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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

COURT OF APPEAL-4TH DIST DIV 3

FILED

SEP 02 2004

MUAMMER GONLUGUR,

Plaintiff and Respondent,

v.

CIRCUIT CITY STORES, INC., et al.,

Defendants and Appellants.

Deputy Clerk _____

G033351

(Super. Ct. No. 03CC11348)

OPINION

Appeal from an order of the Superior Court of Orange County, Ronald L. Bauer, Judge. Affirmed.

Livingston & Mattesich, Rex Darrell Berry, Marc B. Koenigsberg and Karen L. Turner for Defendants and Appellants.

Harris & Kaufman, Matthew A. Kaufman and William E. Harris for Plaintiff and Respondent.

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Defendants Circuit City Stores, Inc. and Circuit City Stores West Coast Inc. appeal from an order denying their petition to compel arbitration of plaintiff Muammer Gonlugur's claim for overtime pay. They contend the court erred in sustaining objections to their evidence of arbitration rules and that they established the existence of an arbitration agreement governing the dispute. We determine that, by virtue of defendants' rules governing arbitration, the agreement is unconscionable, and affirm.

FACTS

Plaintiff, defendants' employee, filed a class action seeking overtime wages and related penalties pursuant to various sections of the Labor Code and Business and Professions Code. In response, defendants filed a petition to compel arbitration. They alleged, and plaintiff did not dispute, that at the time plaintiff submitted his job application in October 1997, as a condition of being considered for employment, he was required to and did sign a dispute resolution agreement (agreement). Defendants filed the declaration of Teri Miles, their assistant general counsel of employment who supervised the arbitration program, to which was attached a copy of the agreement. The agreement required plaintiff to settle all claims arising out of his application for employment, actual employment, or termination of employment by binding arbitration. It contained a one-year statute of limitations for bringing claims and provided the arbitration would be conducted pursuant to defendants' arbitration rules and procedures (rules). The declaration attached a copy of the 2003 version of their rules and stated that "[a]s part of the job application process, prospective applicants are provided a copy of the [rules]"

In his opposition to the petition, plaintiff objected to Miles's declaration. He asserted she had no personal knowledge that all applicants were given a copy of the rules, and particularly that plaintiff was given a copy or what version. He also objected

to her statement that the 2003 rules applied to the dispute. He argued that presumably, plaintiff would have been given the 1997 rules, and there was no testimony that defendants had properly given him notice of amendments to the rules as required by the 1997 rules.

Miles filed a supplemental declaration in which she stated that during her tenure, defendants' practice was to post a memorandum outlining changes to arbitration rules at each of its locations. She also declared her research revealed this had been done each year in which the rules had been amended.

The court sustained plaintiff's objections, finding the 1997 rules required that plaintiff be given 30 days' written notice of modifications to the rules. It stated that defendants "would have to present evidence that the new [set of rules] was brought to [plaintiff's] attention" and had failed to do so. It further stated that, as a result, defendants were left with the 1997 version of the rules, which the court believed "even [defendants] would acknowledge [was] a dead-bang loser. [¶] You wouldn't pretend to assert that as a basis for arbitration in view of the restrictions that it places upon the employee." It denied the petition, finding there was insufficient evidence of the arbitration contract.

DISCUSSION

Preliminarily, defendants point out the rules provide that the substantive law of the state in which the employee works governs the substantive claim, but the enforceability of the agreement is determined by the Federal Arbitration Act (9 U.S.C. § 1 et seq.; FAA) and the Uniform Arbitration Act of Virginia (8.01-581.01 et seq.). Other than this, defendants make no reference to Virginia law. We decline to speculate on why, but note that by their failure to cite to it, defendants have waived any right to rely on it. (*People v. Stanley* (1995) 10 Cal.4th 764, 793; see *Szetela v. Discover Bank* (2002)

97 Cal.App.4th 1094, 1099, fn. 3.) Accordingly, if federal law defers to state law in determining enforceability, we will use California law, as the parties have done.

Existence of an Enforceable Arbitration Agreement

Defendants argue they met their burden to establish an arbitration agreement because they showed plaintiff signed the agreement that required him to arbitrate, his dispute falls within the terms of the agreement, the agreement provided the rules could be amended, and their practice was to post amendments. They contend that is all they were required to show. They further rely on the fact that plaintiff himself filed no declaration in opposition to their petition and that he does not challenge the existence of the agreement. Thus, they argue, they have established the existence of an arbitration agreement and the court must grant their petition. We disagree.

Contrary to defendants' claim, their burden is not to show the existence of an agreement to arbitrate but the existence of an *enforceable* agreement to arbitrate. (*Omar v. Ralphs Grocery Co.* (2004) 118 Cal.App.4th 955, 961.) Both federal and state law provide that an arbitration agreement is not enforceable if there is a basis for the revocation of a contract. (9 U.S.C § 2 [arbitration provision enforceable except where there are grounds "for the revocation of any contract"]; Code Civ. Proc., § 1281 [same].) In determining validity of an arbitration agreement, we look to "ordinary state-law principles that govern the formation of contracts. [Citations.]" (*First Options of Chicago, Inc. v. Kaplan* (1995) 514 U.S. 938, 944 [115 S.Ct. 1920, 131 L.Ed.2d 985].) "Thus, although 'courts may not invalidate arbitration agreements under state laws applicable only to arbitration provisions,' general contract defenses such as fraud, duress, or unconscionability, grounded in state contract law, may operate to invalidate arbitration agreements. [Citation.]" (*Circuit City Stores, Inc. v. Adams* (9th Cir. 2002) 279 F.3d 889, 892, italics omitted.)

Plaintiff argues the agreement is unconscionable. Since this is a ground for revoking a contract, it is properly considered in deciding a petition to compel arbitration. (*Condee v. Longwood Management Corp.* (2001) 88 Cal.App.4th 215, 219.) Plaintiff relies primarily on the unconscionability of the 1997 rules, although he also maintains the 2003 rules are defective for the same reason. Defendants devote a substantial portion of their briefs challenging the court's sustaining of plaintiff's objections to Miles's declaration. They contend the 2003 rules should apply and that they pass muster. We need not decide the evidentiary question. Using the 2003 rules, as defendants suggest, we still find the agreement unconscionable.

Unconscionability

An arbitration agreement will not be enforced if it is unconscionable. (*Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, 114 (*Armendariz*)). “The prevailing view is that [procedural and substantive unconscionability] must both be present . . . for a court to exercise its discretion to refuse to enforce a contract or clause under the doctrine of unconscionability. [Citations.]” (*Stirlen v. Supercuts, Inc.* (1997) 51 Cal.App.4th 1519, 1533, italics omitted.) “The procedural element focuses on the unequal bargaining positions and hidden terms common in the context of adhesion contracts. [Citation.] . . . [T]he substantive element . . . traditionally involves contract terms that are so one-sided as to ‘shock the conscience,’ or that impose harsh or oppressive terms. [Citation.]” (*24 Hour Fitness, Inc. v. Superior Court* (1998) 66 Cal.App.4th 1199, 1213 .)

Substantive Unconscionability

A primary indication of substantive unconscionability is the lack of mutuality in the agreement. Here, the agreement requires plaintiff to resolve “any and all previously unasserted claims, disputes or controversies arising out of or relating to [his]

application or candidacy for employment, employment[,] and/or cessation of employment with [defendants], exclusively by final and binding arbitration” There is no explicit language imposing this requirement on defendants.

Granted, there is some verbiage in the rules that suggests defendants are so bound. For example, the rules state that they apply to arbitrations “held pursuant to the [agreement], whether brought by an [employee] or [defendants].” In addition, they provide that all employment-related disputes “shall be settled exclusively by final and binding arbitration Arbitration shall apply to any and all such disputes . . . whether asserted against [defendants] and/or against any employee”

Miles declared that defendants have initiated more than 50 arbitrations; in her supplemental declaration she stated that since the origin of their arbitration program, defendants never “filed suit over an employment[-]related legal dispute against any [employee] who is a party to the [agreement].” However, noticeably absent from either declaration is a statement that defendants consider themselves bound to arbitrate. Without deciding the issue, we are not persuaded of the mutuality of the agreement.

However, there are several provisions in the agreement that plainly evidence lack of mutuality. First, to commence an arbitration, virtually the only way an employee can sue defendants, he or she must pay a \$75 filing fee to defendants along with the request to arbitrate. “[W]hen an employer imposes mandatory arbitration as a condition of employment, the arbitration agreement or arbitration process cannot generally require the employee to bear any *type* of expense that the employee would not be required to bear if he or she were free to bring the action in court.” (*Armendariz, supra*, 24 Cal.4th at pp. 110-111.) Although he would have to pay a court filing fee, plaintiff would never be required to pay defendants a fee if he were initiating a state court action. Moreover, if defendants wish to commence an arbitration, the agreement does not require them to pay the employee a fee.

In *Ingle v. Circuit City Stores, Inc.* (9th Cir. 2003) 328 F.3d 1165, the court found this same provision unconscionable based on *Armendariz*. (*Id.* at p. 1177.) In addition, it stated that by “requiring employees to pay the fee to the very entity against which they seek redress, [defendants] may very well deter employees from initiating complaints.” (*Ibid.*)

Defendants rely on the provision that allows them to waive the fee, but this does not save them. First, an employee must “demonstrate[an] inability to pay.” Conceivably, this requires an employee to disclose otherwise privileged, or at least private, financial information, an undue burden. And, as stated in *Circuit City Stores, Inc. v. Mantor* (9th Cir. 2003) 335 F.3d 1101 in which the court considered and rejected this very provision, the fact that the agreement gives defendants “the sole discretion to consider applications for waivers indicates that the process of filing could be halted unilaterally by [defendants] if an employee does not have the means to pay the . . . fee.” (*Id.* at p. 1108.) The court noted the provision “might not be one sided” if a “disinterested” third party decided whether the fee could be waived. (*Ibid.*) But, it continued, because the provision requires an employee to “pay an interested party ‘for the privilege of bringing a complaint’ and . . . assigns Circuit City, an interested party, the responsibility for this decision whether to waive the filing fee, this rule is manifestly one-sided, and therefore, substantively unconscionable.” (*Ibid.*, fn. omitted.) Miles declared defendants had “never declined to waive a filing fee” when requested. However, this does not abrogate the fact that defendants still have the power to waive or not.

The agreement also imposes a one-year statute of limitations on plaintiff. “The failure of an [employee] to initiate an arbitration within [one year after the date on which the employee knew or reasonably should have known of the facts giving rise to the claim] shall constitute a waiver with respect to that dispute relative to that [employee].” There is no such limitation on defendants when they file an employment-related arbitration action. Such a one-sided restriction is not permissible. (*Stirlen v. Supercuts*,

Inc. supra, 51 Cal.App.4th at p. 1542.) And, in yet another Ninth Circuit case analyzing defendants' arbitration rules, this provision was found to be unconscionable because it deprived the employee of "the benefit of the full range of statutory remedies." (*Circuit City Stores, Inc. v. Adams, supra*, 279 F.3d at p. 894.)

In addition, the rules bar class actions. We are aware that the issue of whether the FAA preempts a finding that a ban on class actions in an arbitration agreement makes it unconscionable is pending before our Supreme Court (*Discover Bank v. Superior Court*, S113725; *Mandel v. Household Bank (Nevada) National Ass'n.*, S113699). Until such time as it decides, however, the law is that such a provision is fundamentally unfair and unconscionable. (*Szetela v. Discover Bank, supra*, 97 Cal.App.4th at pp. 1101-1102.)

Procedural Unconscionability

Procedural unconscionability is often tied to an adhesion contract. (*Little v. Auto Stiegler, Inc.* (2003) 29 Cal.4th 1064, 1071.) Nonetheless, we may find "procedural unconscionability regardless of whether the contract is adhesive." (*Harper v. Ultimo* (2003) 113 Cal.App.4th 1402, 1410, italics omitted.) It can rest on elements of surprise and oppression. (*Id.* at p. 1406.) Here, both are present.

In order to even apply for a position, plaintiff was required to sign the arbitration agreement. If he was hired, the agreement applied. But, even if he had not been hired, he would have been required to arbitrate any dispute arising out of his application and rejection as an employee. This is "take it or leave it" to the nth degree. (*Szetela v. Discover Bank, supra*, 97 Cal.App.4th at p. 1100; see *Ingle v. Circuit City, supra*, 328 F.3d at p. 1172, fn. 4.)

Moreover, defendants have the unilateral right to amend the rules. Thus, if we accept defendants' claim that the applicable rules are those in effect when the arbitration is filed, plaintiff had no way to know at the time he initially agreed to arbitrate

what the rules would be at the time of the arbitration. This constitutes the requisite surprise. Defendants rely on the fact that changes to the rules are posted, but that does not give an employee notice at the time of the initial employment application.

Although there must be both procedural and substantive unconscionability before a court can refuse to enforce an arbitration agreement, “the two elements need not be present in the same degree.” (*O’Hare v. Municipal Resource Consultants* (2003) 107 Cal.App.4th 267, 273.) “[T]he more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa.” (*Armendariz, supra*, 24 Cal.4th at p. 114.) The record contains sufficient evidence of both substantive and procedural unconscionability to deny defendants’ petition to compel arbitration.

Severability

Defendants suggest that if we find one or more of the provisions of the rules or agreement offensive, we should sever them. They rely on the provision in the rules that if any part of the rules or agreement “conflict[s] with a mandatory provision of applicable law, [it] shall be modified automatically to comply” This, they argue, reflects the parties’ mutual intent “to preserve the core obligation to arbitrate while accommodating changes in the law that may later develop.” We are not persuaded.

“[T]he doctrine of severance attempts to conserve a contractual relationship if to do so would not be condoning an illegal scheme. [Citations.] . . . [¶] . . . If the central purpose of the contract is tainted with illegality, then the contract as a whole cannot be enforced.” (*Armendariz, supra*, 24 Cal.4th at p. 124.)

Such is the case here. The objectionable provisions permeate the entire agreement. “Such multiple defects indicate a systematic effort to impose arbitration on an employee not simply as an alternative to litigation, but as an inferior forum that works to the employer’s advantage.” (*Armendariz, supra*, 24 Cal.4th at p. 124.) In addition,

unconscionability would not be overcome by severing one provision. The court would be required to reform the agreement, a procedure not authorized under these circumstances. (*Id.* at p. 125.) Thus, severance is not appropriate.

DISPOSITION

The order is affirmed. Respondent is awarded his costs on appeal.

RYLAARSDAM, ACTING P. J.

WE CONCUR:

BEDSWORTH, J.

IKOLA, J.