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SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF SAN FRANCISCO

RYAN GUTIERREZ and JAMIE GUTIERREZ, on behalf of themselves and others similarly situated, Plaintiffs, vs. AUTO WEST, INC. dba Autowest Dodge; AUTONATION USA CORPORATION; WELLS FARGO BANK, LTD.; and DOES 1 through 30, inclusive, Defendants.	Case No. 317755 **NOTICE OF ENTRY OF ORDER**

TO ALL PARTIES AND THEIR ATTONREYS OF RECORD:

PLEASE TAKE NOTICE that on July 21, 2005, the Honorable James L. Warren entered the attached order regarding Autowest's motion to compel arbitration after remand from the Court of Appeal.

Date: August 1, 2005

SEVERSON & WERSON
A Professional Corporation

By _____
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IN THE SUPERIOR COURT OF THE STATE OF CALIFORNIA

IN AND FOR THE COUNTY OF SAN FRANCISCO

RYAN GUTIERREZ and JAMIE GUTIERREZ, on behalf of themselves and others similarly situated,

Plaintiffs,

v.

AUTO WEST, INC. dba Autowest Dodge; AUTONATION USA CORPORATION; WELLS FARGO BANK, LTD.; and DOES 1 through 30 inclusive,

Defendants.

Case No. CGC-00-317755

[PROPOSED] ORDER RE AUTO WEST'S MOTION TO COMPEL ARBITRATION AFTER REMAND FROM THE COURT OF APPEAL

Unlimited Civil Case

Date: June 7, 2005
Time: 9:30 a.m.
Dept. 301
Hon. James L. Warren

This case came back to the Superior Court on remand from the Court of Appeal's decision in *Gutierrez v. Auto West, Inc.*, 114 Cal.App.4th 77 (2003). The matter was originally heard on remand on December 15, 2004. The matter was then heard on June 7, 2005, at 9:30 a.m., in Dept. 301 of the above court. Plaintiffs were represented by Bryan Kemnitzer of

Kemnitzer, Anderson, Barron & Ogilvie. Defendants AUTONATION and AUTO WEST DODGE were represented by Laurence Jackson, of Christa & Jackson and defendant WELLS FARGO BANK was represented by Eric Gribben, of Severson & Werson, but it is not seeking to enforce the arbitration provision in the lease agreement. Having considered the pleadings and oral arguments of counsel, the Court finds as follows:

I. Instructions From the Court of Appeal

This Court originally found that the arbitration clause in the contract between GUTIERREZ and AUTO WEST DODGE and AUTONATION was, in fact, procedurally and substantively unconscionable. This Court determined that the arbitration was adhesive, and that the fees required to initiate the arbitration were so substantial that plaintiffs were unable to pay. The Trial Court's conclusion that the arbitration clause in the automobile lease is adhesive was found by the Court of Appeal to be supported by substantial evidence. (*Id* at p. 89.) The Court of Appeal in *Gutierrez v. Auto West, Inc.*, 114 Cal.App.4th 77 (2003), found that the lease was presented to plaintiffs for signature on a take-it-or-leave-it basis. Plaintiffs were given no opportunities to negotiate the printed terms on the lease, and the arbitration clause was particularly inconspicuous. (*Id* at p. 89.)

The Court of Appeal further concluded that, "where a consumer enters into an adhesive contract that mandates arbitration, it is unconscionable to condition that process on the consumer posting fees he or she cannot pay. It is self evident that such a provision is unduly harsh and one-sided, defeats the expectations of the non-drafting party, and shocks the conscience. While arbitration may be within the reasonable expectations of consumers, a process that builds prohibitively expensive fees into the arbitration process is not. "To state it simply, it is substantively unconscionable to require a consumer to give up the right to utilize the judicial system while imposing arbitral form fees that are prohibitively high. Whatever preference for

arbitration might exist, it is not served by an adhesive agreement that effectively involves every form for the redress of dispute, including arbitration itself." (*Id* at p. 89-90.)

The Court went on to conclude that the flaw in this arbitration agreement is readily apparent. Despite the potential for the imposition of a substantial administrative fee, there is no effective procedure for a consumer to obtain a fee waiver or reduction. (*Id* at p. 91.) To the extent the AAA rules create a procedure to ensure fees are unaffordable, it is ineffective. An arbitration agreement must provide some effective avenue of relief from unaffordable fees; this one does not. (*Id* at p. 92.)

After affirming the trial court's decision that the arbitration clause was unconscionable, the Court of Appeal remanded this case to this court to determine if the entire clause should be stricken or if the offending costs provision should be severed and the remainder of the contract enforced. "If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of the unconscionable clause as to avoid any unconscionable result." Id. at 92, quoting Civil Code § 1670.5. The Court of Appeal, relying on *Armendariz v. Foundation Healthy Psychcare Services, Inc.* (2000) 24 Cal.4th 83, found that "a single unconscionable term could justify a refusal to enforce an arbitration agreement if it were drafted in bad faith, because severing such a provision and enforcing the arbitration agreement would encourage the drafters of such agreements to overreach." *Gutierrez*, supra, 114 Cal.App.4th at 93.

The Court of Appeals left this court with the following instructions upon remand:

> We look, principally, at the clarity of the law at the time of the signing of the agreement to determine if the unconscionable provision was drafted in bad faith. (Armendariz). On remand, the court will determine if the provision requiring plaintiffs to pay substantial administrative fees was drafted in bad faith and, then, exercise its discretion to sever this provision or not. (*Id* at p. 93.)

II. The Clarity of the Law At the Time the Agreement was Signed

A. The Law Was Clear In March 2000 That Excessive Forum Costs Were Unlawful

Plaintiffs signed the subject lease agreement on March 19, 2000. In March 2000 there was no doubt that under California law arbitration costs so high that they effectively barred consumers from accessing the arbitral forum were unlawful.

As far back as 1975 the California Court of Appeals recognized that expensive filing fees could effectively bar a consumer's access to arbitration. (*Spence v. Omnibus Industries* (1975) 44 Cal.App.3d 970.) (The American Arbitration Association's (AAA) disproportionate filing fees could render an arbitration clause illusory. "In conclusion, there are many citizens who are not paupers who do not have sufficient funds to pursue arbitration when the filing fee is as large as was the filing fee in this case. For these citizens, the arbitration remedy is illusory." *Id.* at 976.)

Further, in *Patterson v. ITT Consumer Financial Corp.* (1993) 14 Cal.App.4th 1659, the court struck down an arbitration agreement in a consumer contract in part because of the exorbitant fees the consumer was required to pay. In that case, the fee schedule for arbitration was a filing fee of $98 and hearing fees of $750 per three-hour session – far less than the exorbitant fees plaintiffs would have had to pay to proceed to arbitration in the present case. The court found that "[t]he likely effect of these procedures is to deny a borrower against whom a claim has been brought any opportunity to a hearing . . . . In short, the procedure seems designed to discourage borrowers from responding at all." *Id.* at 1666.

Other courts around the country prior to March 2000 had also made clear that it was unlawful to draft an arbitration provision that required excessive arbitration costs and filing fees.[1]

[1] Federal cases on point are relevant to this discussion because plaintiffs also maintained that the imposition of unreasonable arbitration costs frustrated their ability to vindicate federal and state statutory rights. *Gutierrez*, 114 Cal.App.4th at 93-94.

In *Shankle v. B-G Maintenance Mgmt. of Colorado, Inc.*, 163 F.3d 1230 (10th Cir. 1999) while arbitration can offer an adequate forum to vindicate claims, "[t]his supposition falls apart [] if the terms of an arbitration agreement actually prevent an individual from effectively vindicating his or her statutory rights." *Id.* at 1234. Noting that an average arbitration would cost an employee between $1,875 and $5,000, the court concluded that a such a large sum would be prohibitive to many employees and that "[t]he Agreement thus placed [the employee] between the proverbial rock and a hard place – it prohibited the use of the judicial forum where a litigant is not required to pay for a judge's services, and the prohibitive cost substantially limited used of the arbitral forum." *Id.* at 1235 (citations omitted). Accordingly, the court concluded that the arbitration agreement at issue did not provide an effective mechanism for the vindication of the employees' rights and was therefore unenforceable. *Id.*

The Eleventh Circuit also found unenforceable an arbitration clause that required claimants to pay a $2,000 filing fee and to bear potential responsibility for a portion of the arbitrator's fees. It held that "costs of this magnitude [are] a legitimate basis for a conclusion that the clause does not comport with statutory policy [enabling people subjected to workplace discrimination to vindicate their rights]." *Paladino v. Avnet*, 134 F.3d 1054, 1062 (11th Cir. 1998).

Moreover, these federal circuit court decision are far from the only ones which, prior to March 2000, held that excessive forum fees could not lawfully be inserted into an arbitration agreement. See, e.g., *Martens v. Smith Barney, Inc.*, 181 F.R.D. 243, 255-56 (S.D.N.Y. 1998) (finding "arbitration agreements cannot impose financial burdens on plaintiff access to the arbitral forum" including steep filing fees and arbitrators' fees); *Brower v. Gateway 2000*, 676 NYS 2d 569, 574 (N.Y. App. 1998) (holding that an "excessive cost factor [of approximately $5,000] that is necessarily entailed" rendered a provision requiring arbitration in an International

Chamber of Commerce forum unconscionable); *Myers v. Terminix*, 697 NE 2d 277 at 280-81 (Ohio Com.Pl. 1998) (holding unconscionable an arbitration clause that would require claimant to pay a filing fee of $2,000 to pursue claim worth approximately $120,000); *In matter of Arbitration between Teleserve Systems, Inc. and MCI Telecommunications Corp.*, 659 N.Y. S. 2d 659, 660, 664 (N.Y. App. 1997) (finding a filing fee calculated on basis of one-half percent of the amount claimed patently excessive, oppressive, burdensome and a bar to arbitration and therefore unconscionable in contract between sophisticated telecommunications firms); and *Cole v. Burns Int'l Security Services.*, 105 F.3d 1465, 1484-85. (C.A.D.C. 1997) ("[I]f an employee like Cole is required to pay arbitrators' fees ranging from $500-$1,000 per day or more, . . . in addition to administrative and attorney's fees, is it likely that he will be able to pursue his statutory claims? We think not.").

In the complaint, plaintiffs rely on the Consumer Legal Remedies Act and the Vehicle Leasing Act, both consumer protection statutes enacted for a public purpose and providing certain unwaivable rights. A mandatory arbitration agreement cannot undercut unwaivable state's statutory rights by, for example, eliminating certain statutory remedies or by erecting excessive cost barriers. (*Id* at p. 95.)

B. <u>Based on the Status of the Law, Defendants Either Knew or Should Have Known that Their Costs Provision Was Unconscionable March 2000</u>

Based on the foregoing, defendants had every reason to know that in March 2000 the costs provision of their arbitration agreement was substantively unconscionable. The Court of Appeals confirmed that in the present case, "the administrative [filing] fee would be approximately $8,000." *Gutierrez*, 114 Cal.App.4th at 91. The trial court further found that Mr. and Mrs. Gutierrez would have to pay in excess of $10,000 to have only their individual claims heard by an AAA arbitrator. The filing fee for the same action in San Francisco Superior Court

at that time the complaint was filed was $206. In *Spence*, *supra*, the court found that a filing fee that was only 14 times greater than the court's filing fee was unconscionable. In the present case, the filing fee of over $8,000 is approximately 39 times greater the court's filing fee in March 2000. Thus, if a filing fee of 14 times the court's fee was unconscionable as far back as 1975, an arbitral fee of 39 times the court's filing fee in 2000.

Moreover, defendants need not have resorted to a mathematical formula to determine that the fees were unconscionable – common sense delivers the same result. An $8,000 filing fee is far beyond the means of any average consumer. By any rational standard it is unconscionable. The average car buyer would be shocked if they were told, at the time they were purchasing or leasing their vehicle, that their contract required them to pay an $8,000 filing fee to have any dispute with the dealer heard. Because the fees were so far beyond reason, defendants surely knew or should have known that the provision was unconscionable when plaintiffs signed their contract in March 2000, and this court finds the claim deterrent costs and fees to be imposed in bad faith.

III. The Party Seeking to Compel Arbitration Bears the Burden of Proving that the Costs Provision Was Drafted in Good Faith.

Defendant AUTO WEST maintains that the "burden" of proving that the subject arbitration agreement falls on plaintiffs. However, plaintiffs met their burden in the Court of Appeal when they proved that the arbitration provision was both procedurally and substantively unconscionable.[2] Having found that the arbitration costs provision was unconscionable, the burden then naturally shifts to the defendants to show why the remainder of the clause should still be enforced, notwithstanding the fact that it contains an unconscionable provision. In this case that requires the defendants to prove that the costs provision of the arbitration agreement was inserted into the contract in good faith.

That was the holding in *Data Management, Inc. v. Greene* (Alaska 1998) 757 P.2d 62, 64, the case relied upon by the California Supreme Court when *Armendariz* developed the "bad faith" argument against severance. *Amendariz, supra,* at p. 83, 124, fn. 13. In *Data Management*, which dealt with the analogous problem of whether or not to sever an unconscionable covenant-not-to-compete clause, the Alaska Supreme Court adopted the majority rule that "if an overbroad covenant not to compete can be reasonably altered to render it enforceable, then the court shall do so unless it determines the covenant was not drafted in good faith." *Data Management, supra*, 757 P.2d at 64. "**The burden of proving that the covenant was drafted in good faith is on the employer** [i.e. party seeking severance]." *Id.*

Moreover, it would be unfair to place the burden here on plaintiffs because the knowledge of why the unlawful costs provision was inserted into the contract is wholly within the knowledge of the drafting party. Accordingly, logic and fundamental fairness indicate that the burden should lay with the party or parties that have the relevant information wholly within their knowledge – especially when, as stated below, the drafting party asserts the attorney client privilege and refuses to provide its purpose or rationale in inserting the unlawful provision into the contract. As stated in the comments to Evidence Code § 520,

> [t]he burden of proof is sometimes allocated in a manner that is at variance with the general rule. In determining whether the normal allocation of the burden of proof should be altered, the courts consider a number of factors: the knowledge of the parties concerning the particular fact, the availability of the evidence to the parties, the most desirable result in terms of public policy in the absence of proof of the particular fact, and the probability of the existence or nonexistence of the fact. In determining the incidence of the burden of proof, 'the truth is that there is not and cannot be any one general solvent for all cases.'

Evidence Code § 520, Law Revision Commission Comment (citation omitted). Based on these factors established by the legislature the burden of proof should also fall on defendants in this case. The knowledge of why the provision was inserted in the contract, as well as the available

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[2] *Gutierrez*, 118 Cal.App.4th at 87.

relevant evidence, is wholly within the knowledge of the drafting party. However Wells Fargo has absolutely refused to divulge any information relating to their reasons for inserting the subject arbitration provision into its vehicle lease agreements, nor reveal what they knew about the applicable costs of arbitration in March 2000.

For example, plaintiffs' attempts in this case to obtain information concerning defendants decision to insert the unconscionable cost provision into their contract were met with nothing but objections from defendant Wells Fargo. Wells Fargo refused to answer questions on nineteen occasions during a one and a half hour deposition. (*See* Baird deposition.) Furthermore, WELLS FARGO BANK refused to produce witnesses for five of the seven persons most qualified categories plaintiffs requested. (*See* Baird deposition, Exh. 1, and 8:2-25; 9:1-17.) The categories in which WELLS FARGO refused to produce a "person most qualified" are:

1. Wells Fargo's decision to insert a mandatory arbitration agreement in its California vehicle lease agreements.

3. Wells Fargo's review of the relevant legal authority concerning the unconscionability of certain arbitration agreements prior to inserting a mandatory arbitration agreement in its California vehicle lease agreements.

5. Wells Fargo Bank's review of the legality of the arbitration agreement it inserted into its California vehicle lease agreements.

6. Wells Fargo Bank's review of the potential arbitration fees and costs associated with AAA arbitrations.

7. An evaluation regarding providing a provision in auto lease agreements for an effective avenue of relief from unaffordable fees.

Wells Fargo refused to produce the evidence to indicate that it drafted the provision in good faith. (*See* Baird deposition, Exh. 1.) Wells Fargo refused to answer questions whether or not (1) it reviewed case law before drafting the agreement (*see* Baird deposition, 21:13-18); (2) reviewed the AAA rules that were in effect at the time (*see* Baird deposition, 21:19-22); (3) considered the costs involved in arbitration with regard to consumers (*see* Baird deposition, 21:23-25; 22:1-12.);

(4) whether they considered putting in any provision in the lease agreement for an effective avenue of relief from unaffordable fees to consumers (*see* Baird deposition, 24:16-25; or (5) whether unaffordable fees would possibly prevent consumers from being able to protect their rights that they might have under the law (*see* Baird deposition, 10:21-25; 11:1-25; 12:1-7; 13:22-25; 14:1; 15:1).

In addition, WELLS FARGO refused to produce any documents regarding the following categories requested in the deposition notice (*see* Baird deposition 25:1-6):

1. Produce all DOCUMENTS concerning YOUR decision to insert the ARBITRATION AGREEMENT into your form California vehicle lease agreements.

2. Produce all prior drafts of the ARBITRATION AGREEMENT.

5. Produce all documents you reviewed regarding potential arbitration fees and costs associated with AAA arbitration prior to inserting the arbitration provision in California lease agreements.

6. All documents regarding your evaluation regarding providing a provision in auto lease agreements for an effective avenue of relief from unaffordable fees.

Nor was AUTO WEST any more helpful in explaining why an effective costs waiver was not inserted into the contract it presented to the plaintiffs in March 2000. In fact, according to the AUTO WEST person most knowledgeable, Chuck Noriega, he has no idea how much arbitration costs a consumer. (*See* Noriega deposition, 15:18-22.) He has never read the AAA rules regarding costs. (*See* Noriega deposition, 15:23-24; 16:1.) He is not aware of anybody at AUTO WEST DODGE who has read the AAA rules with regard to costs of consumers of going to arbitration. (*See* Noriega deposition, 16:2-8.) He's not aware of anybody at AUTO WEST DODGE at any time contacting WELLS FARGO BANK and discussing the issue of costs of arbitration. (*See* Noriega deposition, 16:9-14.) He is not aware of anybody at AUTO WEST DODGE making the suggestion to WELLS FARGO that it put in a provision in the arbitration

section to the effect that, if a consumer cannot afford to proceed through arbitration, AUTO WEST would pay the costs. (*See* Noriega deposition, 17:6-11; 18:1.) He is not aware of anyone ever suggesting that the arbitration provision provides some effective avenue of relief from unaffordable fees. (*See* Noriega deposition, 18:22-25; 19:1-3.) According to Noriega, there was no option to use a WELLS FARGO lease agreement without an arbitration agreement in March of 2000. (*See* Noriega deposition, 26:14-19.) He is not aware of anyone at AUTO WEST DODGE that ever considered putting in a provision in an auto lease agreement for an effective avenue of relief from unaffordable fees. (*See* Noriega deposition, 30:7-15.) The dealership is not allowed to change the back of the form from WELLS FARGO. (*See* Noriega deposition, 34: 21-24.) AUTO WEST had no idea how much arbitration costs a consumer (*see* Noriega deposition, 15:18-22), never even reviewed the contracts costs provisions (*see* Noriega deposition, 15:23-24; 16:1), never read the AAA rules regarding costs, was not aware of anyone at AUTO WEST DODGE at any time contacting WELLS FARGO BANK and discussing the issue of costs of arbitration (*see* Noriega deposition 16:9-14).

Accordingly, public policy supports a rule that the party asking the court to re-write its otherwise unconscionable arbitration clause explain why it believes an unconscionable clause inserted in its contract was done in good faith. Otherwise the moving party may simply refuse to produce any relevant information regarding the drafting of the unconscionable provision by relying on the attorney client privilege, thus making it difficult to impossible for the objecting party to locate any relevant information on the insertion of the offending clause into the contract and encouraging the drafters of such agreements to overreach.

Finally, as the moving party bearing the burden of proof, AUTO WEST has failed produce any evidence that either it or Wells Fargo decided to utilize the AAA arbitration clause with the unconscionable costs provision, and failed to explain why it could not and did not insert

a clause that offered to pay all arbitration fees that a consumer could not afford to pay. (*Cf. Parrish v. Cingular Wireless*, (2005) 129 Cal.App.4th 601, (upholding an arbitration clause where the moving party inserted a provision into the clause offering to pay all filing fees and arbitration costs). As such, AUTO WEST as the party seeking to compel arbitration of an unconscionable arbitration clause has failed to meet is burden, and the clause will not be enforced.

Defendant AUTO WEST's objection to the depositions of Chuck Noriega and Stewart Baird is overruled. Under the circumstances of this case, the Court finds it appropriate to attach the entire deposition transcripts. In reaching its decision, this court has only considered portions of the deposition transcript which are relevant to the issues before the Court.

IV. Disposition.

For the reasons set forth herein, and based upon all the pleadings and records filed in support of and in opposition to this matter, and based upon instruction from the Court of Appeal in *Gutierrez v. Auto West, Inc.*, 114 Cal.App.4th 77 (2003), and further based upon oral arguments of counsel, the Court declines to sever the unconscionable provision in the arbitration clause at issue in the case and hereby denies the petition. This matter is to be restored to the Civil Action calendar in the San Francisco Superior Court.

Dated: July 20, 2005

Hon. JAMES L. WARREN
Judge of the Superior Court

PROOF OF SERVICE

I, the undersigned, declare that I am over the age of 18 and am not a party to this action. I am employed in the City and County of San Francisco, California; my business address is Severson & Werson, One Embarcadero Center, Suite 2600, San Francisco, California 94111.

On the date below I served a copy, with all exhibits, of the following document(s):

NOTICE OF ENTRY OF ORDER

on all interested parties in said case addressed as follows:

Bryan Kemnitzer, Esq.
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& Ogilvie
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[X] **(BY MAIL)** I caused an envelope to be deposited in the mail at San Francisco, California, with postage thereon fully prepaid.

I am readily familiar with the firm's practice of collecting and processing correspondence for mailing. On the same day that correspondence is placed for collection and mailing, it is deposited in the ordinary course of business with the United States Postal Service in San Francisco, California in sealed envelopes with postage fully prepaid.

[ ] **(BY FAX)** By use of facsimile machine telephone number (415) 956-0439, I caused a true copy to be transmitted to the addressee(s) listed above at the facsimile number(s) noted after the party's address.

The facsimile machine I used complied with California Rules of Court, rule 2003 and no error was reported by the machine. Pursuant to California Rules of Court, rule 2006(d), I caused the machine to print a transmission record of the transmission, a copy of which is attached to this declaration.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. This declaration is executed in San Francisco, California, on August 1, 2005.

MARILYN LI