Drafter Beware: Exercise Caution When Choosing the Law

DIRECTV, Inc. v. Imburgia, 136 S.Ct. 463 (2015).

In 2008, two DIRECTV customers in California brought suit against the company seeking damages for early termination fees that they believed violated California law. Section 9 of the service agreements signed by the customers in 2007 required any disputes be resolved by arbitration. Section 9 also contained a class-arbitration waiver; however, it further stipulated that if the "law of your state" makes the waiver of class arbitration unenforceable, then the entire arbitration provision would be unenforceable. Finally, Section 10 of the agreement made clear that Section 9 "shall be governed by the Federal Arbitration Act."

In 2005, California law provided that the enforcement of class-arbitration waivers in "consumer contract[s] of adhesion" that "predictably involve small amounts of damages" and meet certain other criteria is "unconscionable under California law and should not be enforced." *Imburgia*, 136 S.Ct. at 466 (quoting *Discover Bank v. Sup. Ct.*, 113 P.3d 1100, 1110 (Cal. 2005)). Because neither party disputed that this rule — the "*Discover Bank* rule" — prohibited the class-arbitration waiver in the service agreements and thus invalidated DIRECTV's arbitration clauses with its California customers, the dispute proceeded to litigation.

During the pendency of this litigation in a California court, the United States Supreme Court held the *Discover Bank* rule "stands as an obstacle to the accomplishment and execution of the full purposes and objective of Congress" embodied in the Federal Arbitration Act (FAA). *AT&T Mobility, L.L.C. v. Concepcion*, 131 S.Ct. 1740, 1753 (2011). In other words, the Supreme Court determined that the FAA "pre-empts and invalidates th[e] rule." *Imburgia*, 136 S.Ct. at 466.

After the Court's decision in *Concepcion*, DIRECTV moved the California trial court for an order staying the litigation and compelling arbitration. DIRECTV's request was denied, an appeal ensued, and the California Court of Appeal affirmed. The court reasoned that "just as the parties were free in their contract to refer to the laws of different States or different nations, so too were they free to refer to California law as it would have been" without federal preemption. *Id.* at 467. In other words, the appellate court read the phrase "law of your state" as indicating that state law, without consideration for federal preemption, was to be applied, and, therefore, the parties had contractually agreed to the *Discover Bank* rule. This conclusion was premised on general construction principles of contract law.

In particular, the *Imburgia* court reasoned that Section 10 of the contract, stating that the FAA governed the

arbitration provision contained in Section 9, was a general provision, but the provision voiding arbitration if the "law of your state" would invalidate the class-arbitration waiver was a specific provision. Applying longstanding rules of contract interpretation, the court concluded that the specific invalidation provision must control over the general FAA enforcement provision within the DIRECTV agreement. The court further explained that the meaning of the phrase "law of your state" in this specific context was ambiguous and should, therefore, be construed against DIRECTV. The California Court of Appeal affirmed the lower court's order denying DIRECTV's request that the parties be compelled to arbitrate the dispute, and writs of certiorari were granted noting that the United States 9th Circuit Court of Appeals had reached the opposite conclusion on exactly the same question.

Overturning the California court's decision, the Supreme Court explained that the logical conclusion of the appellate court's holding would be to allow the "law of your state" phrase to apply invalid state law to the dispute. *Id.* at 469. Because the Court could find no other examples of a California court applying that meaning to the phrase "law of your state" in other contractual contexts, it concluded that the California court was interpreting the arbitration clause differently than it would other types of contracts. This method of analyzing an arbitration clause, the Court explained, is not allowed under established FAA jurisprudence. *Id.* Further, the Court noted that although the parties could have selected pre-*Concepcion* California law, there was nothing about use of the phrase "law of your state" that indicated that was their intent. *Id.*

Although the Supreme Court's decision in *Imburgia* dealt with a California law and a California state court's decision, its holding should be noted by practitioners in Louisiana and elsewhere. Practically speaking, attorneys drafting arbitration agreements who wish to take advantage of specific state laws favorable to their clients' interests may find those efforts frustrated if, later, federal courts conclude that state laws affecting the arbitrability of the claim are preempted by federal law. Although these state laws may still have independent force where wholly intrastate relationships are in play, and it may very well have been the parties' intent to disregard federal preemptive effects, arbitrators should be aware of *Imburgia*'s potential to undermine their decisions in later enforcement actions when a subsequent change in federal law occurs. Further, where federal law preempts state law in certain areas, drafters of arbitration agreements should be mindful of this fact and carefully draft clauses making absolutely clear which of the two laws is meant to apply.

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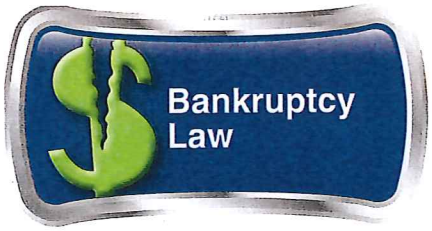

Alter Egos and Corporate Veils

Judgment Factors, L.L.C. v. Packer (In re Packer), 816 F.3d 87 (5 Cir. 2016).

Plaintiff/creditor filed an adversary proceeding against a Chapter 7 debtor objecting to his discharge based on 11 U.S.C. § 727. Plaintiff alleged that various entities owned by the debtor were his alter egos and requested the court reverse pierce their corporate veils. Plaintiff argued that the debtor should have listed these entities' assets in his schedules and those assets should be subject to plaintiff's claims.

On appeal, the 5th Circuit affirmed the lower court's ruling that since plaintiff failed to obtain leave from the trustee to pursue the claims of alter ego and piercing the corporate veil, which constitute property of the debtor's estate and are controlled by the trustee, plaintiff could not seek a judicial determination that any of the debtor's entities were his alter egos.

The 5th Circuit also held plaintiff failed to prove the debtor transferred property belonging to the debtor with the intent to hinder, delay or defraud under section 727(a)(2)(A). In support of its claim, plaintiff argued that the debtor's use of his 100 percent-owned company to pay his personal expenses was an attempt by the debtor to conceal assets. Plaintiff also argued that the debtor's company entered into four contracts worth more than $1 million right before and after the debtor filed for bankruptcy, which was also an attempt to conceal assets. The 5th Circuit found debtor was forthcoming with the trustee and answered all of her questions about his company (and its payment of his personal bills), the contracts of the company and his interactions with the company, and therefore affirmed the lower court's refusal to deny discharge under section 727(a)(2)(A) and (a)(4)(A), which provides for denial of a discharge if the debtor knowingly and fraudulently makes false statements.