Ninth Circuit applies strict notice requirement in rejecting arbitration in consumer suit

(January 12, 2015) - Suppose your company sells a subscription radio service. Your company partners with an automobile manufacturer to provide three months of free service to new car buyers in the hopes of generating interest in the service and, as a result, more subscriptions. By the nature of the arrangement, of course, your company cannot interface directly with the car buyers at the time of purchase because the cars are sold by a third party. But you wish to make clear to the buyer that the free three-month period is governed by contractual terms, including an agreement to arbitrate any dispute. How do you do it?

You might not want to settle for mailing them directly to the buyer — at least not in the Ninth Circuit. In *Knutson v. Sirius XM Radio*, 771 F.3d 559 (9th Cir. 2014), the Ninth Circuit rejected Sirius XM's efforts to enforce an arbitration provision in a customer agreement on the ground that the customer did not have sufficient notice of its terms despite the fact that Sirius XM had mailed those terms directly to the plaintiff.

The crux of the decision was that no one told Knutson at the time he bought his car that the three-month radio subscription was subject to contractual terms, and thus he had "no reason" to think he had any "contractual relationship with Sirius" or any reason to open the mail he received from it one month after buying his car. *Id.* at 566. Knutson did not deny receiving the mailing or even opening it; instead, he claimed not to have discovered the enclosed terms or have any reason to look for them based on the absence of any prior dealing with Sirius XM. *See id.* at 563. The court agreed that Sirius XM had provided insufficient notice of its terms to Knutson and thus allowed him to proceed to litigation on behalf of a putative nationwide class of consumers alleging that Sirius XM had violated the Telephone Consumer Protection Act by calling them in connection with the trial subscription. *See id.* at 564, 570.

In its analysis, the Ninth Circuit appeared to place some weight on *Windsor Mills v. Collins & Aikman Corp.*, 101 Cal. Rptr. 347 (Ct. App. 1972), a four-decade-old decision by one of California's intermediate appellate courts, which held that an offeree cannot be bound by "inconspicuous contractual provisions of which he was unaware, contained in a document whose contractual nature is not obvious." *Id.* at 351 (quoted in *Knutson*, 771 F.3d at 566). As the Ninth Circuit further noted in *Knutson*, the *Windsor Mills* rule "'applies with particular force to provisions for arbitration.'" *Knutson*, 771 F.3d at 566 (quoting *Windsor Mills*, 101 Cal. Rptr. at 351).

This logic is difficult to square with the Supreme Court's recent clarification in *AT&T Mobility v. Concepcion* that state-law contract principles cannot defeat an agreement to arbitrate to the extent they "derive their meaning from the fact that an agreement to arbitrate is at issue." 131 S. Ct. 1740, 1746 (2011). Indeed, both before and after *Concepcion*, other federal appellate courts have recognized that heightened notice requirements applied uniquely to arbitration provisions would be contrary to and displaced by the FAA. See *Awuah v. Coverall N.A., Inc.*, 703 F.3d 36, 45 (1st Cir. 2012) (rejecting argument that Massachusetts law requires additional notice of arbitration provisions and noting that any such rule would in any event be preempted under Concepcion and the FAA) (also citing *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 687 (1996), and *Morales v. Sun Constructors, Inc.*, 541 F.3d 218, 224 (3d Cir. 2008)).

The Ninth Circuit's decision likewise appears to pay little heed to the Supreme Court's recognition that, as a practical matter, "the times in which consumer contracts were anything other than adhesive are long past." *Id.* at 1750 (citing *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1149 (7th Cir. 1997)); see also *Hill*, 105 F.3d at 1149 (noting the impracticality in having cashiers "read legal documents to customers before ringing up sales"). The Ninth Circuit believed that it was imposing no significant obstacle to Sirius XM's desire to bind car buyers, explaining that the "*Toyota* purchase agreement could clearly state that Toyota has a relationship with Sirius XM" or that "*Toyota* could also provide its customers with literature" regarding the service and seeking the customer's assent to an agreement with Sirius XM. *Id.* at 568 (emphases added).

But these proposals would make the enforceability of Sirius XM's terms depend on individual transactions initiated by third-party dealerships with a principal interest in selling cars, not satellite radio subscriptions. The notion that these indirect dealings would provide better notice to potential customers than direct mailings is counterintuitive, to say the least. Moreover, the Ninth Circuit's approach could pave the way to a world in which the enforceability of the arbitration provisions would depend on the interactions between the third-party sales representatives and the buyer in each case, increasing litigation of the threshold issue of arbitrability and thereby significantly undermining a core purpose of the FAA to streamline the process of resolving disputes.

Given the somewhat fact-bound nature of the decision, it is difficult to predict how it will affect other cases. But there are a few important takeaways. First, the Ninth Circuit's embrace of state laws that expressly disfavor arbitration provisions — even after *Concepcion* — suggests a hostility toward consumer arbitration agreements that, though contrary to Supreme Court precedent, could have broad significance in future cases. Second, the Ninth Circuit's outlier pronouncement that the requirement of notice is heightened in cases involving arbitration clauses may set the stage for Supreme Court review in a future case given the expressly contrary view taken by other appellate courts. And third, manufacturers and sellers that distribute goods through or in cooperation with third parties — or indeed any manufacturer that sells products without direct interface with its customers — may wish to take extra steps to ensure that the customer is made aware that the transaction involves not only the third party but also the manufacturer or seller itself.

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