farm Lloyds*, No. 13-14-00616-CV, 2015 WL 6520998 (Tex. App.—Corpus Christi Oct. 28, 2015, orig. proceeding) (per curiam).

H. Experts

The Fifth Circuit addressed the exclusion of expert testimony on bad faith in *Weiser-Brown Operating Co. v. St. Paul Surplus Lines Ins. Co.*¸ 801 F.3d 512 (5th Cir. 2015). The court concluded that the district court did not abuse its discretion by excluding the proffered testimony that the insurer violated an accepted practice in the insurance industry when it failed to send the insured a reservation of rights letter. The expert had no recent experience in claims adjusting, all of his recent experience was from the perspective of the insured making insurance claims, and he could not explain how the Insurance Code required the insurer to send a reservation of rights letter. Under these circumstances, the court found the district court did not abuse its discretion in excluding the testimony.

A jury verdict finding that a homeowner's claim for water damage was not caused by a plumbing leak was supported by expert testimony in *Gulley v. State Farm Lloyds*, 461 S.W.3d 563 (Tex. App.—San Antonio 2014, pet. filed). The insured and insurer presented competing expert testimony supporting their respective positions. The court found that the expert testimony of the insurer's expert was not speculative and conclusory. His opinion that there was no heave at the site of the plumbing leaks, which would indicate that the plumbing leaks were not the cause of the movement, was supported by three sets of elevations and three contour diagrams he relied on, and he had explained his reasoning process within the context of accepted scientific principles. The court also found his opinion that seasonal moisture fluctuations were the cause of the damage, having ruled out the plumbing leaks as the cause, was reliable. The expert provided the factual and logical foundation and supporting engineering principles and texts for his testimony on this point. The court also found sufficient grounds for the expert's opinion that continued movement after the leaks were repaired showed that seasonal moisture was the cause of the damage.

A homeowner could not support his claim that the insurer's instructions to stop drying the house caused additional mold damage, without an expert to support that claim. The court reasoned that the cause of any specific mold infestation is not a subject within the general experience or common sense of a layperson and thus requires expert testimony. *Igwe v. Safeco Ins. Co. of Indiana*, No. A-14-CV-587 LY, 2015 WL 6506391 (W.D. Tex. Oct. 27, 2015).

An attorney did not have to be "highly qualified" to be qualified to give expert opinions on the reasonableness of attorney's fees. *Yowell v. Seneca Specialty Ins. Co.*, No. 4:15CV80-LG-CMC, 2015 WL 4575450 (E.D. Tex. July 28, 2015). The court held that objections to the summary judgment affidavit went to the weight, not the admissibility, of the expert opinions, where they challenged his failure to identify similar cases he had handled, his failure to state how much of his practice related to the relevant area, his failure to state whether he represented insurers or policyholders, and his failure to attach his resume.

I. Evidence

A party seeking a remedy for spoliation of evidence must demonstrate that the other party breached its duty to preserve material and relevant evidence. A court found that a title insurance company had a duty to preserve evidence, even though its representative did not believe the dispute would result in litigation, where litigation objectively should have been anticipated. *IQ Holdings, Inc. v. Stewart Title Guar. Co.*, 451 S.W.3d 861 (Tex. App.—Houston [1st Dist.] 2014, no pet.). However, there was no spoliation where there was evidence from which the court could have concluded that all the material documents were preserved.

J. Removal and Remand

Joining an "abundance" of case law supporting adjuster liability, yet another federal court remanded a suit to state court after removal based on a claim that the adjuster was improperly joined. *Linron Props., Ltd. v. Wausau Underwriters Ins. Co.*, No. 3:15-CV-00293-B, 2015 WL 3755071 (N.D. Tex. June 16, 2015). The court noted that, "A few courts have recently begun to question the appropriateness of holding an adjuster individually liable for unfair settlement practices under section 541.060." *4. The court explained why those cases are wrongly decided. The statute specifically prohibits "failing to attempt in good faith to *effectuate* a prompt, fair, and equitable settlement." (Emphasis added). The court reasoned that the word "effectuate" means "to cause to come into being" or "to bring about." The court reasoned, "The fact that the statute uses the word 'effectuate' rather than a word that conveys finality (e.g., finalized), suggests that its prohibition extends to all persons who play a role in bringing about a prompt, fair, and equitable settlement of a claim." *5. The plaintiff alleged sufficient facts that the adjuster violated this prohibition by retaining an engineering contractor known for arriving at pro-insurer findings, refusing to identify damage, and failing to respond to inquiries regarding the status of the claim. The court therefore granted the motion to remand, finding no improper joinder of the adjuster. *See also Glidewell v. Safeco Ins. Co. of Indiana*, No. 3:15-CV-1099-G (N.D. Tex. Aug. 13, 2015) (finding no improper joinder of adjuster and remanding); *Denley Group, L.L.C. v. Safeco Ins. Co. of Indiana*, No. 3:15-CV-1183-B, 2015 WL 5836226 (N.D. Tex. Sept. 30, 3015) (granting motion to remand).

In contrast, another court found the insurer met its "heavy burden" to show improper joinder of the adjuster and denied the motion to remand in *Mainali Corp v. Covington Spec. Ins. Co.*, No. 3:15-CV-1087-D, 2015 WL 5098047 (N.D. Tex. Aug. 31, 2015). The court held that the adjuster could not be liable under Chapter 541 for "failing to attempt in good faith to effectuate a prompt, fair, and equitable settlement," because as an adjuster he did not have settlement authority on behalf of the insurer. *Id.* at *4. The court held that the adjuster could not be liable under certain provisions of Chapter 541 prohibiting misrepresentations, because the misrepresentations related to the claim, not the policy. While the court assumed the adjuster could be held liable under other provisions prohibiting misrepresentations, the court found insufficient factual allegations and found that the plaintiff made only conclusory allegations. *Id.* at *5.

The *Mainali* court also held that the adjuster could not be liable under any section of Chapter 542, the Prompt Payment of Claims Act, because that statute specifically applies only to insurers, not adjusters. The court held that the plaintiff failed to state a claim against the adjuster under the DTPA, because they merely incorporated the Insurance Code violations. Finally, the court held there was no reasonable factual basis supporting the allegations of fraud against the adjuster.

Another court denied a motion to remand, finding that a nondiverse defendant was improperly joined in *Davis v. State Farm Lloyds*, No. 3:15-CV-0596-B, 2015 WL 4475860 (N.D. Tex. July 21, 2015). Insured homeowners sued their diverse insurer and non-diverse agent relating to improper handling of an insurance claim. The insurer removed on grounds that the agent was improperly joined, and the insureds sought a remand. Regarding the agent, the insureds alleged that he misrepresented the coverage. But the insureds' pleading did not include information about the event that caused the damage, the nature or extent of the damage, or the circumstances underlying the denial of coverage. The court found that the agent was improperly joined because the insureds failed to state a claim against him by failing to allege any facts to indicate how the elements of the causes of action were met. *See also Monclat Hospitality, L.L.C. v. Landmark American Ins. Co.*, No. 4:15-CV-632-A, 2015 WL 5920757 (N.D. Tex. Oct. 8, 2015) (denying motion to remand).

Similarly, the court denied the motion to remand in *Aguilar v. State Farm Lloyds*, No. 4:15-CV-565-A, 2015 WL 5714654 (N.D. Tex. Sept. 28, 2015). The plaintiff did not identify any specific fraudulent representations. Although he alleged conspiracy, the plaintiff did not show that the adjuster was acting outside the scope of his employment for his own personal benefit, which conspiracy requires between a corporation and its agent. Finally, the court held the claims under the Insurance Code were not viable, because they arise out of the contractual relationship between the insurer and insured, and adjusters do not have a contractual relationship with the insured. The court further reasoned that an adjuster cannot be held liable for a violations of the Insurance Code unless he causes an injury distinguishable from the insured's actions.

The court in *Aguilar* got it wrong on its insurance code holdings. The Insurance Code provides its own liability standards and is distinct from the common law duty of good faith and fair dealing arising from the parties' contractual relationship. The court has engrafted onto the statute additional requirements not provided by the statutory text.

K. Multidistrict litigation

Farmers sought to have an MDL pretrial court created for 1565 wind and hail damage cases pending in 166 courts in forty-four counties. The claims arose primarily from eight major storms and several lesser storms that occurred between February 29, 2012, and June 11, 2014. The insurance policies involved in the cases contained substantially the same coverage language, and the plaintiffs in each case alleged that Farmers implemented standard business practices designed to minimize payments to the insureds and maximize profits to the insurer. *In re Farmers Ins. Co. Wind/Hail Storm Litig.*, No. 14-0882, 2015 WL 5098061 (Tex. J.P.M.L., Apr. 7, 2015). The Panel held that the suits were related and ordered that the cases be transferred to three courts for consolidated pretrial proceedings and discovery under Rule 13. In reaching its decision, the Panel found that transfer would further the interests of convenience, efficiency, and justice by avoiding requiring "dozens of trial judges to adjudicate the same issues again and again" or for the same discovery to be duplicated across the various cases. The Panel additionally held that the suits were sufficiently related both because of the "business practices" allegations, which broadened the plaintiffs' claims to seek discovery beyond the facts of their individual losses, and because of the "close proximity" of the suits, since they occurred in eight major groups in contiguous counties over the same two-year period. The Panel rejected the plaintiffs' argument that granting Farmer's motion would give it a "perpetual MDL" because the tag-along procedure would not cover cases arising from new storms occurring outside of the two-year period.

The insurance policies involved in the cases contained substantially the same coverage language, and the plaintiffs in each case alleged that Farmers implemented standard business practices designed to minimize payments to the insureds and maximize profits to the insurer.

XI. OTHER ISSUES

A. Excess & Primary Coverage

A primary insurer tendered a lawsuit to the excess insurer once its policy limits were exhausted. The excess insurer argued that the primary insurer wrongfully refused to defend and indemnify the insured. The disagreement was over whether "expenses" included defense costs in exhausting policy limits, which the primary insurer believed it did. The appellate court agreed with the primary insurer, holding that the ordinary meaning of "expense" included attorneys' fees, as this is an expense to the insurer. Therefore, the primary insurer did not breach its duty to defend and indemnify, as the policy limits were exhausted when it tendered the case to the excess insurer. *Amerisure Mut. Ins. Co. v. Arch Specialty Ins. Co.*, 784 F.3d 270 (5th Cir. 2015).

An insured was sued by various governmental entities for failing to remit hotel taxes collected from consumers. After litigation ensued, the primary insurer notified the insured that the primary policy had been fully exhausted. The excess insurer argued that the insured did not timely report the claim. The court held in favor of the insured, stating that the general notice provision in the excess policy requiring that notices under the excess policy be given as provided in the primary policy could not apply to the specific provision regarding exhaustion of limits when there is no corresponding provision in the primary policy. *Illinois Union Ins. Co. v. Sabre Holdings Corp.,* No. 02-14-00130-CV, 2015 WL 3917981 (Tex. App.—Fort Worth June 25, 2015, pet. filed).

In *L-Con, Inc. v. CRC Ins. Services, Inc.*, No. 4:13-CV-1526, 2015 WL 4724799 (S.D. Tex. Aug. 24, 2015), employees of L-Con were injured and killed while working at another company's oil facility. The court held that the oil facility was an additional insured under L-Con's insurance policy, as the injuries would not have occurred "but for" the work and operations being performed by L-Con employees. The oil facility had its own insurance policy, but the court held that the "other insurance" provisions in both insurance policies at issue were in conflict. Therefore, the court ignored the offending provisions and prorated the liability between the policies up to the applicable limits, with L-Con's insurance policy providing the first layer of excess coverage.

** Mark L. Kincaid is a partner in George Brothers Kincaid & Horton, L.L.P. He graduated from the University of Texas Law School and teaches Texas Insurance Litigation there as an adjunct professor. He is co-author of West's Texas Practice Guide on Insurance Litigation (2015) and has written and spoken frequently on insurance and consumer issues.*

*** Suzette E. Selden graduated with highest honors from Brigham Young University with a B.A. (2002) and with honors from the University of Houston Law Center (2006).*

**** Elizabeth von Kreisler graduated from Reed College with a B.A. (2002) and with high honors from the Texas Tech University School of Law (2007).*

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1 Tex. S.B. 1628, 84th Leg., R.S. (2015). The bill as introduced can be found at Texas Legislature Online, http://www.capitol.state.tx.us/tlodocs/84R/billtext/pdf/SB01628I.pdf#navpanes=0.

2 Tex. H.B. 3646, 84th Leg., R.S. (2015). The bill as introduced can be found at Texas Legislature Online, *http://www.capitol.state.tx.us/tlodocs/84R/billtext/pdf/HB03646I.pdf#navpanes=0*.

3 *See* Angela Morris, *Diverse Opposition Kills Hailstorm Bill*, Tex. Lawyer (May 26, 2015); Angela Morris, *Hailstorm Bill Opponents Fear Rebirth in Insurance Bill*, Tex. Lawyer (May 26, 2015); Mark Curriden, *Texas Businesses Oppose "Crazy, Wacky Bill" Protecting Insurance Companies from Property Owners*, Tex. Lawbook (May 22, 2015). The issue may come back. The lobbyists supporting the bills have vowed to return in 2017. In the meantime, the Texas Senate and House have added "hailstorm lawsuits" to the list of items to be studied in the interim. *See* Angela Morris, *Interim Charges Revive Dead Hailstorm, Prompt Pay Bills*, Tex. Lawyer (Oct. 16, 2015); Angela Morris, *House Committee to Study Hot-Button Issues*, Tex. Lawyer (Nov. 10, 2015).

Will *El Apple* Today Keep Attorneys' Fees Away?

by Mark E. Steiner*

I. Introduction

Beginning in 1997 with its decision in *Arthur Andersen v. Perry Equip. Corp.*,[1] the Texas Supreme Court has issued several opinions that have changed how parties prove their entitlement to attorneys' fees. In 2006, the court reviewed the necessity of segregating attorneys' fees in *Tony Gullo Motors I, L.P. v. Chapa*.[2] More recently, the court issued *El Apple I, Ltd. v. Olivas* (2012) and two subsequent *per curiam* opinions (2013 and 2014) that address whether contemporaneous time records are required in "lodestar" cases (although what's a "lodestar" case is far from clear).[3] It's not a coincidence that all these decisions are designed to limit the recovery of attorneys' fees. These attorneys' fee opinions should be considered part of the court's larger agenda of consistently issuing pro-defense, anti-plaintiff opinions.[4]

This article reviews the recent caselaw on recovery of attorneys' fees in Texas, with a particular emphasis on the post-*El Apple* landscape.

II. *Arthur Andersen* and Contingent Fees

The Texas Supreme Court began tightening proof requirements for recovery of attorneys' fees in *Arthur Andersen v. Perry Equip. Corp.*[5] The plaintiff sued under the DTPA, which, of course, mandates the recovery of reasonable and necessary attorneys' fees for prevailing plaintiffs. Although the supreme court never mentioned what evidence in support of attorneys' fees was provided at trial, apparently the plaintiff had followed the then-common practice of merely entering the contingent fee into evidence. The jury charge asked the jury to calculate attorneys' fees in dollar and cents, as a percentage of plaintiff's recovery, and as a combination of dollars and cents and percentage of recovery. (The supreme court also never mentioned what the jury awarded for attorneys' fees.)[6]

It's not a coincidence that all these decisions are designed to limit the recovery of attorneys' fees.

The court first rejected the practice of the plaintiff asking the jury to award a percentage of the recovery, holding that the jury must be asked to award fees in a specific dollar amount. Second, the court held that proof of a contingent fee contract alone was insufficient. The court reasoned:

> [W]e do not believe that the DTPA authorizes the shifting of the plaintiff's entire contingent fee to the defendant without consideration of the factors required by the Rules of Professional Conduct. A contingent fee may indeed be a reasonable fee from the standpoint of the parties to the contract. But, we cannot agree that the mere fact that a party and a lawyer have agreed to a contingent fee means that the fee arrangement is in and of itself reasonable for purposes of shifting that fee to the defendant.[7]

A plaintiff seeking recovery of reasonable attorneys' fees had to provide some evidence of reasonableness. The court stated, "a fact-finder should consider" the factors listed in the Disciplinary Rules:

> (1) the time and labor required, the novelty and difficulty of the questions involved, and the skill required to perform the legal service properly;
> (2) the likelihood . . . that the acceptance of the particular employment will preclude other employment by the lawyer;
> (3) the fee customarily charged in the locality for similar legal services;
> (4) the amount involved and the results obtained;
> (5) the time limitations imposed by the client or by the circumstances;
> (6) the nature and length of the professional relationship with the client;
> (7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and
> (8) whether the fee is fixed or contingent on results obtained or uncertainty of collection before the legal services have been rendered.[8]

The court stated that "the plaintiff cannot simply ask the jury to award a percentage of the recovery as a fee because without evidence of the factors identified in Disciplinary Rule 1.04, the jury has no meaningful way to determine if the fees were in fact reasonable and necessary."[9] The court also concluded that "a party's contingent fee agreement *should* be considered by the factfinder." The court again used "should" instead of "must" just as it had done with the consideration of the factors from the Disciplinary Rules ("a fact-finder *should* consider"). The court's use of "should" instead of "must" provides considerably less guidance for bench and bar.

Thus, DTPA plaintiffs were left with this rule:

> [T]o recover attorney's fees under the DTPA, the plaintiff must prove that the amount of fees was both reasonably incurred and necessary to the prosecution of the case at bar, and must ask the jury to award the fees in a specific dollar amount, not as a percentage of the judgment.[10]

The aftermath of *Arthur Andersen* was hardly apocalyptic. Attorneys adjusted, and routinely presented testimony on the factors establishing a "reasonable fee."[11] There don't seem to be a lot of reversals because of the plaintiff's failure to establish the *Arthur Andersen* factors.

There have been a couple of Court of Appeals opinions, however, that are worth noting. In *Robertson County v. Wymola*, the plaintiff realized that an attorney fee recovery based upon hours would yield more than a recovery based upon the contingent fee. Consequently, the plaintiff didn't enter its contingent fee agreement into evidence and instead presenting testimony on reasonable fees and hours. The defendant argued that the plaintiff had to enter its fee agreement into evidence to recover attorneys' fees. The plaintiff countered that evidence of the nature of the attorney-client fee arrangement was irrelevant because the testimony was about the regular hourly rate without making any adjustment for the risk involved in a contingent fee case. The trial court refused to order the admission of the contingent fee contract into evidence. The court of appeals held that the trial court didn't abuse its discretion by excluding the fee agreement because the supreme court in *Arthur Andersen* only said that evidence of a contingent fee arrangement was "admissible" and "should" be considered by the fact finder–the supreme court didn't mandate that such evidence must be admitted or considered.[12]

The *Arthur Andersen* court held that a plaintiff couldn't just enter its fee agreement into evidence and ask for a percentage of recovery. But could a plaintiff enter its fee agreement into evidence, offer testimony on the factors from the Disciplinary Rules, and then ask for a percentage of the recovery as per its fee agreement? In *VingCard A.S. v. Merrimac Hosp. Sys., Inc.*, the defendant on appeal argued that plaintiff's counsel ran afoul of *Arthur Andersen* by asking the jury to calculate attorney's fees only as a percentage of the judgment, rather than any specific amount. Plaintiff's counsel had outlined the rule 1.04 factors and had provided information regarding each factor. He had testified that his 30% contingency fee was less than the contingency fee charged in similar cases. He had explained to the jury how to calculate fees based on the amount of damages they awarded, e.g. if the jury awarded $10 million in damages, his fee should be $3 million based on the 30% contingency fee. The court of appeals held that was not reversible error.[13]

III. *Tony Gullo Motors* and Segregating Recoverable and Unrecoverable Fees

Suppose a consumer's attorney brings a lawsuit and alleges both common-law fraud and DTPA violations. At time of trial, the attorney has put in 100 hours on the case. How many hours of the attorney's time are recoverable? That depends. The problem is that the fraud claim doesn't give rise to attorneys' fees while the DTPA claim does. The problem is avoided if all the time spent on the fraud cause of action doubles as time spent on the DTPA claim. The argument would be that the claims are so interrelated that the work on the two claims can't be separated.

The Texas Supreme Court rejected this resolution of the proof problem in *Tony Gullo Motors I, L.P. v. Chapa* in 2006.[14] The court began by stating the long-standing rule that recovery of attorneys' fees isn't allowed unless authorized by statute or contract. Consequently, plaintiffs had always been required to segregate fees between claims for which they are recoverable and claims for which they are not. The court then lamented that its earlier decision in *Stewart Title Guaranty Co. v. Sterling* had created an exception that had swallowed the rule. The *Sterling* exception to the duty to segregate arose when attorneys' fees were sought in connection with "claims arising out of the same transaction and are so interrelated that their prosecution or defense entails proof or denial of essentially the same facts."[15] The court in *Tony Gullo* disapproved this language from *Sterling* because, in practice, every claim had become "inextricably intertwined" and interrelated.[16] The court explained:

> It is certainly true that [plaintiff's] fraud, contract, and DTPA claims were all "dependent upon the same set of facts or circumstances," but that does not mean they all required the same research, discovery, proof, or legal expertise…. To the extent *Sterling* suggested that a common set of underlying facts necessarily made all claims arising therefrom "inseparable" and all legal fees recoverable, it went too far.[17]

But the court also conceded "many if not most legal fees in such cases cannot and need not be precisely allocated to one claim or the other." It noted:

> Many of the services involved in preparing a contract or DTPA claim for trial must still be incurred if tort claims are appended to it; adding the latter claims does not render the former services unrecoverable. Requests for standard disclosures, proof of background facts, depositions of the primary actors, discovery motions and hearings, voir dire of the jury, and a host of other services may be necessary whether a claim is filed alone or with others.[18]

The court concluded, "To the extent such services would have been incurred on a recoverable claim alone, they are not disallowed simply because they do double service."[19]

After *Tony Gullo*, plaintiffs were left with this rule for segregating attorney fee awards: If any attorney's fees relate solely to a claim for which such fees are unrecoverable, a claimant must segregate recoverable from unrecoverable fees. Intertwined facts do not make tort fees recoverable; it is only when discrete legal services advance both a recoverable and unrecoverable claim that they are so intertwined that they need not be segregated.[20]

Unlike the *Arthur Andersen* factors, the mandate from *Tony Gullo* on segregation has proved harder for plaintiffs and their attorneys to follow.[21] In one recent case where the failure to segregate at trial led to a reverse and remand on appeal, the trial court had "repeatedly admonished" the party about segregation. Agreeing with appellant that the failure to segregate was erroneous, the court of appeals stated, with seeming regret, that the remedy was a reverse and remand, not a reverse and render, "however willful and ill-considered the refusal to segregate was."[22]

In *Prudential Ins. Co. v. Durante*, the plaintiff sued for breach of contract, violation of the Prompt Payment Statute, common-law and statutory bad faith, negligence, and Texas Insurance Code violations.[23] At trial, the plaintiff made no attempt to segregate fees and was awarded $200,000 in attorneys' fees. The attorney for plaintiff testified as follows:

> The only other point I wish to make is that I have not attempted to segregate fees in this case, because there are essentially to some degree three lawsuits that were being litigated. However, the facts of one and the facts of all are the same. It is my opinion that it's not really possible to tease out any particular part of any claim or cause of action, because the facts of the three cases are so interrelated that it was all going to be generated whether or not there was a claim against Mr. Schmid directly or it was just against Prudential.[24]

The problem with this testimony is that it seems to be based upon an approach to segregation that was explicitly rejected in *Tony Gullo*.

The outright refusal to segregate fees is a near-guarantee of reversal. Moreover, the courts of appeals haven't been asking for much; they are typically satisfied with an approximation, an opinion, from the attorney about the percentage of work that went into the recoverable claim.[25] Thus, the El Paso Court of Appeals in *Durante* lamented, "Pierce made no effort to estimate a possible segregation of fees in his testimony. While the standard does not mandate the maintenance of separate time records when drafting the different claims, an opinion would be sufficient as to the percentages of segregation as to the claims."[26] The court then ordered a reversal and remand because of the failure to segregate.

Durante wasn't the only recent case where the plaintiff refused to segregate fees at trial and the court of appeals reversed the award of attorneys' fees. In *Jackson Walker, LLP v. Kinsel*, the plaintiffs pursued "claims for which fees could and could not be awarded"; however, their attorneys didn't segregate fees, maintaining the claims were "inextricably intertwined."[27] One lawyer testified that "whatever cause of action the plaintiffs have in this case, the facts basically relate to each of the causes of action. There's not a whole lot of difference between them as far as the facts go. It's the different aspects of the law that apply to the facts that are different, but the facts and basically everything is intertwined and you can't separate those things as between the causes of action."[28] Again, this looks like the approach toward "intertwined facts" that the supreme court rejected in *Tony Gullo*.

In rejecting this "intertwined" argument, the court provided an excellent summary of the current law on segregating attorneys' fees.

> As for the matter of segregation of recoverable from unrecoverable fees, that normally is required. An exception exits, however. It arises when discrete legal services advance both recoverable and unrecoverable claims that are so intertwined that the fees need not be segregated.

The burden to illustrate that the exception applies lies with the fee claimant. And, it is not satisfied by simply suggesting that the causes of action for which fees are and are not recoverable required proof of the same set of facts and circumstances. In other words, intertwined facts alone do not make unrecoverable fees recoverable.[29]

The court concluded that the record "failed to establish that discrete legal services provided by those representing the Kinsels advanced both claims for which fees were recoverable and claims for which they were not. Segregation was necessary and the failure to do so obligates us to remand the issue of segregation for new trial."[30]

IV. *El Apple* and Sufficiency of Proof of Attorneys' Fees

A. *El Apple I, Ltd. v. Olivas*

The most significant recent development from the Texas Supreme Court concerning the recovery of attorneys' fees has been *El Apple* and the two cases that followed it.[31] Moreover, there also have been a considerable number of court of appeals opinions sorting out the impact of *El Apple*.

El Apple involved the calculation of an attorney's fees award in an employment discrimination and retaliation lawsuit brought under the Texas Commission on Human Rights Act. The plaintiff recovered $104,700 on her retaliation claim, and the court awarded $464,000 in attorney's fees for the trial of the case. The attorney's fee award included a 2.0 multiplier. On appeal, the defendant challenged both the sufficiency of the evidence for the award of attorney's fees and the enhancement of the award.

The most significant recent development from the Texas Supreme Court concerning the recovery of attorneys' fees has been *El Apple* and the two cases that followed it.

Texas courts have used the lodestar method for calculating fee awards under the TCHRA because the state law mirrors federal law and federal courts use the lodestar method for Title VII claims. Justice Medina described the lodestar method as follows:

> Under the lodestar method, the determination of what constitutes a reasonable attorney's fee involves two steps. First, the court must determine the reasonable hours spent by counsel in the case and a reasonable hourly rate for such work. The court then multiplies the number of such hours by the applicable rate, the product of which is the base fee or lodestar. The court may then adjust the base lodestar up or down (apply a multiplier), if relevant factors indicate an adjustment is necessary to reach a reasonable fee in the case.[32]

The court also noted how attorney's fees under Texas class action law also mandated the use of the two-step lodestar method.[33]

The sticking point in *El Apple* wasn't the hourly rate but the amount of hours expended. The court noted that the starting point for determining a lodestar fee award is the number of hours "reasonably expended on the litigation." The party applying for the award has the burden of proof. Proof of reasonable hours should include the basic facts underlying the lodestar, which are: "(1) the nature of the work, (2) who performed the services and their rate, (3) approximately when the services were performed, and (4) the number of hours worked."[34]

The question that *El Apple* was somewhat evasive in answering was whether contemporaneous time records are required to prove the hours reasonably expended on the litigation. The court began by noting that a party has "the burden of documenting the hours expended on the litigation and the value of those hours." It noted the defendant's argument that documenting the hours meant providing "contemporaneous time sheets, which evidence the performance of specific tasks, such that the trial court can make a reasoned determination of how much time was reasonably spent pursuing the litigation."[35]

The court recognized that previous Texas courts had not routinely required billing records or other documentary evidence to substantiate a claim for attorney's fees. The court then meekly offered that this "requirement has merit in contested cases under the lodestar approach." It next accepted the proposition that contemporaneous time records were probably a good idea; however, it didn't mandate their use. To establish the basic facts underlying the lodestar amount, the court said, "An attorney could, of course, testify to these details, but in all but the simplest cases, the attorney would *probably* have to refer to some type of record or documentation to provide this information."[36] The court concluded,

> Thus, when there is an expectation that the lodestar method will be used to calculate fees, attorneys *should* document their time much as they would for their own clients, that is, contemporaneous billing records or other documentation recorded reasonably close to the time when the work is performed.[37]

The affidavits provided by the attorneys at the hearing on the fee application fell short of the proof that is necessary to show the hours were "reasonably expended." Neither attorney indicated how their time was devoted to any particular task or category of tasks. Neither attorney presented time records or other documentary evidence. The attorneys gave time estimates based upon the amount of discovery in the case, the number of pleadings filed, the number of witnesses questioned, and the length of the trial. The court determined that "none of the specificity needed for the trial court to make a meaningful lodestar determination" had been provided. The trial court could not discern from the evidence how many hours each of the tasks required and whether that time was reasonable.[38]

B. *Long v. Griffin* and *City of Laredo v. Montano*

The court in *El Apple* defined the lodestar method as a two-step method that involved first arriving at a base fee or lodestar amount and then adjusting that amount up or down. The court specified two situations where such a method was to be used: TCHRA claims and class-action lawsuits. Since 2012, the Texas Supreme Court (and some courts of appeals) have used the term "lodestar" in a much looser manner. The supreme court issued per curiam opinions in 2013 and 2014 that addressed *El Apple* and both opinions are inconsistent with *El Apple* on when the lodestar method applies.[39]

Both *Long v. Griffin* and *City of Laredo v. Montano* appear to apply the term "lodestar" to any situation that involves recovering attorneys' fees on the basis of "reasonable hours times reasonable rate." There is no sense that lodestar is a two-step process, which is how the court had described it in *El Apple*. The court may have realized that the United States Supreme Court in *Perdue v. Kenny A. Ex rel. Winn* had signaled the end of enhancement.[40] The *Perdue* court took a very limited view of when a multiplier would be appropriate in a lodestar case. The Texas Supreme

Court may have concluded that there's no point in referring to a two-step method when there isn't going to be second step. Both cases also stated that the attorneys "chose" the lodestar method by the manner in which they attempted to prove the amount of attorneys' fees.

In *City of Laredo v. Montano*, the court first noted that the "fee-shifting statute in this case, however, does not require that attorney's fees be determined under a lodestar method, as in *El Apple*." That statement seemingly follows the narrow definition of lodestar from *El Apple*, and would limit its application to TCHRA claims and class-action lawsuits. But that sentence was immediately followed by this one: "The property owner nevertheless chose to prove up attorney's fees using this method and so our observations in *El Apple* have similar application here." The court did not explain how the plaintiff chose the lodestar method. Certainly, there is nothing to indicate that the plaintiff asked for a multiplier. It appears that testifying about hours and hourly rates triggered a "lodestar" designation, which, in turn, triggered the proof requirements for a lodestar fee suggested in *El Apple*. But, the court says, that doesn't necessarily mean "that a lodestar fee can only be established through time records or billing statements" as an attorney could testify to the details of his or her work. Then again, the court notes that *El Apple* already warned that "in all but the simplest cases, the attorney would probably have to refer to some type of record or documentation to provide this information."[41] The court then recalled that *El Apple* "encouraged attorneys using the lodestar method to shift their fee to their opponent to keep contemporaneous records of their time." All in all, this opinion is remarkably passive-aggressive. The court also appears very unwilling to say what it is exactly requiring in these cases. It's safe to say that contemporaneous time records are sorta, kinda required.[42]

The court the reviewed the proof offered in the trial court. The court held that one of the attorney's testimony on his hours was "simply devoid of substance." At trial, the attorney had estimated that he spent, on average, six hours a week for the 226 weeks he worked on the case. The court expressed "puzzlement" as the record provided "no clue" about how this figure was calculated; counsel didn't make any records of his time or prepare any invoices or bills for his clients. The court summarized the trial testimony:

> In short, Gonzalez offered nothing to document his time in the case other than the "thousands and thousands and thousands of pages" generated during his representation of the Montanos and his belief that he had reasonably spent 1,356 hours preparing and trying the case. We rejected similar proof in *El Apple*.
>
> Gonzalez's testimony that he spent "a lot of time getting ready for the lawsuit," conducted "a lot of legal research," visited the premises "many, many, many, many times," and spent "countless" hours on motions and depositions is not evidence of a reasonable attorney's fee under lodestar. . . . In *El Apple*, we said that a lodestar calculation requires certain basic proof, including itemizing specific tasks, the time required for those tasks, and the rate charged by the person performing the work. Here, Gonzalez conceded that had he been billing his client he would have itemized his work and provided this information. A similar effort should be made when an adversary is asked to pay instead of the client.[43]

The court found that the other attorney's testimony involved "contemporaneous events and discrete tasks–the trial and associated preparation for each succeeding day" and was sufficient.[44]

The Texas Supreme Court again addressed the ramifications of *El Apple* in 2014. In *Long v. Griffin*, the plaintiffs sought attorneys' fees under Chapter 38 of the Texas Civil Practice and Remedies Code and under the Texas Declaratory Judgment Act. The plaintiffs ultimately didn't prevail on the breach of agreement claim and Chapter 38 was inapplicable. Under the original reasoning of *El Apple*, the declaratory judgment claim by itself wouldn't have been considered a lodestar claim. But, following *Montano*, the court once again found that the plaintiffs "elects to prove attorney's fees via the lodestar method" by "relating the hours worked for each of the two attorneys multiplied by their hourly rates for a total fee."[45]

The court reviewed the affidavit that supported the award of attorney's fees and found it wanting.

> The affidavit supporting the request for attorney's fees only offers generalities. It indicates that one attorney spent 300 hours on the case, another expended 344.50 hours, and the attorneys' respective hourly rates. The affidavit posits that the case involved extensive discovery, several pretrial hearings, multiple summary judgment motions, and a four and one-half day trial, and that litigating the matter required understanding a related suit that settled after ten years of litigation. But no evidence accompanied the affidavit to inform the trial court the time spent on specific tasks.[46]

The attorney's affidavit only offered generalities about the number of hours expended on the case. It lacked any evidence of the time spent on specific tasks. Because no legally sufficient evidence supported the award of attorney fees, the award was reversed.[47]

The court also addressed the real evidentiary problem lurking in many of these cases: time records don't exist because when the case was tried they weren't yet required. The underlying bench trial in *Long* was held nine years before *El Apple* was decided. Contemporaneous time records won't exist because the attorneys failed to see into the future. Without a time machine, contemporaneous time records will seldom exist for cases tried before *El Apple*. The supreme court, as it did in *El Apple*, recognized this problem and cut the attorneys some slack on remand:

> We note that here, as in *El Apple*, contemporaneous evidence may not exist. But the attorneys may reconstruct their work to provide the trial court with sufficient information to allow the court to perform a meaningful review of the fee application.[48]

One big question has been left unanswered in *Long*: what is the impact of Chapter 38 of the Civil Practice and Remedies Code? Section 38.004 says, "The court may take judicial notice of the usual and customary attorney's fees and of the contents of the case file without receiving further evidence in: (1) a proceeding before the court; or (2) a jury case in which the amount of attorney's fees is submitted to the court by agreement." Section 38.003 says, "It is presumed that the usual and customary attorney's fees for a claim of the type described in Section 38.001 are reasonable. The presumption may be rebutted." Because the plaintiffs lost on their assignment claim, Chapter 38 did not apply. But the supreme court's approach to the lodestar method is inconsistent with the language of Chapter 38. To apply *El Apple*'s approach to proof requirements to Chapter 38 cases would abrogate the statutory language.

C. *El Apple* in the Courts of Appeals

1. Applicability of *El Apple*

The courts of appeals have not been consistent in applying *El Apple*. They are split on whether *El Apple* applies to non-lodestar cases. Several courts of appeals have held that *El Apple* doesn't apply to non-lodestar cases.[49] Other courts have held that *El Apple* does apply to, say, breach of contract cases.[50] Both the Dallas Court of Appeals[51] and the Fourteenth Court of Appeals[52] have issued contradictory panel opinions. One Fourteenth Court of Appeals panel explained that *Long* and *Montano* required a different approach and held that *El Apple* applies when a party chooses to use the lodestar method. Thus, that panel found a plaintiff, "chose to use the lodestar method when seeking attorney's fees for services performed through the end of trial" by "offering evidence of the hours of work multiplied by the hourly rate of the person who performed the work."[53]

Most courts of appeals initially were reluctant to apply *El Apple* to breach of contract claims. The Dallas Court of Appeals typified the approach taken by most of these courts. In *Metroplex Mailing Services, LLC v. RR Donnelley & Sons Co.*, a breach of contract case, the court first noted, "nowhere in *El Apple* did the court conclude that all attorney's fees recoveries in Texas would thereafter be governed by the lodestar approach and we do not draw that conclusion here." It also noted that under the traditional method of awarding fees, documentary evidence is not a prerequisite and "an attorney's testimony about his experience, the total amount of fees, and the reasonableness of the fees charged is sufficient to support an award."[54]

In 2015, the Dallas Court of Appeals reaffirmed its position that *El Apple* does not mean that "all attorney's fees recoveries in Texas are governed by the lodestar method" in *Rohrmoos Venture v. UTSW DVA Healthcare, LLP*.[55] The court noted that many of its sister courts also have held that *El Apple* doesn't apply to non-lodestar cases.[56] Acknowledging the language from *Long v. Griffin* about a party "choosing" the lodestar method, the court noted that the appellant didn't assert, and the record didn't show, that the appellee "chose to prove up attorney's fees using this method."[57]

The Fort Worth Court of Appeals also has refused to extend *El Apple*. It recently noted that "under the traditional method of awarding fees, documentary evidence is not a prerequisite. It has consistently been held that an attorney's testimony about his experience, the total amount of fees, and the reasonableness of the fees charged is sufficient to support an award."[58] The court further noted that it previously had declined to extend *El Apple* to require time records in all cases in which an attorney uses the attorney's hourly rate to calculate the fee. "In ordinary hourly-fee breach of contract cases, '[t]ime sheets or other detailed hour calculations are not required if the testimony regarding the hours of work required is not speculative."[59] Similarly, the San Antonio Court of Appeals held that *El Apple* doesn't apply to "a garden-variety breach of contract claim in which the prevailing party sought to recover damages as well as attorney's fees under section 38.001 of the Texas Civil Practice and Remedies Code."[60]

In 2013, the Fourteenth Court of Appeals initially held that *El Apple* didn't apply to a breach of contract case: "Because the lodestar method is not the method used for calculating the appropriate attorney's fees in a breach-of-contract case, [*El Apple*] is not instructive to our analysis."[61]

Since the supreme court issued *City of Laredo v. Montano* in 2013 and *Long v. Griffin* in 2014, the Fourteenth Court of Appeals has handed down a couple of opinions that extended *El Apple* to breach-of-contract cases.

In *Enzo Investments, LP v. White*, the court determined that the plaintiff "chose to use the lodestar method to establish the amount of reasonable and necessary attorney's fees attributable to the successful prosecution of his breach-of-contract claim"; consequently, the plaintiff "was required to provide evidence of the time expended on specific tasks."[62] The court held that one attorney's affidavit was insufficient because it only gave total hours and listed tasks performed for the client. The court stated that from the information provided in the affidavit, it was impossible to evaluate the extent to which the attorney's work was reasonable and necessary to the prosecution of the plaintiff's breach-of-contract claim.

The court's other opinion extending *El Apple* to Chapter 38 claims is far more interesting. While the court in *Auz v. Cisneros* extended *El Apple*, it also recognized that the supreme court in *Long v. Griffin* had "effectively abrogated a number of Texas precedents regarding the application of Chapter 38."[63] The court provided a good summary of Chapter 38 jurisprudence before it was bulldozed by *Long v. Griffin*:

> Under section 38.004 of the Civil Practice and Remedies Code, in a proceeding before the court, the trial court "may take judicial notice of the usual and customary attorney's fees and of the contents of the case file without receiving further evidence." Tex. Civ. Prac. & Rem. Code Ann. § 38.004. Under section 38.003 of the Civil Practice and Remedies Code, "[i]t is presumed that the usual and customary attorney's fees for a claim of the type described in Section 38.001 are reasonable," and that "[t]he presumption may be rebutted." *Id.* § 38.003. In reaching its holding, the *Long* court did not explain how application of the *El Apple I* requirements to attorney's fees requests under Chapter 38 would be consistent with these statutory provisions. *See Long*, 442 S.W.3d at 254-56. Under prior precedent from the Supreme Court of Texas and this court, appellate courts could affirm Chapter 38 attorney's fees awards by presuming that the trial court took judicial notice under section 38.004, even if the party seeking fees did not request judicial notice and even if the trial court did not state that it was taking judicial notice. *See Gill Sav. Ass'n v. Chair King*, 797 S.W.2d 31, 32 (Tex. 1990); *Ross v. 3D Tower Ltd.*, 824 S.W.2d 270, 273 (Tex. App.–Houston [14th Dist.] 1992, writ denied). *See also* Scott A. Brister, *Proof of Attorney's Fees in Texas*, 24 St. Mary's L. J. 313, 333–34 (1993) (observing that Chapter 38 allows a trial court to award reasonable fees without any offer of evidence regarding attorney's fees in a proceeding before the court).[64]

The court apparently recognized the mess the supreme court has created; however, it pointed out that it's not its responsibility to clean up such a mess: "It is not our role as an intermediate court of appeals to abrogate or modify precedent from the Supreme Court of Texas; instead, we must apply the *Long* precedent to this case."[65]

2. Sufficiency of Evidence

Attorney fee awards continue to be reviewed for sufficiency of proof of attorneys' fees. The supreme court in *El Apple* criticized the attorneys' lack of detail on how much time was spent on "particular tasks or categories of tasks."[66] Global testimony or affidavits about the work performed is highly susceptible to attack on appeal.[67] Attorneys need to allocate specific hours to specific tasks.

Although the supreme court allowed in *El Apple* that documentation such as time records may not be required in "the simplest cases."[68] Allocating the hours between the various tasks performed may be required in all cases. Justice Boyce in a concurring opinion in *Auz v. Cisneros* concluded, "Allocation always is required under these decisions when the lodestar method is invoked, even in 'the simplest cases' involving a modest number of hours." That case involved a "modest expenditure of 30 attorney hours." Justice Boyce believed that there was "some flexibility" in requiring documentation under *El Apple*, but there was no such flexibility for allocating which of these 30 hours were spent on which task. He, therefore, joined the majority's determination that the fee award must be reversed "because the supporting affidavit offers a global recitation of categories of tasks performed and the total number of hours expended." Justice Boyce conceded that the reversal "seems like an unduly formalistic result in a simple case involving a simple commercial dispute requiring a modest expenditure of 30 attorney hours to obtain a favorable judgment. By no measure is the requested fee disproportionate to the result."[69]

The First Court of Appeals reversed a fee award of $250,000 where the attorney's one-page affidavit in support of the award "recites her hourly fee, states that Academy has incurred fees in the amount of $185,930 through the date of the affidavit's execution, and avers that the reasonable value of fees that Academy would continue to incur is $50,000 through entry of judgment; $50,000 through appeal to this court; and $100,000 through appeal to the Texas Supreme Court."[70]

The First Court of Appeals also reversed a $145,000 award of attorneys fees in *Boyaki v. John M. O'Quinn & Associates, PLLC*.[71] The court found the affidavits supporting attorneys' fees were deficient because they offered generalities. The first affidavit stated:

> [S]ince September 15, 2009, I have attended several hearings, prepared a Motion for Temporary Injunction, prepared for the hearing. I have reviewed various drafts of letters and email correspondence to opposing counsel. I have communicated to my client, The O'Quinn Law Firm, the status of implementation of the settlement agreement, reviewed Texas cases on the enforcement of Rule 11 settlement agreements, reviewed Plaintiffs' First Amended Original Petition, reviewed Plaintiffs' Motion for Summary Judgment to Enforce Rule Settlement with supporting affidavits. I have also had a number of additional conferences with representatives of my client and co-counsel. Accordingly, since September 15, 2009, I have spent at least 98 hours in rendering the above-described necessary legal services ... in enforcement of the mediated Rule 11 Settlement Agreement.

The second affidavit said:

> [S]ince July 22, 2011, I have prepared various drafts of letters and email correspondence to and for Charles Musslewhite, my co-counsel, I have communicated to my client, The O'Quinn Law Firm the status of implementation of the settlement agreement, researched and reviewed Texas cases on the enforcement of Rule 11 settlement agreements, drafted and edited Plaintiffs' First Amended Original Petition, drafted and edited Plaintiffs' Motion for Summary Judgment to Enforce Rule 11 Settlement, with supporting affidavits, and prepared a proposed Final Summary Judgment. I have also had a number of additional conferences with representatives of my client and co-counsel. Accordingly, since July 22, 2011, I have spent at least 215 hours in rendering the above-described necessary legal services.

The court concluded that the evidence in support was legally insufficient and reversed and remanded.[72]

In another attorney's fees case from the First Court of Appeals, the court affirmed the award, finding none of the problems with generalities it had found in *Johnson* and *Boyaki*.[73] The Texas Attorney General had sued under section 431.047(d) of the Health & Safety Code, and the State was awarded nearly $130,000 in reasonable and necessary fees and costs. On appeal, the defendants presented the now-standard argument that there was no evidence to support the judgment's award of attorney's fees and expenses because the evidence on attorney's fees was too general to apply the lodestar method in a meaningful manner. The First Court of Appeals found that the State's evidence was detailed enough to pass scrutiny:

> The attorney's fees evidence in this case is much more detailed than that provided in *El Apple*, *Long*, or *Boyaki*. The State presented expert testimony regarding its attorney's fees, including the reasonableness and necessity of the work done on the case, the hours spent, the experience and qualifications of the timekeepers for the State, and the prevailing hourly rates of each. The State also submitted an affidavit, a summary of the hours worked and prevailing rates, and a computer-generated summary of the time records of all of the State's timekeepers who worked on the case. The computer generated time summary, entitled "Summary of Services Provided," identifies the case by name, each timekeeper by name and title, a description of each activity, and the hours devoted to that activity by each timekeeper. The activities are divided into categories such as "attend/appear at hearing," "drafting/revising pleadings," and "reviewing/researching law."[74]

The court also rejected the defendants' argument that the evidence was insufficient because it does not say which hearings were attended, which pleadings were revised, and what law was researched. The court noted that "nothing in *El Apple*, *Long*, or *Boyaki* requires such detail." It is enough to indicate how long each person spent working on particular categories of tasks.

3. Discovery

Can plaintiffs who seek attorneys' fees discover the amounts of the defendants' attorneys' fees? That question was answered "yes" by the Corpus Christi Court of Appeals. In a multi-district litigation pretrial proceeding, the insureds–who would be entitled to statutory attorney fees if they prevail–hired an expert who testified that the fees of the opposing party are a factor and an indicator of a reasonable fee. The insureds subsequently moved to serve additional discovery requests on the insurers regarding the amount of attorney fees the insureds had accrued in the underlying cases. The special master for discovery recommended that the trial court grant leave to serve the additional discovery and the trial court did so. The insurers sought mandamus relief. The court of appeals held that the opposing party's legal fees "may be relevant to prove factors one and three from the *Arthur Andersen* factors–that is, the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly, and the fee customarily charged in the locality for similar legal services." The court also pointed out that Justice Hecht considered evidence of the other party's attorneys' fees as an "indicator" of a reasonable fee in his concurring opinion in *El Apple*.[75]

4. Preservation of Error

Whether a party has to preserve error on an attack on the reasonableness of attorneys' fees will depend upon the procedural posture of the case. Several appeals have involved an award of attorneys' fees that accompanied a motion for summary judgment.[76] Courts of appeals have held that an appellant may complain for the first time on appeal about the legal sufficiency of the evidence for the attorneys fee award.[77]

A jury trial will necessitate preserving error on the sufficiency of evidence for the fee award. The Dallas Court of Appeals detailed the problems with one appellant's argument on appeal:

> In reviewing a jury finding, we review the evidence in light of the charge actually given. Here, the jury was given no definitions with respect to reasonable attorney's fees. In particular, the jury was not instructed it was required to make a lodestar calculation by first specifically determining the reasonable hours spent by counsel and the reasonable hourly rate. Additionally, Davenport Meadows' specific complaints focus largely on the lack of specificity with respect to Hopkins' testimony with respect to segregation. But it fails to discuss the contractual provision that authorized the award of attorney's fees and fails to provide any argument or authority that Hopkins was required to segregate any fees in the first instance. Moreover, the jury charge did not require the jury to segregate fees.[78]

The possibility that the court of appeals may order a take-nothing judgment on attorneys' fees means that there may not be a second bite at *El Apple*.

A party must preserve error in the trial court to complain about a failure to segregate fees.[79]

5. Appellate Remedy

A successful attack on the recovery of attorneys' fees almost always results in a reverse and remand and not reverse and render. In segregation of fees cases, a remand is ordered because there is some evidence of attorneys' fees. The Texas Supreme Court in *Tony Gullo Motors* held that the proper remedy would be a remand because the unsegregated fees for the entire case are some evidence of what the segregated amount should be.[80] This rule has been dutifully followed by the courts of appeals.[81]

The Austin Court of Appeals reluctantly ordered a remand where the trial court had denied attorneys' fees because the party willfully failed to segregate attorneys' fees despite many requests and opportunities to do so, among other reasons. The court of appeals noted that the party failed to segregate even after the trial court repeatedly admonished it that the foregoing circumstances were likely impediments to a full fee award.[82] The court of appeals sustained the attack on attorneys' fees and noted that the case would be remanded:

> However willful and ill-considered the refusal to segregate was, the remedy for such failure is not an award of zero attorney's fees, because evidence of unsegregated attorney's fees for the entire case is some evidence of what the segregated amount should be. . . . Accordingly, the supreme court has held that the appropriate remedy for failure or refusal to segregate attorney's fees is remand for segregation.[83]

However, the Corpus Christi Court of Appeals has upheld a no-evidence challenge and then rendered a take-nothing judgment on attorneys' fees. This was a forcible entry and detainer lawsuit. The landlord's attorney provided the following testimony:

> I am an attorney licensed by the Supreme Court in the State of Texas to practice in all of Texas, Judge. I've been working as an attorney for the past approximately 10 years. Now I did represent Mr. Ramos from the time that he– the appeal [sic] was filed up until today which is the conclusion. My hourly rate was $225 an hour and in my expert opinion all of the work that was done was necessary to bring forth the suit and the number of hours set forth that I put into the case were a reasonable and necessary fee that I'm charging is $15,000.

The court cited *El Apple* (without explaining why) and the *Arthur Andersen* factors. The court then summarized the attorney's testimony as constituting "brief testimony [that] touched on his experience as a lawyer in Texas, a general statement about how long he has worked on this specific case, and his hourly rate." It then noted that the lawyer's testimony did not explain–

> (1) the time and labor required in this case, (2) what specific work and services were accomplished, (3) what skill was required to properly perform legal services in this case, (4) what were the fees customarily charged in Hidalgo County for similar legal services, or (5) other factors that would explain the reasonableness of his fee.

The court held that the trial court abused its discretion in awarding attorneys' fees and rendered a take-nothing on attorneys' fees.[84]

The court's action seems unusual. For one thing, the affidavit does appear to be "some" evidence about attorneys' fees. Moreover, the supreme court has ordered remands in the three cases where it recently has found the evidence on attorneys' fees to be legally insufficient. But the Corpus Christi Court of Appeals remedy was not unprecedented. The opinion does cite a case where a $1000 award of attorneys' fees was vacated on appeal. There the plaintiff apparently didn't even request attorneys' fees, provided no proof at trial, and failed to respond to the defendant's argument on appeal.[85] Another opinion cited in the case resulted in the court of appeals vacating the award of attorneys' fees. Again, it appears in that case that no evidence on attorneys' fees was presented in the literal sense and not merely the legal sense of insufficient evidence.[86] Here, there was inadequate testimony, which the court of appeals found was "no evidence."

Consumer lawyers may recall appellate courts in DTPA cases ordering remands where the proof of attorney's fees has been found to be legally insufficient. In a case where the only evidence in the record supporting the award of attorney's fees was an exhibit totaling the fees charged, the Austin Court of Appeals reversed the award of attorney's fees but *remanded* that issue for a new trial. The court explained:

> Although ordinarily the failure to produce any evidence of an element of proof requires that we reverse and render judgment that a plaintiff take nothing, attorney's fees

for a prevailing consumer under the DTPA have been treated differently. *Leggett v. Brinson*, 817 S.W.2d 154, 157 (Tex. App.–El Paso 1991, no writ). In such a case, the proper remedy is to remand to the trial court for presentation of evidence and a determination of whether the requested fees are reasonable and necessary.[87]

In another DTPA case where no proof of attorneys' fees was adduced (the trial court improperly took judicial notice), the court of appeals explained that a remand was necessary because the DTPA mandated attorney's fees. The court noted, "Normally, when we find that there is no evidence to support a finding, the remedy is to reverse and render on the point. However, the award of attorneys' fees under the DTPA presents a unique situation. This is so because an award of attorneys' fees is mandated."[88]

The possibility that the court of appeals may order a take-nothing judgment on attorneys' fees means that there may not be a second bite at *El Apple*. Attorneys should strive to get it right the first time.

** Godwin PC Research Professor and Professor of Law, South Texas College of Law. Professor Steiner received a BA from The University of Texas in1978, a JD from the University of Houston Law Center in 1982, and a Ph.D. from the University of Houston in1993.*

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1 Arthur Andersen & Co. v. Perry Equip. Corp., 945 S.W.2d 812 (Tex. 1997).
2 Tony Gullo Motors I, L.P. v. Chapa, 212 S.W. 3d 299 (Tex. 2006).
3 Long v. Griffin, 442 S.W. 3d 253 (Tex. 2014)(per curiam); City of Laredo v. Montano, 414 S.W. 3d 731 (Tex. 2013)(per curiam); El Apple I, Ltd. v. Olivas, 370 S.W. 3d 757 (Tex. 2012).
4 David A. Anderson, *Judicial Tort Reform in Texas*, 26 Rev. Litig. 1, 7 (2007); R. Jack Ayres, Jr., *Judicial Nullification of the Right to Trial by Jury by "Evolving" Standards of Appellate Review*, 60 Baylor L. Rev. 337 (2008); Phillip Hardberger, *Juries Under Siege*, 30 St. Mary's L.J. 1, 141-42 (1998).
5 Arthur Andersen v. Perry Equip. Corp, 945 S.W. 2d 812 (Tex. 1997).
6 *Id*. at 817, n. 4.
7 *Id.* at 818.
8 *Id.*
9 *Id.* at 819.
10 *Id.*
11 *See, e.g.,* McDonald v. Fox, No. 13-11-00479-CV (Tex. App.–Corpus Christi, Nov. 15, 2012, no pet.)(mem. op.); Alsheikh v. Arabian Nat'l Shipping Corp., No. 01-08-00007-CV (Tex. App.–Houston [1st Dist.] April 2, 2009, no pet.)(mem. op.); EMC Mortg. Corp. v. Davis, 167 S.W.3d 406 (Tex. App.–Austin 2005, pet. denied).
12 Robertson County v. Wymola, 17 S.W.3d 334 (Tex. App.–Austin 2000, pet. denied).
13 VingCard A.S. v. Merrimac Hosp. Sys., Inc., 59 S.W.3d 847 (Tex. App.–Fort Worth 2001, pet. denied).
14 Tony Gullo Motors I, L.P. v. Chapa, 212 S.W.3d 299 (Tex. 2006).
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16 Tony Gullo Motors I, L.P. v. Chapa, 212 S.W.3d 299 (Tex. 2006).
17 *Id*. at 313.
18 *Id.*
19 *Id.*
20 *Id*. at 313-314.
21 *See, e.g.*, Fix it Today, LLC v. Santander Consumer USA, Inc., No. 02-14-00191-CV (Tex. App.–Fort Worth May 7, 2015, no pet. h.)(mem. op.); Jackson Walker, LLP v. Kinsel, No. 07-13-00130-CV (Tex. App.–Amarillo April 10, 2015, pet. filed)(mem. op.)*;* Prudential Ins. Co. v. Durante*,* 443 S.W. 3d 499 (Tex. App.–El Paso 2014, pet. denied)*;* Farmers Group Ins., Inc. v. Poteet*,* 434 S.W.2d 316 (Tex. App.–Fort Worth 2014, pet. denied); Central Austin Apartments, LLC v. UP Austin Holdings, LP, No. 03-13-00080-CV (Tex. App.–Austin Dec. 8, 2014, no pet.)(mem. op.); Border States Elec. Supply v. Coast to Coast Electric*, LLC*, No. 13-13-00118-CV (Tex. App.–Corpus Christi May 29, 2014, pet. denied)(mem. op.); Contemporary Contractors, Inc. v. Centerpoint Apt. Ltd. P/S, No. 05-13-00614-CV (Tex. App.–Dallas July 3, 2014, no pet.)(mem. op.).
22 Central Austin Apartments, LLC v. UP Austin Holdings, LP, No. 03-13-00080-CV (Tex. App.–Austin Dec. 8, 2014, no pet.)(mem. op.).
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24 *Id.* at 514.
25 *See, e.g.,* Corral-Lerma v. Border Demolition & Environmental Inc., 467 S.W. 3d 109, 126 (Tex. App.-El Paso 2015) (pet. denied). (attorney "opined" that twenty percent of time was spent on non-recoverable claim); Sentinel Integrity Solutions, Inc. v. Mistras Group, Inc., 414 S.W.3d 911, 923 (Tex. App.–Houston [1st Dist.] 2013, pet. denied)(attorney "opined" that "'at least' ninety percent" of work was necessary for defending claim). *But see* Enzo Investments, LP v. White, 468 S.W.3d 635 (Tex. App.–Houston [14th Dist.] 2015, pet. denied).
26 Prudential Ins. Co. v. Durante, 443 S.W. 3d at 514.
27 Jackson Walker, LLP v. Kinsel, No. 07-13-00130-CV (Tex. App.–Amarillo April 10, 2015, pet. filed)(mem. op.).
28 *Id.*
29 *Id.* (citations omitted).
30 *Id.*
31 El Apple I, Ltd. v. Olivas, 370 S.W. 3d 757 (Tex. 2012); City of Laredo v. Montano, 414 S.W. 3d 731 (Tex. 2013)(per curiam); Long v. Griffin, 442 SW 3d 253 (Tex. 2014)(per curiam).
32 El Apple I, Ltd. v. Olivas, 370 S.W. 3d at 760.
33 Texas Civil Practice and Remedies Code § 26.003(a) provides for attorney fees in class action lawsuits:

> If an award of attorney's fees is available under applicable substantive law, the rules adopted under this chapter must provide that the trial court shall use the Lodestar method to calculate the amount of attorney's fees to be awarded class counsel. The rules may give the trial court discretion to increase or decrease the fee award calculated by using the Lodestar method by no more than four times based on specified factors.

34 El Apple I, Ltd. v. Olivas, 370 S.W. 3d at 763.
35 *Id*. at 761.
36 *Id*. at 763 (emphasis added).
37 *Id*.
38 *Id*.
39 City of Laredo v. Montano, 414 S.W. 3d 731 (Tex. 2013)(per curiam); Long v. Griffin, 442 S.W. 3d 253 (Tex. 2014)(per curiam).
40 Perdue v. Kenny A. Ex rel. Winn, 130 S. Ct. 1662 (2010).
41 *Id*. Montano, 414 S.W. 3d at 736.
42 414 S.W. 3d 731.
43 *Id.* at 736-737 (citations omitted).
44 *Id.*
45 Long v. Griffin, 442 SW 3d at 255.
46 *Id.*
47 *Id.*
48 *Id.* at 256.
49 Hussami v. Clear Sky MRI & Diagnostic Center, No. 02-14-0014 June 25, 2015, no pet. h.)(mem. op. settled and judgment withdrawn); In re Marriage of Pyrtle, 433 S.W. 3d 152 (Tex. App.–Dallas 2014, pet. denied); Ferrant v. Graham Assoc., Inc., No. 02-12-00190-CV (Tex. App.–Fort Worth May 8, 2014, no pet.)(mem. op.); Myers v. Southwest Bank, No. 02-14-00122-CV (Tex. App.–Fort Worth Dec. 11, 2014, pet. denied)(mem. op.); Paez v. Trent Smith Custom Homes*,* No. 04-13-00394-CV (Tex. App.–San Antonio March 19, 2014, no pet.)(mem. op.); Metroplex Mailing Servs., LLC v. RR Donnelley & Sons Co., 410 S.W.3d 889, 900 (Tex. App.–Dallas 2013, no pet.).

50 *See, e.g.*, Avery v. LPP Mortg., Ltd., No. 01-14-01007-CV (Tex. App.–Houston [1st Dist.] Oct. 29, 2015, no pet. h.)(mem. op.).
51 *Compare* Blackstone Med., Inc. v. Phoenix Surgicals, LLC, 470 S.W. 3d 636, 659 (Tex. App.—Dallas 2015, no pet.) *with* Metroplex Mailing Services, LLC v. RR Donnelley & Sons Co., 410 S.W.3d 889, 900 (Tex. App.–Dallas 2013, no pet.).
52 *Compare* Concert Health Plan, Inc. v. Houston Nw Partners, Ltd., No. 14-12-00457-CV (Tex. App.–Houston [14th Dist.] May 30, 2013, no pet.)(mem. op.) *with* Enzo Investment, LP v. White, 468 S.W.3d 635 (Tex. App—Houston [14th Dist.} 2015, pet. denied).
53 United Nat'l Ins. Co. v. Amj Investments, LLC, 447 S.W.3d 1, 16 (Tex. App.–Houston [14th Dist.] 2014, pet. dism'd).
54 Metroplex Mailing Services, LLC v. RR Donnelley & Sons Co., 410 S.W.3d 889, 900 (Tex. App.–Dallas 2013, no pet.). *See also* Qui Phuoc Ho v. Macarthur Ranch, LLC, No. 05-14-00741-CV (Tex. App.–Dallas Aug. 28, 2015, pet. filed)(mem. op.); In the Interest of J.R. III, No. 05-14-00338-CV (Tex. App.–Dallas Aug. 5, 2015, no pet.)(mem. op.).
55 Rohrmoos Venture v. UTSW DVA Healthcare, LLP, No. 05-14-00774-CV (Tex. App.–Dallas Oct. 5, 2015, no pet. h.)(mem. op.)(citing Metroplex Mailing Servs. LLC v. Donnelly & Sons Co., 410 S.W.3d 889, 900 (Tex. App.–Dallas 2013, no pet.); Powell v. Penhollow, Inc., No. 05-13-01653-CV (Tex. App.–Dallas June 1, 2015, no pet. h.)).
56 *Id.*(citing Ferrant v. Graham Assocs., Inc., No. 02-12-00190-CV (Tex. App.–Fort Worth May 8, 2014, no pet.) (mem. op.); Concert Health Plan, Inc. v. Houston Nw Partners, Ltd., No. 14-12-00457-CV (Tex. App.–Houston [14th Dist.] May 30, 2013, no pet.) (mem. op.); Circle Ridge Prod. Inc. v. Kittrell Family Minerals, LLC, No. 06-13-00009-CV (Tex. App.–Texarkana July 17, 2013, pet. denied) (mem. op.)). One of the cases cited in support, *Concert Health Plan, Inc. v. Houston NW Partners, Ltd.*, hasn't been followed by subsequent panels of the Fourteenth Court of Appeals. *See* Auz v. Cisneros, No. 14-13-00989-CV (Tex. App.– Houston [14th Dist.] Aug. 27, 2015, no pet. h.); United Nat'l Ins. Co. v. Amj Investments, LLC, 447 S.W.3d 1, 16 (Tex. App.–Houston [14th Dist.] 2014, pet. dism'd).
57 *Id.*
58 Myers v. Southwest Bank, No. 02-14-00122-CV (Tex. App.–Fort Worth Dec. 11, 2014, pet. denied)(mem. op.).
59 *Id.* (quoting Ferrant v. Graham Assocs., Inc., No. 02-12-00190-CV (Tex. App.–Fort Worth May 8, 2014, no pet.)(mem. op.)(on reh'g)).
60 Paez v. Trent Smith Custom Homes, No. 04-13-00394-CV (Tex. App.–San Antonio, March 19, 2014)(mem. op.).
61 Concert Health Plan, Inc. v. Houston Nw Partners, Ltd., No. 14-12-00457-CV (Tex. App.– Houston [14th Dist.] May 30, 2013, no pet.) (mem. op.).
62 Enzo Investments, LP v. White, 468 S.W.3d 635 (Tex. App.–Houston [14th Dist.] 2015, pet. denied).
63 Auz v. Cisneros, No. 14-13-00989-CV (Tex. App.– Houston [14th Dist.] Aug. 27, 2015, no pet. h.).
64 *Id.*
65 *Id.*
66 El Apple I, Ltd. v. Olivas, 370 S.W. 3d at 763.
67 *See, e.g.,* Avery v. LPP Mortg., Ltd., No. 01-14-01007-CV (Tex. App.–Houston [1st Dist.] Oct. 29, 2015, no pet. h.)(mem. op.).
68 El Apple I, Ltd. v. Olivas, 370 S.W. 3d at 763.
69 Auz v. Cisneros, No. 14-13-00989-CV (Tex. App.– Houston [14th Dist.] Aug. 27, 2015, no pet.)(concurring op.)
70 Johnson v. Texas Serenity Academy, Inc., No. 01-14-00438-CV (Tex. App.–Houston [1st Dist.] March 12, 2015, pet. filed)(mem. op.).
71 Boyaki v. John M. O'Quinn & Assocs., PLLC, No. 01-12-00984-CV (Tex. App.–Houston [1st Dist.], Sept. 30, 2014, pet. denied)(mem. op.).
72 *Id.*
73 Medical Discount Pharmacy, L.P. v. State, No. 01-13-00963-CV (Tex. App.–Houston [1st Dist.] July 7, 2015, no pet. h.)(mem. op.).
74 *Id.*
75 In re National Lloyds Ins. Co., No. 13-15-00219-CV (Tex. App.–Corpus Christi July 14, 2015, orig. proceeding)(mem. op.).
76 On appealing summary judgments that involve attorneys fees, see Judge David Hittner & Lynne Liberato, *Summary Judgments in Texas: State and Federal Practice*, 52 Hous. L. Rev. 773, 897-892 (2015).
77 Auz v. Cisneros, No. 14-13-00989-CV (Tex. App.– Houston [14th Dist.] Aug. 27, 2015, no pet.); Enzo Investments, LP v. White, 468 S.W.3d 635 (Tex. App.–Houston [14th Dist.] 2015, pet. denied); Schwartzott v. Maravilla Owners Ass'n, Inc., 390 S.W.3d 15, 21, n. 3 (Tex. App.– Houston [14th Dist.] 2012, pet. denied). *See also* City of Houston v. Clear Creek Basin Authority, 589 S.W.2d 671(Tex. 1979) (non-movant may argue on appeal that the grounds in motion for summary judgment are insufficient as a matter of law to support summary judgment without filing an answer or response to the motion).
78 Davenport Meadows, LP v. Dobrushkin, No. 05-12-01471-CV (Tex. App.–Dallas July 30, 2014, pet. denied)(mem. op.).
79 Green Int'l, Inc. v. Solis, 951 S.W.2d 384, 389 (Tex.1997); Dernick Resources, Inc. v. Wilstein, 471 S.W. 3d 468 ((Tex. App.–Houston [1st Dist.] June 30, 2015, pet. pending).
80 Tony Gullo Motors I, L.P. v. Chapa, 212 S.W. 3d at 314.
81 Farmers Group Ins., Inc. v. Poteet, 434 S.W.3d 316, 333 (Tex. App.–Fort Worth 2014, pet. denied).
82 Central Austin Apts. v. UP Austin Holdings, LP, No. 03-13-00080-CV (Tex. App.–Austin, Dec. 8, 2014 no pet.)(mem. op.)(judgmt vacated by agr.).
83 *Id.*
84 Serrano v. Ramos, No. 13-13-00476-CV (Tex. App.–Corpus Christi June 18, 2015, no pet. h.)(mem. op.).
85 Bruce v. Federal Nat'l Mortg. Ass'n, 352 S.W.3d 891 (Tex. App.–Dallas 2011, pet. denied).
86 Charette v. Fitzgerald, 213 S.W.3d 505 (Tex. App.–Houston [14th Dist.] Dec. 21, 2006, no pet.).
87 Murray v. Grayum, No. 03-10-00165-CV (Tex. App.–Austin June 24, 2011, pet. denied)(mem. op.).
88 Scott v. Spalding, No. 11-07-00264-CV (Tex. App.–Eastland Jan. 30, 2009, no pet.)(mem. op.).

Using the Class Action Fairness Act as a Loophole Around the Magnuson Moss's Jurisdictional Requirements

By Sarah Denis*

Recent federal district court decisions are erroneously allowing the Class Action Fairness Act [CAFA] to supersede the Magnuson Moss Warranty Act's [MMWA] Class Action's requirements. This could potentially be a red flag for those who think CAFA can be used to evade the MMWA's jurisdictional requirements. Courts are disregarding the jurisdictional limitations of the MMWA, allowing CAFA to trump its requirements. These courts are stating that, where CAFA's conditions are met, CAFA provides an alternative basis for jurisdiction without regard for the MMWA. Consider this hypothetical that explains this scenario: Plaintiffs file a complaint under the MMWA, and Defendants move to dismiss Plaintiffs' claims under the MMWA for lack of subject-matter jurisdiction. Defendants argue that the MMWA provides:

> [n]o claim shall be cognizable in a 'suit' brought by a consumer for a violation of the **Act** if 'the amount in controversy of any individual claim is less than the sum or value of $25,' the total 'amount in controversy is less than the sum or value of $50,000' or 'the action is brought as a class action, and the number of named plaintiffs is less than one hundred.'[1]

The Complaint neither names one hundred plaintiffs nor states that any individual plaintiff is seeking more than $25. Defendants argue that Plaintiffs' MMWA claims must be dismissed because the Complaint neither names one hundred plaintiffs nor states that any individual plaintiff is seeking more than $25. However, Plaintiffs' counsel will argue cleverly, with a smirk on his face, and say, "Honorable Judge, my client is not invoking the MMWA as a basis for the Court's jurisdiction, but instead my client relies on the CAFA." The judge, then, will consider this argument and ask himself whether this newly enacted CAFA presents an alternative basis for jurisdiction over Plaintiffs' MMWA claims. The truth of the matter is that the judge will most likely answer this question in the affirmative. Why? Is it because recent decisions that have engaged in the same inquiry are saying yes? Likely, the judge will say to himself, "I would hate to be an odd ball if all these judges are allowing jurisdiction pursuant to CAFA, so I shall do the same." More likely than not, the judge will agree with the weight of authority, and find Plaintiffs' MMWA claims may go forward.

This is not what Congress intended. If Congress wanted to create a more relaxed class action requirement for MMWA claims, then perhaps it would have done so prior to the enactment of the CAFA, or at the very least Congress could have added a provision in the CAFA allowing it to trump the MMWA. Allowing district courts to exercise jurisdiction based on CAFA is a mistake, and will lead to the flooding of the district courts. This comment explains why this is a misconception and courts should adhere to what Congress expressly set out in the MMWA, and not allow CAFA to trump the MMWA.

Part I of this comment provides background on the MMWA's Class Action requirements, and the CAFA. **Part II** analyzes the discrepancy between the two conflicting class action requirements, and argues courts should give deference to the interpretation set forth in the MMWA. **Part III** applies both the *Barr v. General Motors* and *Kuns v. Ford Motor* framework to the MMWA's class action requirements, and demonstrates that the *Barr* interpretation deserves deference. The comment concludes by arguing, when read properly in light of *Barr*, the MMWA's Class Action requirements are stringent, and courts should not allow CAFA to create a loophole based on what Congress set out in 1975.

I. BACKGROUND

A. Magnuson-Moss Warranty Act

Congress enacted the MMWA[2] with the purpose of protecting consumers from deceptive warranty practices,[3] specifically, narrow consumer product warranties that were often too convoluted for a layperson to understand.[4] In doing so, Congress wanted to safeguard consumers by imposing some requirements on warrantors and requiring warrantors to make detailed disclosures of information necessary to allow consumers to understand written warranties.[5] The MMWA provides consumers with a guideline that allows consumers to compare warranty coverage before a purchase and to know what to expect if a product goes wrong.[6] The MMWA allows a consumer to assert a civil cause of action to enforce the terms of an implied or express warranty or a violation of the Act.[7] Notably, however, this consumer friendly statute requires consumers to follow a stringent jurisdictional requirement to file a claim in federal court.[8]

Sections 2310(d)(1) and (3) of the MMWA provides[9]

> [s]ubject to subsections (a)(3) and (e), a consumer who is damaged by the failure of a supplier, warrantor, or service contractor to comply with any obligation under this title [15 USCS §§ 2301 et seq.], or under a written warranty, implied warranty, or service contract, may bring suit for damages and other legal and equitable relief-- (A) in any court of competent jurisdiction in any State or the District of Columbia; or (B) in an appropriate district court of the United States, subject to paragraph (3) of this subsection. . . .
>
> . . . . [] No claim shall be cognizable in a suit brought under paragraph (1)(B) of this subsection--(A) if the amount in controversy of any individual claim is less than the sum or value of $ 25; (B) if the amount in controversy is less than the sum or value of $ 50,000 (exclusive of interests and costs) computed on the basis of all claims to be determined in this suit; or (C) if the action is brought as a class action, and the number of named plaintiffs is less than one hundred.[10]

As stated above, "no claim shall be cognizable" in federal district courts unless the number of members in the plaintiff's class is greater than one hundred.[11] Congress set forth this provision in order "to prevent such actions from occupying a federal forum at all unless these prerequisites are met," and to "avoid trivial or insignificant actions being brought as class actions in the federal courts."[12] However, soon after the passage of the CAFA, district courts allowed CAFA to serve as a loophole around the MMWA, and are failing to prevent these trivial and insignificant actions from occupying a federal forum.[13]

B. Class Action Fairness Act

Congress intended to address a different need when it passed the CAFA[14] than when it passed the MMWA.[15] CAFA was enacted with the purpose of enhancing and expanding class actions in federal jurisdiction.[16] In doing so, Congress broadened federal jurisdiction by establishing lenient requirements in order to protect defendants from "inequitable state treatment" and "to put an end to certain abusive state practices by plaintiffs' counsel."[17] Subject to its relaxed requirements, CAFA provides federal courts with jurisdiction over class actions provided that: The amount of controversy must be more than $5 million and satisfy any of the following:

> (1) "Any member of the plaintiff class is from a state other than the state of any defendant;"
> (2) "Any member of [the plaintiff class] is a foreign state or … subject of a foreign state and any defendant is a citizen of a State;" or
> (3) "Any member of [the plaintiff class] is a citizen of a State and any defendant is a foreign state or … subject of a foreign state."[18]

CAFA's grant of jurisdiction over qualifying class actions is quite broad.[19] It provides district courts with original jurisdiction over "*any* civil action" that satisfies both the amount in controversy requirement and "is a class action," as long as certain specified other criteria are met.[20] Although it may be argued that because CAFA contains several enumerated exceptions:[21] the "Securities Act"[22] exception and the "Securities Exchange Act of 1934,"[23] CAFA is harmonious with the MMWA. Courts have argued that because Congress failed to include the MMWA as an enumerated exception, "they may not assume that those omissions were accidental, and must "assume that Congress is aware of existing law when it passes legislation."[24] However, it is a fallacy to say that because Congress failed to list MMWA under the enumerated exceptions, courts should assume that the CAFA trumps the MMWA? Therefore, Part II and III analyze this misconception, and demonstrate that courts should not allow CAFA to supersede the MMWA's Class Action requirements.

II. WHICH REQUIREMENT TO APPLY?

A. *Barr v. General Motors*[25]

In *Barr,* the Plaintiff purchased an automobile from General Motors and discovered discoloration of the car's paint.

The Plaintiff claimed the automobile had been painted with defective paint and brought suit as the representative of a class action involving herself and all the persons in the country that had purchased the car from the defendants with defective paint. In the Complaint, the Plaintiff stated MMWA was the basis of federal jurisdiction. Defendants, however, moved to dismiss because the complaint was conclusory as to the size of the class.

The Plaintiff argued that discovery would "certainly" demonstrate the 100 named plaintiffs existed. The Court rejected Plaintiff's argument and ruled the buyer could not claim that discovery would certainly demonstrate the class existed.[26] The Court held that the buyer's allegations as to the size of the class were insufficient to satisfy the numerosity requirement under the MMWA statutory requirement, which requires that a class action brought under MMWA must have at least 100 named plaintiffs;[27] and that the jurisdictional prerequisite to a class action under the MMWA had to be met at the time the Court certified class action.[28] The Court held that concluding otherwise would frustrate the purpose of jurisdictional provisions, which is, "to avoid trivial or insignificant actions being brought as class actions in the federal courts."[29]

B. *Kuns v. Ford Motor Co.*[30]

As noted above to bring a class action pursuant to the MMWA, a complaint must list at least one hundred named plaintiffs.[31] In *Kuns*, a purchaser of a sport utility vehicle brought a class action against the dealership alleging that it violated, among other things, the MMWA. Kuns filed her complaint against the dealership as the only named plaintiff, and the Court correctly determined that it did not have jurisdiction under the MMWA. However, Kuns' counsel found a loophole around the MMWA class action requirement, and filed an amended complaint asserting federal jurisdiction pursuant to CAFA. The Court held that even though courts have not addressed this "jurisdictional interplay," it nevertheless had jurisdiction pursuant to the CAFA. [32]

To bring a class action pursuant to the MMWA, a complaint must list at least one hundred named plaintiffs.

The Court reasoned that the CAFA—the more recent of the two statutes—"can render a district court a 'court of competent jurisdiction' and permit it to retain jurisdiction where the CAFA requisites are met but the MMWA requisites are not."[33] The Court based its reasoning on *Keegan v. Am. Honda Motor Co.,* which held that as a "general rule" the CAFA effectively supersedes the MMWA's more stringent jurisdictional requirements.[34]

In *Keegan,* Plaintiffs brought an action on behalf of all individuals who purchased or leased a defective model year 2006 and 2007 Honda Civic and 2006 through 2008 Honda Civic Hybrid vehicles. Plaintiffs alleged the vehicles were defective, and that the rear control arm originally installed in the vehicles were too short. However, Defendants moved to dismiss the complaint because the complaint failed to meet the requirements of §2310(d)(3)(C), and consequently lacked jurisdiction to hear the MMWA claim.

Defendants argued that the MMWA only permits the exercise of federal jurisdiction over class actions where the number of named plaintiffs equals or exceeds one hundred.[35] Plaintiffs argued that the Court had jurisdiction pursuant to an alternative basis for jurisdiction under CAFA. Plaintiffs argued that, even if the number of proposed plaintiffs is less than 100, the Court allegedly has jurisdiction under CAFA.[36] The Court nevertheless followed the weight of authority,[37] and held that the absence of at least one hundred named plaintiffs it does not prevent the Plaintiff from asserting claims under the MMWA. The jurisdiction requirement was satisfied because Plaintiffs properly invoked jurisdiction under CAFA.[38]

C. The Text and Legislative History

1. The Text

In *Barr,* as noted above, the Plaintiff filed her complaint against General Motors because the automobile had defective paint. Subsequently, the Court dismissed the Complaint because the Plaintiffs did not meet the class action requirements of §2310(d)(3)(C). The Court recognized that "the language of § 2310(d)(3)(C) means what it says; there must be at least one hundred individuals *named* in the complaint, or at the very least identified in the motion to certify the class."[39]

In recent court opinions, district courts are reconciling CAFA with the MMWA.[40] These courts are arguing that "as a firmly embedded principle of statutory construction requires courts to presume that Congress enacts legislation with knowledge of existing law and, consequently, the newly-enacted statute is "harmonious with the existing law."[41] But perhaps this is a mistake, as statutes conferring jurisdiction on federal courts are to be strictly construed, and doubts are resolved against federal jurisdiction.[42] Therefore, courts should not forget "as a basic principle of statutory construction that a statute dealing with a narrow, precise, and specific subject is not to be submerged by a later enacted statute covering a more generalized spectrum."[43]

2. *Statutory Interpretation and Canons of Interpretation*

In *Radzanower v. Touche Ross & Co.*, the United States Supreme Court held that as a basic principle of statutory construction a statute dealing with a narrow, precise, and specific subject should not submerged by a later enacted statute covering a more generalized spectrum.[44] In *Radzanower*, the Complaint was dismissed on the ground that venue was improper under the National Bank Act, which provided that an action could not be brought in the district where the bank was "established."[45] On certiorari, the Supreme Court rejected the representative's contention that the venue provision of the later-enacted Securities Exchange Act of 1934, partially repealed the National Bank Act's venue provision.[46]

The Court held that the Securities Exchange Act of 1934, the later enacted statute, covers a more generalized spectrum than the National Bank Act which has a narrow, precise, and specific subject, should not submerged by the later statute. Similarly, the MMWA is a statute dealing with a narrow, precise, and specific subject that requires at least one hundred individuals named in a complaint.[47] The CAFA's grant of jurisdiction over qualifying class actions is quite broad and more generalized, which provides district courts with original jurisdiction over "*any* civil action" that both satisfies the amount in controversy requirement and "is a class action," as long as certain specified other criteria are met.[48] Therefore, as a basic principle of statutory construction, the MMWA should not be submerged by CAFA, the more generalized statute.

3. *Legislative History and Federal Judiciary*

The MMWA's legislative history demonstrates that it is inconsistent to construe the MMWA as not requiring 100 members in a Class Action.[49] House Report 93-1107 is part of the legislative history of the Magnuson-Moss Warranty Act, and a glance at the portion dealing with section 2310(d) reveals the following:[50]

[1055] The purpose of these jurisdictional provisions is to avoid trivial or insignificant actions being brought as class actions in the federal courts. However, if the conditions of [Section 2310(d)(3)] are met by a class of consumers damaged by a failure to comply with a warranty as defined in this statute, Section [2310](d) should be construed reasonably to authorize the maintenance of a class action. In this context, we would emphasize that this section is remedial in nature and is designed to facilitate relief that would otherwise not be available as a practical matter for individual consumers.

However, scholars who support CAFA argue that CAFA's legislative history prevails, as it is the last one to be enacted.[51] District courts argue that Congress is presumed to enact legislation with knowledge of the law,[52] but these courts fail to acknowledge a couple of important points in the legislative history that support the proposition that Congress intended a strict interpretation of the MMWA's class action requirement.[53] Thus, the reading of the House Report turns the statute's language on its head, as the drafters recognized that federal courts should not be burdened by "trivial or insignificant actions."[54]

III. DOES CAFA PRESENT AN ALTERNATIVE BASIS FOR JURISDICTION OVER MMWA CLAIMS?

The truth of the matter is that courts disagree about the answer to this question. As discussed above, some courts have held that where its conditions are met, CAFA provides an alternative basis for jurisdiction without regard for the MMWA.[55] However, courts should not disregard the text of the MMWA, and instead should consider the argument that MMWA claims that do not satisfy that statute's requirements may be brought pursuant to CAFA to be "flatly contradicted by the plain text of the MMWA." [56]

For example, in *Ebin v. Kangadis Food Inc.*, the Court dismissed the Plaintiffs' MMWA claims for lack of subject-matter jurisdiction.[57] The Court rejected Plaintiffs' contention at oral argument that "CAFA creates an alternative basis for federal jurisdiction over the MMWA claim." In order to bolster their argument, Plaintiffs' filed a supplemental letter-brief which cited to recent MMWA cases, suggesting their MMWA claims were viable under the CAFA. However, the Court held that Plaintiffs' position was incorrect, as "it was flatly contradicted by the plain text of the MMWA."[58] The Court reasoned that, the MMWA clearly provides no claim shall be cognizable in a suit brought under paragraph (1) (B) of the MMWA, unless the MMWA's independent jurisdictional requirements were met.

A. Countervailing issues with the Application of *Kuns* to the MMWA

Applying the *Kuns*[59] test to the MMWA presents several problems. First, it is important to acknowledge why Congress drafted its own set of class action jurisdictional requirements for the MMWA, for the purpose of not flooding district courts with claims that belong in state courts.[60] In 1996, Congress "recognized the importance of balancing the need to assist the Federal judiciary in reducing its increasing caseload with the needs of those making use of our Federal courts."[61] If courts allow CAFA to serve as an admission ticket into district courts and supersede MMWA, this will do exactly the opposite of what Congress has strived to prevent.[62]

Statistics indicate that since 2006, soon after the enactment of CAFA, approximately fifteen courts allowed CAFA to supersede the class action requirements of the MMWA.[63] In 2007, at least four district courts allowed CAFA to trump the class action requirements of the MMWA.[64] More recently, in 2013 no less than five courts allowed CAFA to supersede the class action requirements of the MMWA.[65] If this trend continues, our district courts will be burdened by the "trivial or insignificant actions" Congress believed belonged in state courts.[66] This is why in the MMWA Congress expressly distinguished between federal and state courts, "attempting to strike a balance between the needs of federal courts and the needs of legitimate potential plaintiffs."[67] Consequently, if plaintiffs cannot meet the class action requirements under the MMWA, they have no "hook to maintain jurisdiction in district courts, and courts should acknowledge that the "congressionally approved balance of federal and state judicial responsibilities" tips in favor of remanding."[68]

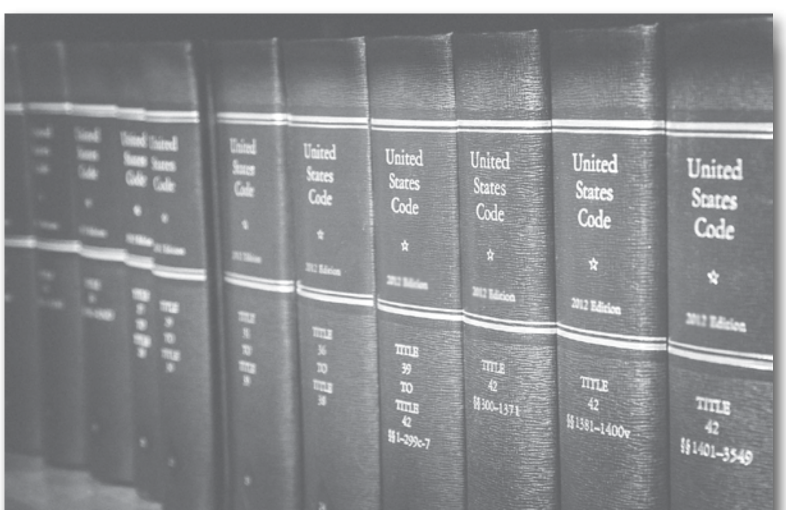
B. The *Kuns* Precedents Do Not Support CAFA to Supersede the MMWA's Class Action Requirements.

None of the precedents under *Kuns* support the argument CAFA supersedes the MMWA's Class Action requirements. Since the enactment of the MMWA, it has been well established that plaintiffs must meet all three requirements set out in 15 U.S.C. § 2310(d)(3). For example, in *Lieb v. American Motors Corp.*, the Court dismissed the Plaintiff's class claims under the Magnuson-Moss Act because only one plaintiff was named in the complaint.[69] The Court found that "the Complaint is deficient measured against the explicit and unambiguous statutory mandate and must be dismissed as a class action."[70] Similarly, in *Watts v. Volkswagen*, the Court dismissed class claims under the Magnuson-Moss Act because there were only two named plaintiffs in the complaint.[71] Finally, as discussed above, in *Barr,* the Court found that "the language of § 2310 (d) (3) (C) means what it says; there must be at least one hundred individuals named in the complaint."[72] Case law is well settled that plaintiffs must meet the stringent Class Action requirements set forth in the MMWA.

C. Has Congress Directly Spoken to the Issue? [73]

Congress has not spoken on this specific issue, but the language of § 2310(d)(3) is essentially a limitation,[74] and Congress makes it unmistakably clear that, as the House Report reflects, the purpose is to avoid such "trivial or insignificant actions" being brought in the federal courts."[75]

Even if Congress has not addressed this jurisdictional interplay, case law has construed that MMWA overrides statutes that supersedes it. For example, in *Watts v Volkswagen*,[7676] the Court held that it did not have subject matter jurisdiction under MMWA because there were only two named Plaintiffs.[77] The



Court relied on the MMWA legislative history, which "does not shed light on when the requirement of 100 named plaintiffs must be met."[78] The Court also noted that, "[i]n the absence of any express language to indicate a Congressional intent to change the general rule concerning when the jurisdictional facts must exist, we decline to find that it has been changed."[79] As the court in *Watts notes*, in the absence of any express language to indicate a Congressional intent to change the general rule concerning the jurisdictional requirements of the MMWA, courts must decline to find that the MMWA has been changed.

CONCLUSION

The crossroads of the MMWA and the CAFA is a field where two conflicting class action requirements meet: the *CAFA's requirements* regarding judicial deference to the broadening of federal jurisdiction and the *MMWA's stringent requirement* to prevent actions from occupying a federal forum unless these prerequisites are met favoring a strict interpretation of the MMWA. Applying the *Barr* framework, CAFA in this context should not supersede the MMWA class action requirements. Even after applying the *Kuns* framework, any further discussion of the statute in the *Barr* framework clearly establishes that Congress did not intend for CAFA to supersede the MMWA's Class Action requirements and that the MMWA interpretation deserves deference. The MMWA's Class Action requirements are stringent, and courts should not allow CAFA to create a loophole on what Congress expressly set out in 1975.

** University of Miami School of Law, 2016; candidate for J.D., class of 2017. The author would like to thank Tom, her mentor, for all his advice, encouragement, and support. The author also would like to thank Professor Jennifer S. Martin, St. Thomas University School of Law, for her support and topic suggestion. In addition, she would like to thank Alexa Bontkowski, for her skillful editing and insightful comments on an early draft of this comment. This article appeared on the* National Law Review *database as the winner of the Fall 2015* National Law Review *Student Writing Competition, http://www.natlawreview.com/article/using-class-action-fairness-act-cafa-loophole-around-magnuson-moss-s-jurisdictional.*

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1 15 U.S.C. § 2310 (2015).

2 15 U.S.C.A. §§ 2301 *et seq. (2015).*

3 *See* Skelton v. Gen. Motors Corp., 660 F.2d 311, 313 (7th Cir. 1981) (noting the MMWA is "a remedial statute designed to protect consumers from deceptive warranty practices.").

4 *See* S.Rep.No.93-151, 93d Cong., 1st Sess. 6-8 (1973); H.R.Rep. No.93-1107, 93d Cong., 2d Sess. 22-29, reprinted in (1974) U.S.C.C.A.N. 7702, 7705-11(determining that "the paper with the filigree border bearing the bold caption "Warranty' or "Guarantee' was often of no greater worth than the paper it was printed on.").

5 *See* 16 C.F.R. § 701.3(a) (2015); *see also Skelton*, 660 F.2d at 311, 313 (concluding that "[p]ursuant to this provision, the FTC has, by regulation, required that warrantors made detailed disclosures of information necessary to allow consumers to understand and enforce written warranties.").

6 16 C.F.R. § 701.3(a) (2015).

7 *See* 15 U.S.C. § 2310(d) (2015) (explaining that any "consumer who is damaged by the failure of a supplier, warrantor, or service contractor to comply with any obligation under this chapter, or under a written warranty, implied warranty, or service contract" may file suit for damages and other legal and equitable relief.").

8 *See* Barr v. Gen. Motors Corp., 80 F.R.D. 136, 139 (S.D. Ohio 1978) (stating that "for the purpose of the Act is to prevent such actions from occupying a federal forum at all unless these prerequisites are met.").

9 *See* 15 U.S.C. § 2310 (2015).

10 *Id.*

11 *See Barr*, 80 F.R.D. at 138.

12 *Id.*

13 *Id.*

14 28 U.S.C. §§ 1332(d), 1453, and 1711–1715 (2015).

15 *See* S. REP. NO. 109-14, at 4-5 (2005), as *reprinted in 2005* U.S.C.A.A.N.

16 *See* Miss. ex rel. Hood v. AU Optronics Corp., 134 U.S. 736 (2014); *see also* Sarah S. Vance, *A Primer on the Class Action Fairness Act of 2005*, 80 Tul. L. Rev. 1617, 1643 (2006) (stating "CAFA represents the largest expansion of federal jurisdiction in recent memory."); Lowery v. Ala. Power Co., 483 F.3d 1184, 1193 (11th Cir. 2007) (determining that CAFA's enactment is "a sea change in diversity jurisdiction.").

17 *See Lowery*, 483 F.3d at 1193 (highlighting "Congress enacted CAFA to address inequitable state court treatment of class actions and to put an end to certain abusive practices by plaintiffs' class counsel.").

18 *See* Class Action Fairness Act of 2005, Pub. L. No. 119, Stat. 4 (2005).

19 *Id.*

20 28 U.S.C. § 1332(d)(2) (2015).

21 See 28 U.S.C. § 1332(d)(9)(A), (c).

22 *See* Securities Act of 1933, Pub. L. No. 22, 48 Stat. 74, 73 (1933).

23 *See* Securities Exchange Act of 1934, Pub. L. No. 291, 48 Stat. 881, 73 (1934).

24 *See* Hall v. United States, 132 U.S. 1882, 1889 (2012); Doe v. Bin Laden, 663 F.3d 64, 70 (2d Cir. 2011).

25 *See* Barr v. Gen. Motors Corp., 80 F.R.D. 136 (S.D. Ohio 1978).

26 *Id.* (concluding "[i]t is also insufficient, for purposes of 15 U.S.C. § 2310(d)(3) to state that discovery will "certainly" demonstrate that the class exists.").

27 *Id.* at 140.

28 *Id.* at 139.

29 *Id.* at 138.

30 543 F. App'x 572 (6th Cir. 2013)

31 *See* 15 U.S.C. § 2310(d)(3) (2015).

32 *Kuns,* 543 F. App'x at 574 (stating "our circuit has not yet addressed the jurisdictional interplay of the CAFA and the MMWA. Nor, apparently, have most of our sister circuits.").

33 *Id.*

34 *See* Keegan v. Am. Honda Motor Corp.*,* 838 F. Supp. 2d 929, 954-55 (C.D. Cal. 2012).

35 *See* 15 U.S.C. § 2310(d)(3)(C).

36 *See* Ibarra v. Manheim Investments, Inc., 775 F.3d 1193, 1195 (9th Cir. 2015) (noting that federal courts have original jurisdiction under CAFA, so long as the amount in controversy is more than more than $5,000,000, exclusive of interest and costs, and there is a diversity of citizenship between any member of the class and any defendant).

37 *See* Wolph v. Acer America Corp., No. C 09-01314, 2009 U.S. Dist. LEXIS 83681, at *2 (N.D. Cal. Sept. 14, 2009); Brothers v. Hewlett-Packard Co., No. C-06-02254, 2007 U.S. Dist. LEXIS 13155, at *8 (N.D. Cal. Feb. 12, 2007); *see also* Stella v. LVMH Perfumes and Cosmetics, 564 F.Supp.2d 833, 837-38 (N.D. Ill. 2008).

38 *See Keegan*, 838 F. Supp. 2d 929, 955 (C.D. Cal. 2012) (concluding that it had subject matter jurisdiction to hear plaintiffs' Magnuson-Moss claims "despite the fact that there are not one hundred named plaintiffs.").

39 Barr v. Gen. Motors Corp., 80 F.R.D. 136, 138 (S.D. Ohio 1978).

40 Chavis v. Fidelity Warranty Services, Inc., 415 F. Supp. 2d 620, 626 (D.S.C. 2006).

41 McCalley v Samsung Electronics America, Inc., 2008 WL 878402, at *5 (D.N.J. Mar. 31, 2008) (interpreting this statute as logical in "light of the fact that CAFA's legislative history clearly indicates the congressional intent to expand federal jurisdiction over class actions.").

42 Ward v. Tupelo Auto Sales, No. 1:98CV261-B-D, 1998 U.S. Dist. LEXIS 19074 (N.D. Miss. Nov. 20, 1998).

43 *Danilov v. Aguirre*, 370 F. Supp. 2d 441, 445 (E.D. Va. 2005); *see also* Radzanower v. Touche Ross & Co., 426 U.S. 148, 153 (1976).

44 Radzanower v. Touche Ross & Co., 426 U.S. 148, 153 (1976).

45 12 U.S.C. § 94 (2015).

46 15 U.S.C. § 78aa (2015).

47 *See* U.S.C. § 2310(d) (2015).

48 28 U.S.C. § 1332(d)(2) (2015).

49 *See* Boelens v. Redman Homes, Inc., 748 F.2d 1058, 1067 (5th Cir. 1984) (stating "statutes conferring jurisdiction on federal courts are to be strictly construed, and doubts resolved against federal jurisdiction.").

50 *See* House Report 93-1107; *see also* Sarah T. Lepak, *Federal Jurisdiction Under the Magnuson-Moss Warranty Act* , 52 Kan. L. Rev. 1041, 1054-1055 (2004).

51 *See McCalley*, note 39 at *5 (D.N.J. Mar. 31, 2008).

52 *See, e,g.,* Witt v. United Cos. Lending Corp., 113 F.3d 508, 513 (4th Cir. 1997).

53 H.R.Rep.No.93-1107, 93d Cong., 2d Sess. (1974), *reprinted in* [1974] U.S.Code Cong. & Admin.News, p. 7725. (stating that "[t]he reference to the "representative capacity of the named plaintiffs" indicates that the named plaintiffs, whom the statute provides shall number at least one hundred, will represent the remainder of the class. The named plaintiffs must therefore be identified for the Court to be able to determine such representative capacity.").

54 *Id.*

55 *See Chavis,* note 38 at 626.

56 *See* Ebin v. Kangadis Food Inc., No. 2311, 2013 U.S. Dist. LEXIS 107224, at *4 (S.D.N.Y. July 25, 2013) (dismissing MMWA claims for lack of subject-matter jurisdiction and holding that the argument that MMWA claims that do not satisfy that statute's requirements may be brought pursuant to CAFA to be "flatly contradicted by the plain text of the MMWA.").

57 *Id.*

58 *Id.*

59 Kuns v. Ford Motor, 543 F. App'x 572 (6th Cir. 2013).

60 *See* House Report 93-1107.

61 *See* S. REP. NO. 104-366 (1996), as *reprinted in* 1996 U.S.C.C.A.N. 4202, 4209.

62 *Id.*

63 *See, e.g.,* Chavis v. Fidelity Warranty Services, Inc., 415 F. Supp. 2d 620, 626 (D.S.C. 2006); Stella v. LVMH Perfumes and Cosmetics, 564 F.Supp.2d 833, 837-38 (N.D. Ill. 2008); McCalley v Samsung Electronics America, Inc., 2008 WL 878402, at *5 (D.N.J. Mar. 31, 2008); Birdsong v. Apple, Inc., 590 F.3d 955 (9th Cir. 2009).

64 *See* Payne v. Fujifilm U.S.A., Inc., No. CIV.A. 07-385 (JAG), 2007 U.S. Dist. LEXIS 94765, 2007 WL 4591281, at *7 (D.N.J. Dec. 28, 2007); McGee v. Continental Tire North Am., Inc., No. CIV.06-6234 (GEB), 2007 U.S. Dist. LEXIS 62869, 2007 WL 2462624, at *2-3 (D.N.J. Aug. 27, 2007); Clark v. Wynn's Extended Care*,* No. 06 C 2933, 2007 U.S. Dist. LEXIS 27386, 2007 WL 922244, at *4-5 (N.D. Ill. Mar. 23, 2007); McWhorter v. Elsea, Inc., 2007 U.S. Dist. LEXIS 26914, 2007 WL 1101249 (S.D. Ohio April 11, 2007); Brothers*,* 2007 U.S. Dist. LEXIS 13155, 2007 WL 485979 (N.D. Cal. Feb. 12, 2007).

65 *See* Kuns, 543 F. App'x 572 (6th Cir. 2013); In re Scotts EZ Seed Litig., No. 12 CV 4727 (VB), 2013 U.S. Dist. LEXIS 73808 (S.D.N.Y. 2013); Route v. Mead Johnson Nutrition Co., No. 12-7350-GW, 2013 U.S. Dist. LEXIS 35069 (C.D. Cal. Feb. 21, 2013); Dye v. Bodacious Food Co., No. 14-80627, 2014 U.S. Dist. LEXIS 180826 (S.D. Fla. Sept. 9, 2014); Weisblum v. Prophase Labs, Inc., 88 F. Supp. 3d 283 (S.D.N.Y. 2015).

66 *See* House Report 93-1107.

67 *See* Sarah T. Lepak, *Federal Jurisdiction Under the Magnuson-Moss Warranty Act*, 52 Kan. L. Rev. 1041, 1054-1055 (2004).

68 *See* Grable & Sons Metal Prods. v. Darue Eng'g & Mfg., 545 U.S. 308, 314 (2005).

69 538 F. Supp. 127, 132 (S.D.N.Y. 1982).

70 *Id.*

71 Watts v. Volkswagen Artiengesellschaft, 488 F. Supp. 1233, 1235-36 (W.D. Ark. 1980).

72 Barr v. Gen. Motors Corp., 80 F.R.D. 136, 139 (S.D. Ohio 1978).

73 *See* 15 U.S.C. § 2310(d)(3) (2015).

74 *See* H.R.Rep.No.93-1107, 93d Cong., 2d Sess. (1974), as *reprinted in* 1974 U.S.C.C.N. 7724; *see also* Barr v. Gen. Motors Corp., 80 F.R.D. 136, 138 (S.D. Ohio 1978).

75 *See* Donahue v. Bill Page Toyota, Inc., 164 F. Supp. 2d 778, 782 (E.D. Va. 2001); *see also* H.R. Rep. No. 93-1107 (1974), *reprinted in* 1974 U.S.C.C.A.N. 7702, 7724.

76 Watts v. Volkswagen Artiengesellschaft, 488 F. Supp. 2d 1233 (W.D. Ark. 1980).

77 *Id.*at 1236, stating that 28 USCS § 1337 does not provide jurisdictional basis independent of requirements found in MMWA or proceeding arising under any Act of Congress regulating commerce, special provisions of Magnuson-Moss Federal Warranty Act (15 U.S.C. § 2310) override general rule.

78 *See* 1974 U.S.C.C.A.N. 7702, 7723-7724 and 7759.

79 *Watts*, 488 F. Supp. at 1236 (W.D. Ark. 1980).

CC Approves New TCPA Rules

TELEPHONE CONSUMER PROTECTION ACT*

By Michael C. Lueder**

Recently, the FCC ruled on 21 long-standing petitions and letters seeking clarifications of the ***Telephone Consumer Protection Act***. FCC Chairman Tom Wheeler's proposed rules were approved with a 3-2 vote. The new rules which were released in June are mostly bad for businesses that use automatic telephone dialing technology.

The majority of the Commission did not distinguish scammers from legitimate businesses. Commissioner Jessica Rosenworcel cited scammer calls from "Rachel" of the mysterious "Card Member Services" as support for her decision to approve the new rules. Chairman Wheeler cited the 214,000 consumer complaints about robocalls, but gave no breakdown as to how many of these complaints involved con artists and how many related to businesses calling, for example, to collect debt.

The new rules provide:

- Telephone service providers can offer robocall blocking technologies to consumers. Providers previously asserted the FCC prohibited such technology.
- Consumers now have the right to revoke their consent to receive calls and text messages sent from autodialers in any reasonable way at any time. Many courts had concluded that consumers have a right to revoke consent. Some said that revocation must be in writing. Some said consent, once given, cannot be taken back. Now all courts likely will hold that consent may be revoked in any reasonable way at any time. One Commissioner said the rules provide that simply telling a payment clerk at a retail store is

The new rules which were released in June are mostly bad for businesses that use automatic telephone dialing technology.

a reasonable way to revoke consent. It is true, consent will be nearly impossible to track.

- To prevent "inheriting" consent for unwanted calls from a previous subscriber, callers will be required to stop calling reassigned wireless and wired telephone numbers after a single call. This is so regardless of whether the caller learns that the number has been reassigned. Apparently dead air will equal knowledge of a change.
- The TCPA prohibits the use of automatic telephone dialing systems to call wireless phones and to leave pre-recorded telemarketing messages on landlines without consent. "Automatic telephone dialing system" is defined as "equipment which has the capacity to (A) to store or produce telephone numbers to be called, using a random or sequential number generator; and (B) to dial such numbers." The new rule clarifies this definition includes machines with a future capacity to dial randomly, sequentially and even from a list loaded into the dialer. Human intervention — like touch screen dialing button — is not sufficient to overcome ATDS status. Although an FCC staffer stated "capacity" is not unbounded, under the new rule, an i-Phone might be considered an ATDS. Commissioner Michael O'Reilly, who voted against the proposal, said if Jim meets Jane at a bar and later asks her friend for her telephone number, he violates the TCPA if he calls her the next day for a date. Why? Jim does not have Jane's consent to call and his phone is an ATDS.
- Consent survives when a consumer ports his number from a land to a wireless phone.

The rule provides for some limited and specific exceptions for "urgent circumstances," which include free calls or text messages to wireless devices that alert consumers of potential fraud or that remind them of urgent medication refills. Consumers will still have an opportunity to opt-out of these types of calls and texts.

The new proposal reaffirms many of the existing FCC and court interpretations of the TCPA:

- Text messages are calls.
- Consent must come from the called party, not the intended recipient of the call.
- The FTC will continue to administer the National Do-Not-Call Registry to prevent unwanted telemarketing calls.
- Wireless and home phone subscribers can continue to prevent telemarketing robocalls made without prior written consent.
- Autodialed and prerecorded telemarketing and information calls and text messages to mobile phones will still require prior consent.
- Political calls will still be subject to restrictions on prerecorded, artificial voice, and autodialed calls to wireless phones, but will continue to not be subject to the National Do-Not-Call Registry because they do not contain telephone solicitations.
- Consumers will still have a private right of action for violations of the TCPA along with statutory penalties.

These new rules will significantly restrict business's use of autodialing technologies. The devil will be in the details.

A couple things are certain about these new rules. They will not stop scammers who use spoofed Caller IDs and originate calls from outside of the United States and, therefore, outside of the jurisdiction of the FCC and/or FTC. They will just make it harder and more expensive for legitimate businesses to reach their customers. By the way, not all businesses are going to disapprove of the ruling; the TCPA class action bar will love it.

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*** Michael Lueder is a partner and litigation attorney with Foley & Lardner LLP. His practice is concentrated in several areas, including Telephone Consumer Protection Act ("TCPA"), banking, class action, employment, and consumer litigation. Mr. Lueder is co-chair of the firm's Consumer Financial Services Practice. He is also a member of our Finance & Financial Institutions and Labor & Employment Practices and our Hospitality Industry Team. Prior to joining the firm, Mr. Lueder served as chief litigation counsel for one of the largest banks in the country.*

Consumer News Alert Recent Decisions

Since 2006, the Center for Consumer Law has published the "Consumer News Alert." This short newsletter contains everything from consumer tips and scam alerts, to shopping hints and financial calculators. It also has a section just for attorneys, highlighting recent decisions. The alert is delivered by email three times a week. Below is a listing of some of the cases discussed during the past few months. To subscribe and begin receiving your free copy of the Consumer News Alert in your mailbox, visit www.peopleslawyer.net.

FEDERAL CIRCUIT COURTS

Court finds warranty plan ambiguous. The Second Circuit reversed a district court's finding in favor of the defendant because a warranty plan was unambiguous and did not apply to the first year following purchase. The Second Circuit found the contract ambiguous in several respects relevant to Plaintiff's claim. The court vacated the judgment and remanded the case to the district court with instructions to deny defendant's motion to dismiss. *Orlander v. Staples, Inc.*, 802 F.3d 289 (2d Cir. Sept. 16, 2015) http://law.justia.com/cases/federal/appellate-courts/ca2/14-2677/14-2677-2015-09-16.html

New York ban on credit card surcharges is upheld. Plaintiffs filed an action against New York in the Southern District of New York on June 4, 2013. They alleged, respectively, that New York's ban on credit card surcharges by a merchant violates the First Amendment's free-speech guarantee, is void for vagueness under the Due Process Clause of the Fourteenth Amendment, and is preempted by the Sherman Antitrust Act. The district court held (1) the law violates the First Amendment and is unconstitutionally vague in violation of the Due Process Clause of the Fourteenth Amendment, (2) permanently enjoin[ed] the defendants from enforcing it against the plaintiffs, and (3) dismissed Plaintiffs' preemption claim as moot, without prejudice. In a lengthy opinion tracing the history of the state and federal law, as well as the plaintiff's First Amendment and Due Process arguments, the Second Circuit vacated the judgment and remanded the matter to the district court. *Expressions Hair Design v. Schneiderman*, 803 F.3d 94 (2d Cir. Sept. 29, 2015). http://law.justia.com/cases/federal/appellate-courts/ca2/13-4533/13-4533-2015-09-29.html

Identity theft suit not preempted by the federal Fair Credit Reporting Act. The Second Circuit held that a suit under state law based on identity theft was not preempted. The court held that 15 U.S.C. 1681t(b)(1)(F) preempts only those claims that concern a defendant's responsibilities as a furnisher of information under the FCRA. These identity theft claims were not preempted because they did not concern Chase's responsibilities as a furnisher. The court further concluded that, to the extent that plaintiff's complaint seeks relief based on Chase's erroneous or otherwise improper furnishing of information to consumer reporting agencies, those claims were preempted. *Galper v. JP Morgan Chase Bank, N.A.*, 802 F.3d 437 (2d Cir. Sept. 30, 2015). http://law.justia.com/cases/federal/appellate-courts/ca2/14-867/14-867-2015-09-30.html

Antitrust attack on credit card arbitration clauses fails. The Second Circuit held that the record supported the district court's conclusion that the "final decision to adopt class-action-barring clauses was something the Issuing Banks hashed out individually and internally." *Ross v. Citigroup, Inc.*, 2015 WL 7292176 (2d Cir. Nov. 19, 2015). https://www.courtlistener.com/opinion/3155989/ross-v-citigroup-inc/

User of phone line can sue under TCPA. Leyse filed suit under the Telephone Consumer Protection Act, after receiving a prerecorded telemarketing call on the landline he shares with his roommate. Leyse was not the intended recipient of the call—his roommate was. The district court dismissed for lack of statutory standing. The Third Circuit reversed, concluding that Leyse has statutory standing. His status as a regular user of the phone line and occupant of the residence that was called brings him within the language of the Act and the zone of interests it protects. Leyse v. Bank of America, N.A., 538 Fed. Appx. 156 (3d Cir. Oct. 4, 2013). http://law.justia.com/cases/federal/appellate-courts/ca3/14-4073/14-4073-2015-10-14.html

Phone call was not communication in connection with a debt. Brown owed student loan debt. A collection employee from Van Ru left a voicemail at Brown's business that stated the caller's and Van Ru's names, a return number, and a reference number. The caller asked that someone from the business's payroll department return her call. Brown sued Van Ru for violations of the Fair Debt Collection Practices Act, 15 U.S.C. 1692c(b), alleging that the voicemail was a communication "in connection with the collection of any debt" with a third party . The district court granted Van Ru judgment on the pleadings. The Sixth Circuit affirmed. The voicemail left at Brown's business was not a "communication" as defined in the Act. A communication must "convey . . . information regarding a debt directly or indirectly to any person through any medium," and the voicemail message did not convey such information. *Brown v. Van Ru Credit Corp.*, 804 F. 3d 740 (6th Cir. Oct. 22, 2015). http://law.justia.com/cases/federal/appellate-courts/ca6/15-1323/15-1323-2015-10-22.html

Letter sent after consumer disputed debt violates Fair Debt Collection Practices Act. The Seventh Circuit held that a letter sent by a debt collector asking for additional information, and providing a way to return with payment violated the FDCPA. The court noted that once a consumer disputes a debt, the collector must cease collection until it verifies the debt. *Leeb v. Nationwide Credit Corp.*, 2015 WL 7351753 (7th Cir. Nov. 20, 2015). http://law.justia.com/cases/federal/appellate-courts/ca7/14-1329/14-1329-2015-11-20.html

Offer for the full amount requested in a Telephone Consumer Protection Act suit does not moot the case. The Seventh Circuit reversed itself, and held that an offer for the full amount requested does not moot the case. The court stated: "If an offer to satisfy all of the plaintiff's demands really moots a case, then it self-destructs," the court wrote. "Rule 68 is captioned 'Offer of Judgment.' But a district court cannot enter judgment in a moot case. All it can do is dismiss for lack of a case or controversy. So if the $3,002 offer made this case moot, then even if Chapman had accepted it the district court could not have ordered First Index to pay. It could have done nothing but dismiss the suit." *Chapman v. First Index, Inc.*, 796 F.3d 783 (7th Cir. Aug. 6, 2015). http://law.justia.com/cases/federal/appellate-courts/ca7/14-2773/14-2773-2015-08-06.html

Swearing to truth of affidavit without personal knowledge does not violate Fair Debt Collection Practices Act. The Eighth Circuit noted that Section 1692 of the FDCPA prohibits a debt collector from making a "false, deceptive or misleading representation or means in connection with the collection of any debt," or using "unfair or unconscionable means to collect or attempt to collect any debt." The consumer alleged that by swearing to the truth of the affidavit without having personal knowledge of the facts contained within it, the attorney violated both of these provisions. The court noted that even if we were to assume that Basler's attestations were literally false, Janson has not plausibly alleged that he or anyone else was misled by that falsehood. Absent an allegation that he actually did not owe rent, Janson has not plausibly alleged that the defendant's practice misled the state court in any meaningful way. *Janson v. Katharyn B. Davis, LLC*, 806 F.3d 435 (8th Cir. Nov. 17, 2015). http://law.justia.com/cases/federal/appellate-courts/ca8/15-1381/15-1381-2015-11-17.html

Attorney's fees may be awarded in a suit for damages to provide redress for a violation of the automatic bankruptcy stay. When a debtor files for bankruptcy, the Bankruptcy Code imposes an automatic stay on actions against the debtor to collect pre-petition debts. The Ninth Circuit reversed an earlier position it took in *Sternberg v. Johnston*, 595 F.3d 937 (9th Cir. 2010), and held that the court may award attorney's fees in an action for damages for violation of automatic stay. The court noted, "Having reconsidered the matter, we conclude that *Sternberg* misconstrued the plain meaning of § 362(k). To the extent it is inconsistent with this opinion, Sternberg is overruled." The court concluded, "For these reasons, § 362(k) is best read as authorizing an award of attorney's fees incurred in prosecuting an action for damages under the statute." *In re Schwartz-Tallard*, 803 F.3d 1095 (9th Cir. Oct. 14, 2015). http://law.justia.com/cases/federal/appellate-courts/ca9/12-60052/12-60052-2015-10-14.html

Court finds Credit Reporting Agency used reasonable procedures in reporting information. The Tenth Circuit affirmed the dismissal of a consumer's claim that a CRA failed to properly report and investigate a disputed lien. The court noted that although the question of whether a CRA followed reasonable procedures is ordinarily for the jury, in cases where CRAs clearly employ reasonable procedures, the issue may be decided on summary judgment. In the instant case, the court concluded that the reporting and the re-investigation both followed reasonable procedures as a matter of law. *Wright v. Experian Information Solutions*, 805 F.3d 1232 (10th Cir. Nov. 10, 2015). http://law.justia.com/cases/federal/appellate-courts/ca10/14-1371/14-1371-2015-11-10.html

FEDERAL DISTRICT COURTS

Unpaid property taxes are not a debt under the Fair Debt Collections Practices Act ("FDCPA"). The Middle District of North Carolina dismissed a plaintiff's complaint noting that a threshold requirement for application of the FDCPA is an attempt to collect a "debt," but that property taxes and associated costs do not arise out of the type of consumer transaction contemplated by the FDCPA's definition of "debt." *Armstrong v. Bardill,* No. 1:13-CV-1140, WL 5159090 (M.D.N.C. Sept. 2, 2015). http://law.justia.com/cases/federal/district-courts/north-carolina/ncmdce/1:2013cv01140/64768/15/

STATE COURTS

Arbitration in contract written in English not enforceable when contract negotiated in Spanish and translated into Spanish. A California appellate court held that an arbitration clause contained in a signed contract written in English was unenforceable when the consumer negotiated the agreement in Spanish and also signed a Spanish translation that did not contain the arbitration provision. The court noted that the consumer "is not attempting to avoid the arbitration agreement because of his limited understanding of the English language. Rather, he is relying on the fact that Pena's Motors provided him with what purported to be a Spanish translation of the English contract he was being asked to sign, a Spanish translation which did not contain the arbitration agreement." *Ramos v. Westlake Services LLC*, 2015 WL 7482148 (Cal. Ct. App. Oct. 30, 2015). http://law.justia.com/cases/california/court-of-appeal/2015/a141353.html

Agreement finance companies made with tort plaintiffs seeking funds to pay personal expenses while waiting for their lawsuits to settle or go to trial were loans. The specific issue this case presented for the Colorado Supreme Court's review centered on whether the companies forwarding of expense money to tort plaintiffs constituted a "loan." Petitioners contended they were "asset purchases," but the Colorado Uniform Consumer Credit Code interprets these transactions as loans. The Supreme Court agreed with the UCCC: these transactions are loans. Oasis Legal Fin. Grp., LLC v. Coffman, 2015 WL 7177951 (Colo. Nov. 16, 2015). http://law.justia.com/cases/colorado/supreme-court/2015/13sc497.html

The Kentucky Supreme Court applied the generally accepted rule that compliance with government regulations imposes a substantially higher standard to justify the award of punitive damages.

Kentucky Supreme Court reverses award of punitive damages in Nissan case. The Kentucky Supreme Court applied the generally accepted rule that compliance with government regulations imposes a substantially higher standard to justify the award of punitive damages. The court stated, "Successful completion of regulatory product testing weighs against a finding of gross negligence." The court noted, however, "mere compliance with regulatory products standards, either mandatory or voluntary, does not automatically foreclose a punitive damages jury instruction. In other words, proof indicating that a manufacturer exercised slight care by complying with relevant regulatory mandates is not dispositive where additional evidence is presented that tends to prove reckless or wanton conduct." In the instant case, the court found insufficient evidence of reckless or wanton care was presented. *Nissan Motor Co., Ltd. v. Maddox*, 2015 WL 5626432 (Ky. Sept. 24, 2015). http://law.justia.com/cases/kentucky/supreme-court/2015/2013-sc-000685-dg.html

Arbitration agreement signed by nursing home resident's attorney in fact not enforceable. The Kentucky Supreme Court held that the power-of-attorney instruments did not authorize the resident's attorney-in-fact to waive the resident's right to access to the courts. The court held that (1) without a clear and convincing manifestation of the principal's intention to do so, delegation to an agent of the authority to waive a trial by jury is not authorized, and the principal's assent to the waiver is not validly obtained; and (2) the arbitration agreements in these cases were never validly formed. *Extendicare Homes, Inc. v. Whisman*, 2015 WL 5634309 (Ky. Oct. 29, 2015). http://law.justia.com/cases/kentucky/supreme-court/2015/2013-sc-000426-i-0.html

Applying Minnesota payday lending law to a Delaware company that made loans over the Internet is not unconstitutional. The lender argued that the application of Minnesota law to its loans violated the extraterritoriality principle of Article I, Section 8, Clause 3 of the United States Constitution, which prohibits a state from regulating commerce that occurs "wholly outside the . . . [s]tate." The Minnesota Supreme Court noted that the commerce regulated by Minnesota's payday-lending law in this case, which involved a Delaware company lending money to residents of Minnesota and making deposits and withdrawals through Minnesota banks, was not wholly extraterritorial.

> "In this case, the "economic activity" regulated by Minnesota's payday-lending law involved more than just Integrity's signature; the law governed the entire transaction between Integrity and borrowers. The law regulated the payment of funds to and from Minnesota borrowers, which for most of these loan transactions included electronic transfers into and out of Minnesota banks, activities that certainly qualify as commerce."

Swanson v. Integrity Advance, LLC, 870 N.W.2d 90 (Minn. Oct. 7, 2015). http://law.justia.com/cases/minnesota/supreme-court/2015/a13-1388.html

Claim against hospital based on a slip and fall claim is not a health care liability claim (HCLC) under the Texas Medical Liability Act. The Texas Supreme Court reversed the court of appeal's decision that the TMLA applied to plaintiff's premises liability claim. The Supreme Court stated: "We conclude that the record before us does not reflect a substantive nexus between the safety standards Reddic claims the hospital violated and the hospital's provision of health care." The court concluded, "Thus, the record does not support the hospital's contention that Reddic's claim is an HCLC. *Reddic v. E. Texas Med. Ctr. Reg'l Health Care Sys.*, 2015 WL 6558270 (Tex. Oct. 30, 2015). http://law.justia.com/cases/texas/supreme-court/2015/14-0333.html

Deposit returned to buyer after contract cancelled should not be setoff against damages. The Vermont Supreme Court held that a buyer's recovery under the state's consumer protection act should not be offset by any deposit returned by the seller. The seller cancelled the contract and returned the deposit as required. The deposit amount was not part of the buyer's damages. *McKinstry v. Fecteau Residential Homes, Inc.*, 2015 VT 125 (Vt. Sept. 18, 2015). http://law.justia.com/cases/vermont/supreme-court/2015/2015-vt-125.html

RECENT DEVELOPMENTS

DECEPTIVE TRADE PRACTICES AND WARRANTIES

COURT FOUND WARRANTY PLAN AMBIGUOUS

Orelander v. Staples, Inc., 802 F.3d 289 (2d Cir. 2015). http://law.justia.com/cases/federal/appellate-courts/ca2/14-2677/14-2677-2015-09-16.html

FACTS: Plaintiff, Andrew Orelander ("Plaintiff"), purchased a Hewlett Packard computer a long with a two-year "Carry-in" Protection Plan from a Staples ("Defendant") store. The Protection Plan Brochure ("Contract") referenced restrictions regarding certain provisions that could only be found in the full Terms and Conditions. After eight months of use, Plaintiff brought the computer back to Staples to exchange the computer due to Internet connectivity issues.

Defendant's employee told Plaintiff to contact Hewlett Packard directly because the Protection Plan provided no coverage until the manufacturer's warranty expired. Plaintiff also tried, unsuccessfully, to procure the full Terms and Conditions referenced in the Contract. Subsequently, Plaintiff received a letter from a Staples Sales Manager reiterating that the Staples Protection Plan covers the second year when the manufacturer's warranty expires.

Plaintiff filed suit for breach of contract, breach of express and implied warranties, and unjust enrichment. The district court granted Defendant's motion to dismiss for failure to state a claim. Plaintiff appealed the dismissal of the breach of contract claim.

HOLDING: Vacated and Remanded.

REASONING: The Second Circuit began its analysis by noting that whether a contract is ambiguous is a question of law. A contract term is unambiguous if it has a precise meaning with "no reasonable basis for a difference of opinion." The court found the contract ambiguous in several respects. The court noted that the small print paragraph that discussed the restrictions applied only to one provision, and that the "one-time replacement" provision was ambiguous because none of the other provisions referred to the restrictions. The court further reasoned that the paragraph that discussed the restrictions was open to multiple reasonable interpretations. Therefore, the contract was ambiguous and the court vacated the district court's judgment and remanded it to the district court with instructions to deny Defendant's motion to dismiss for failure to state a claim.

CONSUMER CREDIT

APPLYING MINNESOTA PAYDAY LENDING LAW TO A DELAWARE COMPANY THAT MADE LOANS OVER THE INTERNET IS NOT UNCONSTITUTIONAL

State v. Integrity Advance, LLC, ___ N.W.2d ___ (Minn. 2015). http://law.justia.com/cases/minnesota/supreme-court/2015/a13-1388.html

FACTS: The State of Minnesota ("Minnesota") brought a civil action against an out-of-state payday lender, Integrity Advance, LLC ("Integrity"), alleging it violated a variety of the state's payday-lending statutes regulating loans made to Minnesota residents.

The loans were negotiated and signed over the Internet while the residents remained in Minnesota even though Integrity resided in Delaware. Integrity counterclaimed and requested a declaratory judgment that Minnesota's payday-lending laws were unconstitutional under the extraterritorial doctrine of the Commerce Clause, which prohibits a state from regulating commerce that occurs "wholly outside the. . .[s]tate." The district court rejected Integrity's constitutional challenges and granted summary judgment to the State. Integrity appealed.

HOLDING: Affirmed.

REASONING: Integrity argued that the law violated the extraterritorial doctrine of the Commerce Clause because the location of the commerce regulated was entirely out-of-state, as it had signed the loan contracts in Delaware. The Minnesota Supreme Court rejected that argument under several grounds. First, the economic activity regulated by the law involved the entire transaction and not just Integrity's signature. The supreme court held that the location of where the contract was signed was "only one factor among many in determining the 'location' of commerce."

Additionally, Minnesota's payday-lending laws are expressly restricted in scope to transactions involving Minnesota residents who were physically present in Minnesota when the transaction was completed. The supreme court found this limitation distinguishable from other challenged laws that regulated out-of-state business merely for advertising to residences within the state.

Finally, the supreme court found even though the law required lenders to provide more favorable interest rates for Minnesota residents, case precedent does not prohibit a state from seeking lower prices for its consumers. Because Minnesota's payday-lending laws did not tie any of these rates to the rates charged in other states, they could not be considered wholly extraterritorial.

USER OF PHONE LINE CAN SUE UNDER THE TCPA

Leyse v. Bank of Am. Nat'l. Ass'n, ___ F.3d ___ (3d Cir. 2015). http://www2.ca3.uscourts.gov/opinarch/144073p.pdf

FACTS: A telemarketer advertising credit cards for the Appellee, Bank of America National Association ("Bank of America"), called the phone of Appellant, Mark Leyse ("Leyse"), which was shared with his roommate, Genevieve Dutriaux. Dutriaux was the telephone subscriber and intended recipient of the call. The message allegedly violated the advertising restrictions of the TCPA. The TCPA prohibits any person from calling a residential telephone line using an artificial or prerecorded voice to deliver a message without the prior express consent of the called party, unless the call is initiated for emergency purposes or is exempted by rule or order by the Federal Communications Commission.

Bank of America filed a motion to dismiss, arguing that Leyse was not the "called party" under the TCPA and did not have statutory standing to bring suit. The district court granted Bank of America's motion to dismiss, and agreed that Leyse did not have statutory standing because he did not qualify as the "called party." He was not the intended recipient of the call. Leyse appealed.

HOLDING: Vacated and remanded.

REASONING: The Third Circuit held that the district court erred in granting Bank of America's motion to dismiss. The court stated that the TCPA forbids using a prerecorded voice when calling any telephone line without the consent of the called party. The TCPA established that "any person" has a private right of action for violations of the TCPA. A party must be within the zone of interest protected by the law. A mere houseguest, visitor, or others who picks up the phone are not included in the TCPA's zone of interests.

The court also reasoned that Congress passed the TCPA after outrage over the proliferation of prerecorded telemarketing calls to private residences, which consumers regarded as a nuisance and an intrusive invasion of privacy. The court determined that the TCPA's zone of interests encompassed more than just the intended recipients of prerecorded telemarketing calls because the actual recipient suffers the nuisance and invasion of privacy. "From this evidence, it is clear that the Act's zone of interests encompasses more than just the intended recipients of prerecorded telemarketing calls. It is the actual recipient, intended or not, who suffers the nuisance and invasion of privacy." Therefore, the court concluded that Leyse was within the class authorized to sue.

NEW YORK BAN ON CREDIT CARD SURCHARGES IS UPHELD

Expressions Hair Design v. Schneiderman, 803 F.3d 94 (2d Cir. 2015).
http://business.cch.com/BANKD/ExpressionsHairDesign_09292015.pdf

FACTS: Plaintiffs, Expressions Hair Design ("Plaintiffs") sued Defendants, Schneiderman, ("Defendants"), challenging the constitutionality of New York General Business Law §518 ("Section 518"). Section 518, enacted by the New York legislature as a response to the expiration of a federal surcharge ban, provides that "no seller in any sales transaction may impose a surcharge on a holder who elects to use a credit card in lieu of payment by cash, check, or similar means."

Plaintiffs brought suit claiming that Section 518: 1) violated the First Amendment's free-speech guarantee; 2) was void for vagueness under the Due Process Clause of the Fourteenth Amendment; and 3) was preempted by the Sherman Antitrust Act. The district court ruled that Section 518 violated the First Amendment and was unconstitutionally vague, but dismissed the Plaintiffs' preemption claim. Defendants appealed.

HOLDING: Vacated and remanded.

REASONING: The Second Circuit rejected the argument that Section 518 violated the First Amendment as applied to the single-sticker pricing scheme, because the prohibition of certain prices did not implicate the First Amendment. The prohibition of certain relationships between prices did not raise any First Amendment constitutional issues. The court made clear that even though prices are communicated through language, they are not "speech" within the meaning of the First Amendment.

The court made clear that even though prices are communicated through language, they are not "speech" within the meaning of the First Amendment.

The court abstained from ruling on the Plaintiffs' overbreadth challenge of Section 518 as applied to the dual pricing scheme. It refused to hold that Section 518 was unconstitutional based entirely on speculation that the New York courts might give it an expansive reading.

Plaintiffs also argued that Section 518 was unconstitutionally vague under the Due Process Clause. The court rejected this argument and concluded that sellers of ordinary intelligence would be able to understand how to avoid imposing a credit card surcharge and that New York authorities would have sufficient guidance in determining whether such sellers violated the law.

COURT FINDS CREDIT REPORTING AGENCY USED REASONABLE PROCEDURES IN REPORTING INFORMATION

Wright v. Experian Information Solutions, ___ F.3d ___ (10th Cir. 2015).
https://www.ca10.uscourts.gov/opinions/14/14-1371.pdf

FACTS: Plaintiff ("Wright") commenced action against credit reporting agencies under the Fair Credit Reporting Act ("FCRA") and the Colorado Consumer Credit Reporting Act ("CCCRA"). A federal tax lien was placed on Wright due to unpaid employment taxes. Defendant, Experian Information Solutions ("Experian") received Wright's lien information and included it in Wright's credit reports. Wright claimed the credit reports were inaccurate, and Experian acted unreasonably in reporting the federal tax lien and responding to his letters.

The district court granted summary judgment to Experian, holding that Experian used reasonable procedures in reinvestigating tax lien information after Wright disputed his credit report. Wright appealed.

HOLDING: Affirmed.

REASONING: Wright alleged Experian violated the FCRA and CCCRA by failing to follow reasonable procedures to assure maximum possible accuracy in preparing the credit report and for failing to reasonably reinvestigate his dispute. The Tenth Circuit Court held that "reasonableness of the procedures" is generally defined as requiring Consumer Reporting Agencies ("CRAs") to look beyond information furnished to them when it is inconsistent with the CRAs' own records, contains a facial inaccuracy, or comes from an unreliable source.

The court held Experian acted reasonably in compiling Wright's consumer report because the information Experian collected from public records was not inaccurate on its face, inconsistent with information Experian already had on file, or obtained from a source that was known to be unreliable. The court also held Experian conducted a reasonable reinvestigation by conducting more than a cursory investigation into the reliability of information reported to potential creditors.

PROVIDING CREDITOR WITH A CELLPHONE NUMBER IS "PRIOR EXPRESS CONSENT" UNDER THE TELEPHONE CONSUMER PROTECTION ACT ("TCPA")

Hill v. Homeward Residential, Inc., 799 F.3d 544 (6th Cir. 2015). http://www.consumerclassdefense.com/files/2015/09/Hill-v-Homeward.pdf

FACTS: Plaintiff-Appellant ("Hill") obtained a mortgage loan from Jordan West Companies in 2003, which was transferred to Defendant-Appellee ("Homeward"). Hill provided his home and work numbers on the original loan. Hill contacted Homeward to advise the company his phone number had changed. Homeward replaced Hill's home number with his cellphone number in its records. When Hill fell behind on his mortgage payments he instructed Homeward to only call his cellphone to collect his payments, leaving his cellphone number the only number listed in Homeward's records. Homeward called Hill an alleged 482 times from 2009 to 2013 by auto-dial and manual-dial.

Hill filed suit in federal court alleging that Homeward's calls constituted either knowing or negligent violations of the Telephone Consumer Protection Act ("TCPA"). Each side moved for summary judgment, but the court denied the motions. The jury returned a general verdict for Homeward and the court accepted the verdict and issued judgment. Hill appealed.

HOLDING: Affirmed.

REASONING: Hill argued that the jury instruction on "prior express consent" was too broad because it left out a small excerpt. The omitted excerpt included the instruction that "prior express consent" is granted only if the wireless number was provided during the transaction that resulted in the debt owed. Hill argued the word *initial* should be added before "transaction," thus limiting consent to only when it's given at the "*initial transaction*."

The Sixth Circuit held that the language in the jury instruction was proper. The jury instruction adequately reflected the legal definition of "prior express consent" promulgated by the Federal Communications Commission ("FCC"). The instructions paraphrased the FCC's definition of "prior effective consent"—that a party who gives an "invitation or permission to be called at [a certain] number" has given its express consent with respect to that number. The instructions quote verbatim the FCC's later clarification of that definition in the debtor—creditor context; that a creditor doesn't violate the Act when it calls a debtor who has "provided [his number] in connection with an existing debt." The FCC never used the word *initial* or *original* before "*transaction*" that involves the debt, but said that the debtor has given consent when he gives his number "*during the transaction*." A debtor does not need to give his consent to automated calls specifically; his general consent to being called on a cellphone constitutes "prior express consent." Hill gave his cellphone number to Homeward during the transaction and, therefore, provided Homeward with "prior express consent" under the TCPA.

The jury instruction adequately reflected the legal definition of "prior express consent" promulgated by the Federal Communications Commission.

DEBT COLLECTION

UNPAID PROPERTY TAXES ARE NOT A DEBT UNDER THE FAIR DEBT COLLECTION PRACTICES ACT ("FDCPA")

Armstrong v. Bardill, ___ F. Supp. 2d ___ (M.D.N.C. 2015).
http://law.justia.com/cases/federal/district-courts/north-carolina/ncmdce/1:2013cv01140/64768/15/

FACTS: Defendant, Mark Bardill ("Bardill"), attempted to collect a debt for unpaid property taxes and associated amounts owed for attorney fees, court costs, service costs, and a copy charge from Plaintiff, Cory Armstrong ("Armstrong"). Armstrong initiated suit, alleging Bardill's debt collection practices violated the FDCPA. Bardill filed a motion to dismiss for failure to state a claim because the FDCPA does not apply to the collection of unpaid property taxes.
HOLDING: Affirmed.
REASONING: Since the FDCPA does not apply to the collection of unpaid property taxes or other obligations imposed by law, Bardill argued Armstrong failed to state a claim. The court stated that property taxes do not qualify as debt because debt is defined as an obligation arising out of a transaction where the money, property, insurance, or services, which are the subject of the transaction are primarily for personal, family, or household purposes. The court agreed that there is no "transaction" here of the kind contemplated by the FDCPA.

PHONE CALL WAS NOT COMMUNICATION IN CONNECTION WITH DEBT

Brown v. Van Ru Credit Corp. ___ F.3d ___ (6th Cir. 2015).
http://caselaw.findlaw.com/us-6th-circuit/1716304.html

FACTS: Plaintiff-Appellant, William Brown III ("Brown") owed debt on a student loan, which Defendant-Appellee, Van Ru Credit Corporation ("Van Ru") was retained to collect. A Van Ru employee left a voicemail at Brown's business that stated the caller's and Van Ru's names, a return number, and a reference number. The caller asked that someone from the business's payroll department return her call. Brandon Harris, an employee at the business, heard the message and was aware that Van Ru was a debt collector.

Brown filed suit, alleging Van Ru's voicemail violated two provisions of the FDCPA. First, Brown alleged that Van Ru violated 15 U.S.C. §1692c(b) by communicating with a third party regarding Brown's debt. Second, Brown alleged that Van Ru violated 15 U.S.C. §1692g(a) by failing to provide required written notices after an initial communication with the consumer. The district court granted Van Ru's motion for judgment on the pleadings and denied Brown's motion to amend his complaint. Brown appealed.
HOLDING: Affirmed.
REASONING: Under the FDCPA, "communication" is defined as "the conveying of information regarding a debt directly or indirectly to any person through any medium." 15 U.S.C. §1692a(2) (West 2015). To convey information regarding a debt, a communication must at a minimum imply the existence of a debt. The Sixth Circuit Court held Van Ru's voicemail was not a communication because it did not convey information regarding Brown's debt. The court reasoned that the reference number and toll-free number only gave the impression that the caller had some type of business relationship with Brown. The fact that the voicemail asked for someone from payroll to call back suggested only that Van Ru sought some sort of payroll information.

AGREEMENT FINANCING COMPANIES, MADE WITH TORT PLAINTIFFS SEEKING FUNDS TO PAY PERSONAL EXPENSES WHILE WAITING FOR THEIR LAWSUITS TO SETTLE OR GO TO TRIAL WERE LOANS

Oasis Legal Fin. Grp. V. Coffman ___ P.3d ___ (Colo. 2015).
http://www.cobar.org/opinions/opinion.cfm?opinionid=9991&courtid=2

FACTS: The petitioner, Oasis, was in the business of buying interests in the potential proceeds of personal injury cases by executing agreements with tort plaintiffs. By the terms of the agreements, the money could not be used to prosecute the legal claims, because the tort plaintiffs were to use the funds to pay personal expenses. In exchange, the tort plaintiffs agree to pay Oasis a portion of future litigation proceeds. This amount included the amount advanced and an additional amount based on a "multiplier" that increased based on the length of time it took for the lawsuit to reach a resolution. If litigation proceeds were less than the amount due, the tort plaintiffs were not required to repay the shortfall.

The court stated that unconditional obligation to repay is not required for these types of transactions to be considered loans, because the analysis depends upon the design of the transaction.

The Office of the Administrator of the Colorado Uniform Commercial Credit Code ("UCCC") issued an opinion letter, which classified these transactions as loans under the UCCC. Oasis filed an action against the Attorney General and the Administrator ("the State") seeking a declaratory judgment arguing the funding agreements as asset purchases rather than loans. The trial court found for the State and held that transactions of this type constitute loans under the UCCC. The court of appeals affirmed the trial court's decision. Oasis appealed.
HOLDING: Affirmed.
REASONING: The Colorado Supreme Court found that the litigation financing transactions were loans subject to Colorado's UCCC. The court began by discussing the purpose of the UCCC as well as the policies behind the statute, which is meant to be liberally construed so as to protect consumers from unfair practices, foster competition among credit suppliers, and simplify consumer credit law. Under the UCCC, "consumer loan" is defined as loans made by a person or entity that regularly makes loans and meets four requirements. First, the consumer must be a person, not an organization. Second, the debt must be incurred primarily for personal, family or household purposes. Third, the debt must be by written agreement payable in installments or a finance charge

must be made. Fourth, the principal may not exceed $75,000, unless it is secured by an interest in land.

The court then applied each of the four elements to the agreements in question and found that the tort plaintiffs were "persons," and the advances were for personal, family or household purposes, and that the sums were below the $75,000 limit. The court also determined that the transactions created debt, because they created an obligation to repay. The court further stated that unconditional obligation to repay is not required for these types of transactions to be considered loans, because the analysis depends upon the design of the transaction.

LETTER SENT AFTER CONSUMER DISPUTED DEBT VIOLATES FAIR DEBT COLLECTION PRACTICES ACT

Leeb v. Nationwide Credit Corp. ___ F.3d ___ (7th Cir. 2015).
http://law.justia.com/cases/federal/appellate-courts/ca7/14-1329/14-1329-2015-11-20.html

FACTS: Appellee Gregory Leeb ("Leeb") disputed a debt owed to Appellant Nationwide Credit Corporation ("Nationwide") for a medical provider claim. Leeb claimed that his insurance company should have paid debt and Nationwide should acknowledge that such debt was disputed and refrain from making any negative credit reports. Leeb informed the medical provider of insurer's responsibility for payment and the medical provider took Leeb's account out of collections. Leeb informed Nationwide of the transaction. Nationwide sent a letter to Leeb including his debt balance, instructions on payment, acknowledgement of his dispute, a request for more information, and a statement that the letter was "from a debt collector attempting to collect a debt and any information obtained will be used for that purpose."

Leeb filed suit, contending that by sending the letter and not "ceasing collection" until it verified the debt, Nationwide violated the FDCPA. The district court held for Leeb on summary judgment. Nationwide appealed.
HOLDING: Affirmed.
REASONING: Nationwide argued that because Leeb did not subjectively view the letter as an attempt to collect the debt before it was verified and that the letter acknowledged that the debt was disputed, it should not be concluded as an attempt. Therefore they did "cease collection" under the FDCPA. 15 U.S.C.S. §1692g(b).

The Third Circuit rejected Nationwide's argument, reasoning that an objective standard is used to determine whether a letter was sent "in connection with an attempt to collect a debt" so it is likewise appropriate for the inquiry of whether sending a particular letter, a debt collector failed to "cease collection." Leeb not believing he owed the debt did not strip him of §1692g(b) protection.

The court reasoned that Nationwide sent its letter in response to Leeb's demand for an acknowledgement of his dispute, but Leeb did not demand a letter "from a debt collector attempting to collect a debt," stating his balance and instructing him to send payment. When the content and context are analyzed objectively, Nationwide's letter was an attempt to collect a debt, so Nationwide failed to "cease collection," violating §1692g(b).

TEXAS DEBT COLLECTION ACT CLAIMS FAIL

Rucker v. Bank of America, ___ F.3d ___ (5th Cir. 2015).
http://law.justia.com/cases/federal/appellate-courts/ca5/15-10373/15-10373-2015-11-20.html

FACTS: Diana Rucker ("Rucker") sued Bank of America ("BOA"), her mortgage servicer, claiming that BOA misrepresented the status of the mortgage, in violation of the Texas Debt Collection Act (TDCA). The district court concluded that the economic-loss rule applied to TDCA claims and granted summary judgment in favor of BOA. Before the parties filed briefs on appeal, the court of appeals decided, in *McCaig v. Wells Fargo Bank, N.A.*, 788 F.3d 463, 474-75 (5th Cir. 2015), that the economic-loss rule does not bar TDCA claims. Rucker appealed.
HOLDING: Affirmed
REASONING: The Fifth Circuit explained the TDCA prohibits mortgage servicers from attempting to recover an outstanding loan by threatening to take action prohibited by law. Rucker alleged that BOA's threat of foreclosure was unlawful because BOA had not yet given the statutorily required notice of acceleration. The court noted because Rucker was in default for several years, irrespective of any statutory notice requirement, BOA did not violate TDCA by threatening to foreclose.

The court added that TDCA prohibits mortgage servicers from making misrepresentation about a debt. The court examined the letters, which Rucker contended that BOA sent. It concluded that they were consistent with the amounts she owed, properly described her debts and obligations, and explicitly stated that the loan was in default, thus the letters are not a misrepresentation.

ARBITRATION

ANTITRUST ATTACK ON CREDIT CARD ARBITRATION CLAUSE FAILS.

Ross v. Citigroup, Inc., ___ F.3d ___ (2d Cir. 2015).
https://www.courtlistener.com/opinion/3155989/ross-v-citigroup-inc/

FACTS: Robert Ross and other individual cardholders ("Plaintiffs") initiated a lawsuit against Citigroup, Inc., and other credit card issuing banks ("Defendants"). Plaintiffs alleged that defendants illegally colluded to adopt class-action-barring arbitration clauses in their agreements with cardholders, in violation of the Sherman Act, 15 U.S.C. §1. After a five-week bench trial, the district court ruled in favor of the defendants. Although the court found that there was conscious parallel action by defendants in the adoption of the arbitration clauses, the court believed that the decision to include the clauses in cardholder agreements was something that each card issuing banks hashed out internally, and, therefore, did not meet the collusion threshold of §1 of the Sherman Act. Plaintiffs appealed.
HOLDING: Affirmed.
REASONING: Plaintiffs challenged the finding that defendants did not collusively adopt class-action-barring arbitration clauses in violation of the Sherman Act. The Second Circuit noted eight factors that must be weighed in addition to a finding of conscious parallel action to find defendants in violation of the Sherman Act. The factors the court listed included: (1) whether defendants had a motive to collude, (2) the quantity and nature of the inter-firm communications between defendants and other issuing banks, (3) whether the acts were contrary to the self interest of the defendants, (4) whether the arbitration clauses were "artificially standardized" as a result of an illegal agreement, (5) whether communications about a separate conspiracy to fix foreign currency exchange fees helped prove the instant conspiracy (6) whether the lack of notes, internal work product, or recollection regarding meetings may suggest a conspiracy, (7) the documentation of the meetings, and (8) recollections of the meetings. After weighing the evidence against these factors, the court found that the defendants adopted the class-action-barring clauses individually, and the district court's ruling for the defendants was affirmed.

ARBITRATION AGREEMENT SIGNED BY NURSING HOME RESIDENT'S ATTORNEY IN FACT NOT ENFORCEABLE

Extendicare Homes, Inc. v. Whisman, ___ S.W.3d ___ (Ky. 2015).
http://law.justia.com/cases/kentucky/supreme-court/2015/2013-sc-000426-i.html

FACTS: Van Buren Adams executed a power-of-attorney document (the "Adams-Whisman POA") designating his daughter, Belinda Whisman ("Whisman"), as his attorney-in-fact. Adams was then admitted as a resident at Extendicare Homes, Inc. ("Extendicare"), a nursing home. Whisman executed the documents required for Adams' admission to Exendicare and signed an arbitration agreement.

After Adams' death, his estate brought suit against Extendicare, who in turn moved to submit the dispute to arbitration. Whisman argued that the power of attorney document did not vest Whisman with the authority to commit Adams' claims to arbitration.

Extendicare claimed that the authority "to institute or defend suits concerning my property or rights" transferred by the agreement implicitly carried with it the authority to enter into the pre-dispute arbitration agreement. The lower court concluded that the Adams-Whisman POA did not give Whisman the authority to waive Adams' estate's right to bring a lawsuit before a jury rather than before an arbitration panel. Extendicare appealed the lower court's decision and the court of appeals also denied Extendicare's motion and ruled in favor of Whisman. Extendicare appealed.

The authority to waive the constitutional right to a jury trial should not be inferred absent express authorization in the power-of-attorney document.

HOLDING: Affirmed.
REASONING: The Kentucky Supreme Court explained that the fundamental principle of contract formation is that, to create a valid contract, there must be a voluntary, complete assent by the parties having capacity to contract. This principle also applies when the issue is the formation of an arbitration agreement, which the parties must provide express assent. An attorney-in-fact can provide a person's assent to a contractual agreement only if the authority to do so was duly conferred upon the attorney-in-fact by the power-of-attorney instrument.

The supreme court held the authority to waive the constitutional right to a jury trial should not be inferred absent express authorization in the power-of-attorney document. Courts should strictly construe the power-of-attorney in conformity with the principal's purpose. Thus, the attorney-in-fact in this case did not have the express authority to bind the principle to an arbitration agreement.

ARBITRATION CLAUSE BINDING ON NON-SIGNATORY BENEFICIARY OF WILL

Ameriprise Fin. Servs. v. Jones, ___ So. 3d ___ (Ala. 2015).
http://law.justia.com/cases/alabama/supreme-court/2015/1140893.html

FACTS: Charles Jones ("Defendant") opened two investment accounts with Ameriprise Financial Services ("Plaintiff") that required execution of an agreement ("the Agreement") containing an arbitration provision. Defendant executed a will leaving all property to the Plaintiff. When Defendant died, Plaintiffs made a claim for the funds in the Defendant's accounts, which were denied. Defendants filed a motion in response seeking to compel arbitration.

The Plaintiff conceded they were equitably estopped from avoiding arbitration as to all their claims except for a tort-of-outrage claim. The Alabama Circuit Court concluded that all claims except the tort-of-outrage claim must be arbitrated and that the tort-of-outrage claim would proceed to trial. Defendant appealed solely as to the circuit court's ruling on the arbitrability of the tort-of-outrage claim.

HOLDING: Reversed and remanded.

REASONING: The Alabama Supreme Court found that the Plaintiffs established themselves as third-party beneficiaries of the Agreement and rendered themselves subject to the accompanying burdens created by it. Further, the Agreement, by its express terms, applied to "all controversies that may arise." The supreme court found this language to refer to "any controversies," not merely those that arose between the parties or related to the Agreement.

ARBITRATION IN CONTRACT WRITTEN IN ENGLISH NOT ENFORCEABLE WHEN CONTRACT NEGOTIATED IN SPANISH AND TRANSLATED INTO SPANISH

Ramos v. Westlake Services, ___ Cal. Rptr. 3d ___ (Cal. Ct. App. 2015).
http://www.courts.ca.gov/opinions/documents/A141353.PDF

FACTS: Plaintiff Alfredo Ramos ("Ramos") purchased a used automobile from Pena's Motors ("Pena's Motors"). Pena's Motors had authority to sell and make representations on behalf of Defendant Westlake Services LLC ("Westlake") regarding the sale of its Guaranteed Auto Protection ("GAP") contracts. The negotiation for Ramos's purchase was conducted primarily in Spanish. Pena's Motors then provided Ramos with what purported to be a Spanish translation of the sales contract written in English. Ramos signed the English contract. Westlake later charged Ramos money for a GAP contract.

Ramos sued Westlake for failing to provide him a Spanish translation of the GAP contract. Westlake moved to compel arbitration of Ramos's claim alleging that the sales contract signed by Ramos contained arbitration agreement. Ramos argued that there was no arbitration agreement because the contract was negotiated primarily in Spanish and the Spanish translation of the contract provided by Pena's Motors did not include the arbitration provisions. The trial court denied Westlake's motion to compel arbitration finding that the Spanish translation of the contract that Ramos received did not contain the arbitration provisions. Westlake appealed.

HOLDING: Affirmed.

REASONING: Westlake argued the trial court erred by finding that Westlake had not shown the existence of an arbitration agreement. The court of appeals rejected Westlake's argument by concluding that there was no mutual assent regarding the arbitration agreement and Ramos reasonably relied on the provided Spanish translation of the English contract that lacked arbitration provisions.

First, mutual assent did not exist when the arbitration provisions were hidden in the English contract and not included in the Spanish translation given to Ramos. The court of appeals found that this is a claim of fraud in the execution of the arbitration agreement. A contract is void for fraud in the execution when the signor is deceived as to the nature of his act and actually does not know what he is signing.

A contract is void for fraud in the execution when the signor is deceived as to the nature of his act and actually does not know what he is signing.

Second, Ramos's reliance on the Spanish translation lacking arbitration provisions was reasonable. When Ramos was provided with a document that purported to be the Spanish translation of the English Contract that Ramos had to sign, Pena's Motors implicitly represented to Ramos that the translation was accurate. The court of appeals further opined that it would be inconsistent to hold that Ramos was not entitled to rely on the accuracy of the translation when the translation is required by the Consumers Legal Remedies Act.

BANKRUPTCY

ATTORNEYS' FEES MAY BE AWARDED IN A SUIT FOR DAMAGES TO PROVIDE REDRESS FOR A VIOLATION OF THE AUTOMATIC BANKRUPTCY STAY

In Re Schwartz-Tallard, 803 F.3d 1095 (9th Cir. 2015).
http://cdn.ca9.uscourts.gov/datastore/opinions/2015/10/14/12-60052.pdf

FACTS: Irene Schwartz-Tallard ("Schwartz-Tallard"), the debtor, took out a mortgage on her home in Nevada. Schwartz-Tallard subsequently filed a Chapter 13 bankruptcy petition, after which she continued making monthly mortgage payments to America's Servicing Company ("ASC"). Due to a mistake on their part, ASC foreclosed on Schwartz-Tallard's home. Soon thereafter, ASC purchased the home at the foreclosure sale and promptly served Schwartz-Tallard with an eviction notice.

Schwartz-Tallard then filed a motion in bankruptcy court, requesting relief under 11 U.S.C. §362. Specifically, Schwartz-Tallard sought an order requiring ASC to re-convey title to the home as well as an award of actual damages, punitive damages, and attorneys' fees. The bankruptcy court found for Schwartz-Tallard, and ordered ASC to re-convey title to Schwartz-Tallard. The bankruptcy court also awarded $40,000 in economic and emotional distress damages, $20,000 in punitive damages, and $20,000 for attorneys' fees.

ASC appealed to the federal district court that ultimately upheld the ruling of the bankruptcy court. Subsequently, Schwartz-Tallard returned to the bankruptcy court to recover the $10,000 in attorneys' fees incurred in district court opposing ASC's appeal. The bankruptcy court denied this motion. Schwartz-Tallard appealed to the Bankruptcy Appellate Panel ("BAP") that reversed, finding that Schwartz-Tallard was entitled to the $10,000 in additional attorneys' fees incurred in federal district court.

HOLDING: Affirmed

REASONING: The Ninth Circuit analyzed 11 U.S.C. §362(k) that allows for the recovery of "actual damages, including costs and attorneys' fees." The court stated that the Bankruptcy code did not contain any provisions specifically authorizing sanctions for violations of an automatic stay, but noted that courts generally treated stays like court orders, thereby awarding damages when automatic stays were knowingly violated. The court also explained that the American Rule usually requires parties to bear their own attorneys' fees, but the common law always recognized an exception to permit fee awards in litigation brought to remedy willful violations of court orders.

The court discussed congressional intent for §362(k), finding that Congress could not have meant to allow the recovery of attorneys' fees incurred in litigation ending the stay violation, while disallowing the recovery of attorneys' fees incurred for the recovery of damages. The statute states "including costs and attorneys' fees," with no limitation on the remedy or type of damage for which the fees are incurred. The court found that Schwartz-Tallard was entitled to the $10,000 in additional attorneys' fees incurred while defending the damages award on appeal in federal district court.

MISCELLANEOUS

MINOR CHANGES IN TELEMARKETING LANGUAGE DO NOT DEFEAT CLASS CERTIFICATION

Reyes v. Netdeposit, LLC, 802 F.3d 469 (3d Cir. 2015).
http://www2.ca3.uscourts.gov/opinarch/141228p.pdf

FACTS: Plaintiff, Reynaldo Reyes ("Reyes") provided his bank account information to NHS Systems in an unsolicited phone call. NHS Systems contracted with Defendants, Zions First National Bank and its payment-processor subsidiaries ("Zions") to make two unauthorized debits from Reyes's bank account. When Reyes called to complain about the withdrawals, he alleged that he was directed to a misleading audio recording. Reyes alleged that Zions operated a complete sham enterprise, involving slightly different sales pitches to offer individuals various valueless products in order to obtain consumer's bank account information and make unauthorized debits.

Reyes filed a class action suit, alleging civil violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO") under 18 U.S.C. §1962(c) and (d). The district court denied class certification, concluding that Reyes failed to satisfy the elements of commonality and predominance under Federal Rule 23 because Zions utilized non-standardized sales scripts with minor changes in language to defraud individuals. Reyes appealed.

HOLDING: Vacated and remanded

REASONING: Reyes argued that the manner in which individuals were defrauded was irrelevant because Zions engaged in systematic fraud and operated a business without any "legitimate business substance."

The Third Circuit held that under this "complete sham" theory, the predominance requirement could be satisfied by an overarching theme of fraud and defining fraudulent aspects of Zions' conduct. A class may be certified in spite of slight variations that may occur in the perpetration of a fraudulent scheme.

> **Requiring "absolute conformity of conduct and harm... for class certification" would allow "unscrupulous businesses [to] victimize consumers with impunity merely by tweaking the language in a script . . . "**

The court further explained that requiring "absolute conformity of conduct and harm… for class certification" would allow "unscrupulous businesses [to] victimize consumers with impunity merely by tweaking the language in a script . . . "

OFFER OF THE FULL AMOUNT REQUESTED IN A TELEPHONE CONSUMER PROTECTION ACT SUIT DOES NOT MOOT THE CASE

Chapman v. First Index, Inc., 796 F.3d 783 (7th Cir. 2015).
http://caselaw.findlaw.com/us-7th-circuit/1710075.html

FACTS: Plaintiff-Appellant, Arnold Chapman ("Chapman"), received two unsolicited faxes from Defendant-Appellee, First Index, Inc. ("First Index"). Chapman filed suit alleging that First Index violated the Telephone Consumer Protection Act, and requested an injunction against First Index and $3,000. First Index claimed they had obtained oral permission from the fax recipients.

First Index made an offer of judgment under Rule 68 of Federal Rules of Civil Procedure (FRCP) for $3,002, an injunction, and set a deadline for Chapman's acceptance. Chapman never replied and the offer lapsed. First Index subsequently asked the district court to dismiss Chapman's claim as moot. The district court granted First Index's motion to dismiss and entered a final, take-nothing judgment. Chapman appealed.

HOLDING: Vacated and remanded.

REASONING: First Index argued that the case became moot when their offer of judgment lapsed. The Seventh Circuit Court held that First Index's offer of full compensation pursuant to FRCP 68 did not render Chapman's claim moot. In coming to this conclusion, the court asserted that a case becomes moot only when the court cannot grant any effectual relief to the prevailing party. Applying this standard, the court held that Chapman's case was not moot because the district court could have awarded damages or have entered an injunction.

The court further reasoned that because a district court cannot enter judgment in a moot case, the case would inevitably self-destruct if an offer to satisfy all of the plaintiff's demands did in fact moot the case. Under this reasoning, the court noted that even if Chapman had accepted First Index's offer, the offer itself would have already rendered the case moot, and the district court could not have ordered First Index to pay.

The court asserted that Rule 68(d) provided the consequence of a plaintiff's decision not to accept a defendant's offer. According to Rule 68(d), the offeree would be required to pay any costs incurred after the offer was made if the judgment the offeree ultimately obtains is not more favorable than the unaccepted offer. The court could only have dismissed the case for lack of controversy. Instead of mooting the case, the court stated that acceptance of an offer of judgment that meets the full demands of the plaintiff is an affirmative defense, perhaps in the nature of estoppel or waiver.

RULE 68 OFFER TO INDIVIDUAL PLAINTIFF DOES NOT MOOT CLASS ACTION

Hooks v. Landmark Indus., Inc., 797 F.3d 309 (5th Cir. 2015).
http://www.ca5.uscourts.gov/opinions%5Cpub%5C14/14-20496-CV0.pdf

FACTS: Plaintiff-Appellant David Hooks ("Hooks") made a withdrawal from an automated teller machine (ATM) operated by Defendant-Appellee Landmark Industries, Inc. ("Landmark"). Landmark charged Hooks for the withdrawal, but did not post notice on or at the ATM to inform customers that a fee would be charged for its use, a violation of the Electronic Funds Transfer Act (EFTA).

Hooks filed suit, and the court responded with an initial class certification filing deadline. Landmark tendered an offer of judgment to Hooks under Federal Rule of Civil Procedure 68 (Rule 68), proposing to settle his claim and pay costs accrued and reasonable attorneys' fees until the date of acceptance. Hooks declined, and requested an extension on his certification filing, which was granted. Landmark filed a motion to dismiss for lack of subject matter jurisdiction. The district court certified the class and denied the motion to dismiss. Landmark filed a second motion to dismiss. The district court granted the motion. Hooks appealed.

HOLDING: Reversed and remanded.

REASONING: The Fifth Circuit noted a circuit split over the issue: some circuits held that a Rule 68 offer moots an individual's claim while other circuits held that an unaccepted Rule 68 offer cannot moot an individual's claim. Following the latter courts' logic—bolstered by a dissenting opinion from Justice Kagan in *Mabary v. Home Town Bank, N.A.*—the Fifth Circuit held that an unaccepted offer of judgment to a named plaintiff in a class action was a legal nullity and had no operative effect. Furthermore, the court found that a plaintiff who rejects an offer of judgment on his or her individual claim under Rule 68 has the choice to accept the offer and have the case dismissed or to reject the offer and proceed with the class action.

The Fifth Circuit's holding echoed a previously held concern for defendant-induced mootness in the case of class actions where defendants attempt to "pick off" individual plaintiffs before class certification "[b]y tendering to the named plaintiffs the full amount of their personal claims each time suit is brought as a class action." A contrary rule, the court noted, would encourage defendants to unilaterally moot the claims of named plaintiffs even when the plaintiffs turned down settlement offers and, therefore, had received no actual relief.

CLAIM AGAINST HOSPITAL BASED ON A SLIP AND FALL CLAIM IS NOT A HEALTH CARE LIABILITY CLAIM (HCLC) UNDER THE TEXAS MEDICAL LIABILITY ACT

Reddic v. E. Tex. Med. Ctr. Reg'l Health Care Sys., ___ S.W.3d ___ (Tex. 2015).
http://law.justia.com/cases/texas/supreme-court/2015/14-0333.html

FACTS: Appellee, Louisa Reddic ("Reddic"), a visitor at Appellant, East Texas Medical Center-Crockett Hospital ("the Hospital"), fell when she slipped on a floor mat between the Hospital's main entrance and the front desk. Reddic sued the Hospital

Reddic's claim was not a HCLC because it did not have a sufficient enough relationship to the providing of health care.

on a premises liability theory. The Hospital responded by filing a motion to dismiss in which it asserted that Reddic's claim was a HCLC under the Texas Medical Liability Act ("the Act"), and she did not serve an expert report, required by the Act.

The trial court denied the Hospital's motion, but the court of appeals reversed. Reddic appealed.

HOLDING: Reversed and remanded.

REASONING: Reddic argued that the facts underlying her claim did not have a substantive relationship with the Hospital's provision of health care and, therefore, it was not a HCLC.

The Texas Supreme Court agreed and found that Reddic's claim was not a HCLC because it did not have a sufficient enough relationship to the providing of health care. The supreme court explained that the pivotal issue in a safety standards-based claim is whether the standards on which the claim is based implicate the defendant's duties as a health care provider, including its duties to provide for patient safety.

Reddic's claim was not a HCLC because it did not have a sufficient enough relationship to the providing of health care.

For a claim to be a HCLC, the Act requires that it must have more of a relationship to the provision of health care than that it arises from an occurrence inside a hospital. The record did not show that the safety standards at issue were related to the provision of health care by anything more than the location of Reddic's fall being inside a hospital.