Avoiding Mandatory Arbitration in Products Liability Cases

By Leslie M. Kroeger, Theodore J. Leopold & Diana L. Martin

As consumer class action attorneys are painfully aware, in *AT&T Mobility LLC v. Concepcion*, 131 S.Ct. 1740 (2011), the United States Supreme Court determined that the federal government views arbitration with such favor that state courts are sometimes preempted from striking provisions of arbitration clauses that are unconscionable under state law. Since *Concepcion*, courts are understandably reluctant to deny motions to compel arbitration when parties to a dispute have entered into an agreement to arbitrate. But a California court recently decided in a couple of cases that arbitration agreements can be invoked by manufacturers of defective products that are not even signatories to the arbitration agreement. These cases indicate a trending defense strategy by manufacturers that plaintiffs' attorneys should consider when filing a products liability claim.

In the recent case of *In re Apple iPhone 3G Products Liability Litigation*, 859 Fed.Supp.2d 1084 (N.D. Cal. 2012), plaintiffs claimed their iPhone 3Gs failed to perform as promised due to Apple hardware or software flaws and that AT&T's 3G network could not accommodate the iPhone 3G users, resulting in users paying for 3G service that they were not receiving. They brought breach of warranty claims against Apple and AT&T. The plaintiffs had entered into terms of service agreements with AT&T that included an arbitration provision. Apple, as the product manufacturer, was not a party to the terms of service agreement, but moved to compel arbitration anyway. After applying the doctrine of equitable estoppel, the district court granted Apple's motion.

"A defendant that is a non-signatory to an agreement providing for arbitration may compel arbitration of claims by a plaintiff that is a signatory to such an agreement on the basis of equitable estoppel so long as two requirements are met: (1) the subject matter of the dispute must be 'intertwined with the contract providing for arbitration'; and (2) there must be a 'relationship among the parties of a nature that justifies a conclusion that the party which agreed to arbitrate with another entity should be estopped from denying an obligation to arbitrate a similar dispute with the adversary which is not a party to the arbitration agreement.'" *Id.* at 8 (quoting *In re Apple & AT & TM Antitrust Litig.*, 826 Fed.Supp.2d 1168 (N.D. Cal. 2011).) The court found both of these requirements satisfied. Despite plaintiffs' allegations that their iPhones suffered from hardware and software defects, the court determined the core allegation of the complaint was that AT&T's network could not accommodate the iPhone 3G users, resulting in them paying higher rates for a service that could not be delivered over AT&T's network. So plaintiffs' allegations were intertwined with their service agreements to use AT&T's 3G network because plaintiffs only had access to the network because they signed those service agreements granting them access. *Id.* And the relationship prong of the equitable estoppel test was satisfied by plaintiffs' allegations that Apple and AT&T entered into a fraudulent scheme in which they conspired to engage in racketeering activity. *Id.* at 9. The court determined that those allegations demonstrated the plaintiffs understood Apple and AT&T to have a relationship with each other that was sufficient to equitably estop plaintiffs from refusing to arbitrate with Apple as they had agreed to do with AT&T. *Id.*

The same conclusion was reached in *Lau v. Mercedes-Benz USA, LLC*, CV 11-1940 MEJ, 2012 WL 370557 (N.D. Cal. 1-31-2012). There, the plaintiff purchased a defective Mercedes from an authorized dealer. When purchasing the car, the plaintiff signed a retail installment sales contract with the dealer that contained an arbitration clause which allowed for arbitration of "[a]ny claim or dispute, whether in contract, tort, statute, or otherwise … between you and us … which arise out of or relate to your credit application, purchase or condition of this vehicle, this contract or any resulting transaction or relationship (including any such relationship with third parties who do not sign this contract) shall … be resolved by neutral, binding arbitration and not by a court action. …" *Id.* at 2. Plaintiff sued Mercedes for breach of warranty and Mercedes moved to compel arbitration under the plaintiff's sales contract with the dealer. The district court found Mercedes had standing to do so. *Id.* at 5.

Applying the same doctrine of equitable estoppel, the court first determined the plaintiff's breach of warranty claim was intertwined with the purchase agreement because the claim was founded on the plaintiff's purchase of the vehicle, which was accomplished by virtue of the purchase agreement. *Id.* at 4. Thus, without the agreement, the legal relationship between the manufacturer and the plaintiff necessary for the plaintiff to have standing to bring the warranty claim would not have existed. *Id.* The court next decided that the relationship prong of the equitable estoppel doctrine was satisfied by the agency relationship between the manufacturer and its authorized dealer. *Id.* at 5. It held, Mercedes "has standing as a non-signatory party to the purchase agreement to enforce the terms of the arbitration clause under the theories of equitable estoppel and principal-agency relationship." *Id.*

Nevertheless, and despite *Concepcion*, the district court held the arbitration clause was unconscionable and unenforceable. *Id.* at 11. The plaintiff was forced to take the entire purchase agreement on a take-it-or-leave-it basis without the opportunity to negotiate any terms, and was directed to sign only the front side of the form without ever seeing the arbitration clause on the back of the form. *Id.* at 8-9. This was sufficient for the court to find procedural unconscionability. *Id.* And the arbitration clause was procedurally unconscionable because the plaintiff would have to advance between $10,000 and $15,000 in order to bring his claim in arbitration, and would be required to lay out even more money to take an appeal of the arbitrator's decision. *Id.* at 9-10.

Of course, you can't rely on a Florida court striking down an arbitration clause in your products case, particularly after *Concepcion* put businesses on notice of the way an arbitration clause should look in order to pass muster, making it unlikely that clauses as one-sided as that in *Lau* will continue to be used. But, *Lau* and the *iPhone 3G Litigation* demonstrate another way to avoid being taken to arbitration by a non-signatory product manufacturer—careful pleading. In the iPhone litigation, the court found the plaintiffs' claims focused on both the problem with AT&T's network, as well as the iPhone defects, such that it was impossible to bring a claim just against Apple without necessarily implicating both AT&T and its service agreement. 2012 WL 1622643, 7. AT&T was an indispensable party in the case against Apple. *Id.* at 2. The fate of the plaintiffs in that case was dictated by the allegations made in the complaint. If the complaint had originally contained allegations focusing just on the product defects, rather than focusing on both the product defects and the network service problems, a different result likely would have been reached by the court with regard to both prongs of the equitable estoppel doctrine. The claims against Apple would not have been intertwined with AT&T's network problems, and there would have been no allegations of a fraudulent scheme by both defendants, giving rise to the necessary relationship between Apple and AT&T.

Pleading around the rule in *Lau* is more difficult. There, the plaintiff did not allege anything more than the mere purchase of the product that resulted in the court finding the first prong of the equitable estoppel doctrine was satisfied. 2012 WL 370557, 4-5. But the court focused on the fact that the plaintiff was bringing an express warranty claim, which he only had standing to do because he had entered into a sales agreement with the manufacturer's agent. Under Florida law, while a plaintiff is required to have privity of contract in order to bring a warranty claim, no privity is required to bring a strict liability action for damages caused by a product defect. See *Kramer v. Piper Aircraft Corp.*, 520 So. 2d 37, 39-40 (Fla. 1988) (holding privity of contract is required for breach of warranty action). So, at least in those cases where the product defect causes damages to person or property in addition to those suffered by the defective product itself, see *Indem. Ins. Co. of N. Am. v. Am. Aviation, Inc.*, 891 So.2d 532, 541 (Fla. 2004) (explaining products liability economic loss rule precludes tort liability for defective product that injures only itself), a plaintiff should be able to plead in tort, rather than contract, to avoid being equitably estopped from avoiding an arbitration request made by the product manufacturer. Furthermore, if the plaintiff's contract with the dealer specifically disclaims any warranties, then the agreement is unrelated to, rather than intertwined with, a claim for breach of warranty. *In re Toyota Motor Corp. Unintended Acceleration Mktg., Sales Practices, & Products Liab. Litig.*, 838 F. Supp. 2d 967, 992 (C.D. Cal. 2012). Causes of action for fraud and FDUTPA violations in the sale of a product are also unrelated to a product purchase agreement. *See Id.* at 993-94.

Although the attempt of manufacturers to compel arbitration in products liability cases is a new trend that has yet to gain prevalence, the risk is real. And the more legal authority there is supporting the ability of a manufacturer to compel arbitration under a contract to which the manufacturer is not even a party, the more likely manufacturers are to attempt this tactic. Plaintiffs' attorneys should, therefore, review the plaintiff's purchase agreement for the product and attempt to carefully plead around the scope of any arbitration clause and avoid allegations that can be interpreted as intertwining the subject of the contract with the allegations in the complaint or creating a relationship between the product dealer and manufacturer.

Leslie M. Kroeger

Ms. Kroeger is a shareholder at Leopold Law, P.A. is a successful civil trial attorney with a practice focused on complex civil litigation matters, including products liability, automotive crashworthiness, wrongful death and cases involving managed care abuse. As a dedicated advocate, Ms. Kroeger has been vocal in the Florida Legislature lobbying on behalf of consumers and promoting vehicle safety. She has achieved an AV rating from Martindale-Hubbell and was recently recognized as one of Florida's Legal Elite. She currently serves as a member of the Executive Committee of the Florida Justice Association.

Theodore J. Leopold

Mr. Leopold is a managing partner of Leopold Law, P.A. has a national practice specializing in consumer justice litigation with a focus on complex products liability, managed care, catastrophic injury, automotive crashworthiness, wrongful death and class action litigation. For many consecutive years, Mr. Leopold has been profiled in The Best Lawyers in America.

Diana L. Martin

Ms. Martin is an associate at Leopold Law, P.A., in Palm Beach Gardens, where she handles civil appeals in state and federal courts and provides litigation support. Ms. Martin is a 2002 high-honors graduate of the University of FloJrida Levin College of Law. Before entering private practice, she was a law clerk to the Honorable Martha Warner at the Fourth District Court of Appeal.