ORIGINAL

OFFICIAL TRANSCRIPT
PROCEEDINGS BEFORE

THE SUPREME COURT OF THE UNITED STATES

DKT/CASE NO. 82-500

TITLE SOUTHLAND CORPORATION, ET AL., Appellants v. RICHARD D. KEATING, ET AL.

PLACE Washington, D. C.

DATE October 4, 1983

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IN THE SUPREME COURT OF THE UNITED STATES

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SOUTHLAND CORPORATION, ET AL., :

Appellants :

v. : No. 82-500

RICHARD D. KEATING, ET AL. :

- -x

Washington, D.C.

Tuesday, October 4, 1983

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 1:05 p.m.

APPEARANCES:

MARK J. SPOONER, ESQ., Washington, D.C.; on behalf of the Appellants.

JOHN F. WELLS, ESQ., Oakland, Cal.; on behalf of the Appellees.

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C O N T E N T S

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P R O C E E D I N G S

CHIEF JUSTICE BURGER: Mr. Spooner.

ORAL ARGUMENT OF MARK J. SPOONER, ESQ.,

ON BEHALF OF APPELLANTS

MR. SPOONER: Mr. Chief Justice, and may it please the Court:

This case presents two important issues of interpretation under the Federal Arbitration Act. A preliminary question regarding the Court's jurisdiction to hear the case has also been raised, and I will address that point at the outset of my argument.

On the merits the two issues are first whether the states are free to enact statutory exceptions to the Federal Arbitration Act thereby striking down arbitration agreements that would otherwise be valid, irrevocable and enforceable under the specific terms of Section 2 of the federal statute. The second issue is whether the states are free to engraft their judicial class action procedures onto private arbitrations involving interstate commerce being conducted pursuant to the Federal Arbitration Act.

The issues in this case arose in the following way: The Plaintiff Appellees are former franchisees of 7-Eleven convenient stores in the State of California.

They alleged that their franchisor, the

Southland Corporation, violated the terms of the franchise agreement with respect to certain of its bookkeeping procedures and also that it did not fully disclose to them at the time they became franchisees the types of procedures that it would use in preparing financial statements for their stores. They claimed that Southland's actions and inactions constituted a breach of contract, a breach of a fiduciary duty, a common law fraud, and a violation of the state's franchise investment law which requires franchisors to make certain types of disclosures to their respective franchisees.

These cases were filed in court notwithstanding a broad forum arbitration clause in the franchise agreement, and the Plaintiffs have resisted arbitration. This effort has been successful so far because they have convinced the California Supreme Court that it is contrary to the public policy of the state's franchise invesment law to require franchisees to arbitrate claims that they base on that statute.

They have also convinced the California Supreme Court with respect to the clearly arbitrable claims, the common law, breach of contract and fraud claims, to remand the cases not to an arbitrator but back to the trial court so that the court can conduct

class certification proceedings and thereafter to supervise any arbitration which is held to be appropriate for class-wide adjudication.

We have brought this case here under Section 1257 of the judicial code. The Plaintiffs have argued that jurisdiction is lacking because the decision below allegedly does not constitute a final judgment.

They base this argument on the fact that the California Supreme Court contemplates that extensive judicial proceedings are yet to come in the trial court. I submit if it may please the Court that that is precisely the point that the parties agreed to arbitrate this case in a nonjudicial forum and that is where we ought to be.

The evil, if I may use that term, of the California Supreme Court's decision is precisely that it is compelling extensive judicial proceedings to occur in the trial court. Under the practical tests that this Court uses to determine finality we think that the decision is clearly final because it decides important issues under a federal statute in a definitive way. These issues are collateral to the merits of the case and in addition the decision is final in the sense that if this Court reverses the decision of the Court below the judicial proceedings clearly will be at an end.

QUESTION: The class arbitration issue was certainly not clearly raised below was it?

MR. SPOONER: Your Honor, it was raised below. We stated the issue in the California Supreme Court as follows: Whether a court may enter an order compelling the private commercial arbitration governed by the Federal Arbitration Act and the rules of the American Arbitration Association to proceed as a class action.

The Plaintiffs have argued strenuously in their brief in this Court that we did not litigate this issue as a federal question, but I submit that that claim is a red herring. What happened was that the parties all stipulated in the court below that this case involved interstate commerce and thus the federal Act applied.

Our argument was that arbitration and class actions were fundamentally incompatible with one another and, therefore, if you superimposed class action procedures which would necessarily involve extensive judicial involvement onto a private arbitration you would in essence be destroying the arbitration proceeding as the nonjudicial procedure it was itended to be.

We also --

QUESTION: Mr. Spooner, do you think that Congress intended the Federal Arbitration Act to govern procedings in state courts?

MR. SPOONER: It did not intend the Federal Arbitration Act to govern procedures in state court relating to arbitration. For example, --

QUESTION: Do you think it intended the Federal Arbitration Act to apply to state courts at all?

MR. SPOONER: Yes, in the sense that the state courts are required to enforce the Federal Arbitration Act just as the federal courts are. This Court in the Moses Cohen Hopsital case last term specifically held that.

QUESTION: Did it hold that? I thought Moses Cohen came from a federal ccurt.

MR. SPOONER: It did, Your Honor. It came from a federal court, but --

QUESTION: I thought a holding was something that was necessary to the disposition of a case.

MR. SPOONER: Well, Your Honor, I stand corrected. The Court did state several points in its opinion and I may -- It may not have been the holding of the decision, but the Court emphasized that the Federal Arbitration Act establishes a substantive right in favor

of arbitration and that this substantive right prevails over any state substantive or procedural policies to the contrary.

QUESTION: But it was dicta, was it not?

MR. SPOONER: I think that is correct, Your Honor.

Turning to the first of the issues presented here on the merits, the question is whether the states are free to enact statutory exceptance to the Federal Arbitration Act. We believe that the court was clearly incorrect in so holding.

The Federal Arbitration Act was specifically designed to overrule state policies and legislation which would do precisely what the California statute does in this case. Section 2 --

QUESTION: Well is the evidence of the congressional intent not somewhat indicative that it only intended it to imply in federal courts? The problem came I suppose with Erie v. Thompkins and all of that, but the evidence of what Congress intended is pretty clearly against you.

MR. SPOONER: Your Honor, I do not agree that the evidence is clearly against us. The procedural protections in many of the sections of the Federal Arbitration Act speak to what the United States courts

should do if proceedings relating to arbitration are brought in the United States courts.

However, Section 2 of the federal statute specifically says without limiting the protection of the statute to any particular courts that arbitration agreements involving maritime trade or interstate commerce shall be valid, irrevocable and enforceable save on such grounds as exist at law or in equity for the revocation of any contract. What Congress did in this section was to broadly declare that these contracts shall be upheld and they shall be enforced except on grounds that apply to any contract such as waiver or duress in a particular case.

But if a contract satisfies those general doctrines of contract formation, Section 2 of the Federal Arbitration Act says that that contract must be enforced. I think also that if Section 2 were read otherwise very unfortunate results would occur because the enforceability of an arbitration agreement in interstate commerce would depend on the forum in which enforcement was sought.

That would lead to forum shopping and would destroy the predictability in interstate commercial dealings that is so important. Section 2 does not say that arbitration agreements in interstate commerce shall

be enforceable unless the states provide otherwise, and we do not think it can logically be read in that fashion.

If it were, states could undermine the entire policy of the Act merely by creating a cause of action in which they say that you cannot arbitrate this claim. I think this case presents a pretty good example of precisely that problem.

The Plaintiffs' claim in this case is essentially a breach of contract and a fraud claim. They say that their franchisor mislead them and failed to disclose material facts.

The common law fraud claim is clearly arbitrable and the statutory claim is indistinguishable in terms of its elements, in terms of its basic nature from the common law claim. Yet what the Appellees are arguing in this case is that if the legislature of California chooses to say that you cannot arbitrate this kind of claim then what would otherwise be valid and enforceable under the federal statute ceases to become so.

The Plaintiffs' argument on this issue really boils down to stating that Congress has occasionally adopted exceptions to the Federal Arbitration Act when it has passed various types of federal legislation sc

why should the states not be free to do so. Well the answer to that is simply that the Supremacy Clause applies to the states and it does not control what Congress can do.

What Congress gives it can take away, but the states cannot take away what Congress has made valid and enforceable in a federal statute. There are obvious policy differences as well between exceptions to a protective federal statute like this where the exceptions are created by Congress and the states.

Congress when it is considering adopting an exception can carefully balance the different considerations and can keep the scope of the excepticns within very narrow limits, but when each of 50 individual states are permitted to adopt exceptions the scope of those exceptions will become virtually uncontrolled. The other important difference from a policy pcint of view is that any exceptions adopted by Congress will apply uniformly throughout the United States and parties that enter into arbitration agreements will be able to predict whether those agreements are going to be enforced or not with respect to particular kinds of claims.

But if each state can decide for itself when these agreements are going to be enforced and when they

are not that predictability would be lost. The Plaintiffs' position in this case or rather I should say the California legislation in this case as interpreted by the State Supreme Court reflects we think a basic mistrust for arbitration.

The underlying notion of their argument seems to be that arbitration is somehow going to be a vehicle that is going to allow the party with the superior resources to defeat small claims. I think that that basic premise is one that has to be challenged, that arbitration is beneficial for everybody but particularly beneficial when small claims and people with limited resources are involved.

The party with the superior resources can often litigate cases to death, can take full advantage of discovery rules, string out the case forever and frustrate small claims. But if a party is free to bring a case in arbitration he can get it tried promptly. He can devote the resources to it that it deserves, and he can prevent the liberal discovery rules and the backlog of the courts from frustrating getting a resolution of his claim.

QUESTION: Mr. Spooner, what if the California legislature had felt very strongly contrary perhaps perversely contrary to the way you are now speaking and

felt that arbitration was just simply a trap for the unwary and, therefore, it said that no contractual undertaking in this state providing for arbitration shall be enforced. Do you think that is just all down the well, so to speak, after the Federal Arbitration Act?

MR. SPOONER: Yes, we do, Your Honor.

QUESTION: What if Congress adopted a statute called the Federal Confession of Judgment Statute providing that there should be confessions of judgment permissible in all proceedings in federal or state courts and lots of states I guess have a policy against confessions of judgment because they regard them as pretty one-sided. No problem about enforcing that if Congress said so?

MR. SPOONER: Well, it is a question of whether that legislation would be within the proper scope of Congress' power to legislate in interstate commerce, and if it were a constitutional exercise of its power certainly it would overrule any contrary legislation enacted by the individual states.

With regard to the Federal Arbitration Act, I think that this Court held in the Prima Paint case that the statute clearly is a proper exercise of Congress' power to legislate in the area of interstate commerce.

If I may turn to the second issue which is presented here for review, the class action issue, what the Court held was that this case should go back to the trial court even with respect to claims that are clearly subject to arbitration, the nonfranchise investment law claims, so that the court could conduct class certification proceedings.

QUESTION: Mr. Spooner, may I interrupt you here? You started out to tell us a little bit about jurisdiction and the final judgment question, but I really did not understand your argument on why this portion of the judgment is final.

You are just starting out about all the proceedings that are going to take place on remand. I think maybe you ought to be sure you have covered everything you want to say on that.

MR. SPOONER: The decision on both issues is final, Justice Stevens, and with respect to this one in particular we think that it is final for two reasons. First of all, a specific California statute, Section 1294 of the California Code of Civil Procedure, specifically states that if a petition to compel arbitration is denied the party has to take its appeal immediately.

So Southland took its appeal at the juncture

in this case when it was compelled to do so as a matter of California law. Secondly, the Plaintiffs' argument is that a class has not been certified yet in this case and that Southland may be able to convince the trial court not to certify a class and, therefore, we do nct have a final judgment.

What this misses, I think, is that the issue here is more fundamental than that. Even if at the end of judicial class certification proceedings Southland were able to defeat the class, it would have been required to go through many months of very highly judicial proceedings which would be enmeshed with the underlying merits of the case.

This Court has stressed that class certification issues requrie a very careful inquiry into the nature of the claims that are involved in the case and the type of evidence that would be presented at a trial. Therefore, what inevitably happens in these cases is that the parties take detailed discovery to explore that issue.

They brief the issue extensively to the Court. The Court often holds an evidentiary hearing on the issue, and this Court has held that evidentiary hearings may be required in some instances. Then a decision is rendered.

Now even if at the end of this many months of proceedings Southland were able to defeat the class, we think that the decision of the California court here opens up a judicial procedure which is in direct contradiction of the policy of the Federal Arbitration Act which as this Court said in the Moses Cohen case is to move people out of court and into arbitration as quickly and easily as possible.

QUESTION: Is it not still true that the alternatives on remand are several really as I understand? One is that they may allow the arbitration to go forward under some kind of judicial supervision with sort of a semi-class action.

Another is there would be no arbitration at all. Another is there would be an old-fashioned class action.

I am not sure the issues are as clear cut as you seem to describe them. I do not know what is going to happen when this case goes back on this issue.

Is that not the very reason we tend to postpone review because we are trying to know exactly what we are called upon to decide?

MR. SPOONER: I do not think that the Court would be free to say that there will be no arbitration at all with respect to claims.

QUESTION: Well, as I understood it if you do not consent to a class-type arbitration then they could decline to arbitrate at all under the California Supreme Court's opinion or did I misread it?

MR. SPOONER: That is the implication of what they would do, but our position on the merits is that under the Federal Arbitration Act they do not have the power to do that. They do not have the power to do that because the federal statute creates a right of the parties to have their arbitration agreement enforced and it is not the province of the court to decide in a particular case that some other procedure would be more efficient.

Therefore --

QUESTION: It is not within the province of the trial court to construe the contract as authorizing some kind of a joint arbitration with three or four different franchisees?

MR. SPOONER: If the contract provided for a class-wide arbitration, then the issue would be could it do so without violating principles of due process of law. There is no issue here in that regard because the contract does not say anything about class action proceedings, and I think that the California Supreme Court rendered a decision which assumes that the

contract does not provide for such arbitration.

The thrust of its decision is that regardless of whether the parties agree to it or not this can be imposed on the parties.

Speaking very briefly about the merits of this class action issue, our position is simply that the two procedures, class actions and arbitrations, are fundamentally incompatible with one another. The whole idea of arbitration is to establish a procedure which is simple and quick and inexpensive and informal and most of all nonjudicial whereas class actions by their very nature as well as by due process considerations are necessarily very formalized in their procedures, very time consuming, very expensive and most of all highly regulated by the courts.

If a court did not actively supervise every stage of this proceeding and guarantee that the named represenative is adequately represented the class, if the court did not ensure that the evidence being presented in trial were truly common to all class members the results of that arbitration would not be binding on absent class members. So if a court tries to create a hybrid of the two procedures you would have to have a court looking over the arbitrator's shoulders every step of the way and ycu would be creating endless

opportunities for one part or the other to go running back to court asking a judge to second-guess what the arbitrator has done.

We think that this Court has to make a choice. You can either tell parties --

QUESTION: Mr. Schooner, why under California procedure would the California courts not be free to say the arbitrator can conduct a class proceeding as he wants to. We will only check it out when you bring an action to enforce the arbitration award so that you would not have any interim supervision of the arbitration at all.

MR. SPOONER: Your Honor, I think the reason for that is that you cannot -- A judge unless he is involved in a class action case and if he is just looking at it after the fact he is not in a position to know what kind of job the class represents.

QUESTION: That may make good sense as a matter of legal observation, but can you tell from the opinion of the Supreme Court of California that they adopted your proposition?

MR. SPOONER: The Court specifically said that in addition to the class certification proceedings the Court would have to exercise a measure of control over the arbitration itself in order to ensure that the

interests of the class were being adequately represented as well as to approve any settlements or dismissals.

They did not define what that measure of supervision and control would be, but our position is that it would necessarily be quite extensive and regardless of whether it was extensive or not it would be inconsistent with the idea that arbitration is supposed to be a procedure apart from the court systems taking place outside of that forum.

QUESTION: Mr. Spooner, may I ask another question? It really again relates a little bit to the finality, but do we know that on remand if the issues are a little more clearly defined than they seem to be now, say, for example, that you get an arbitration of whether there was adequate disclosure and presumably you have got some form documents you give every franchisee. Do we know it will be contrary to your client's interest to have a single arbitration resolving that issue for everybody who says you did not make an adequate disclosure?

That seems to me it is not perfectly clear that you would oppose the class.

MR. SPOONER: That we would oppose it?

QUESTION: Yes

MR. SPOONER: The client would oppose it, Your

Honor, because one of the primary attributes of arbitration is that when somebody raises a claim you can litigate it simply and informally. If we had a class-wise arbitration proceeding you would have two things that would change the ballgame altogether.

First of all, we think that the procedures and the complexities of such a procedure would be such that the case would become more complicated than if it has remained in court all along. Secondly, there would be severe questions about whether if Southland won in such a procedure the results would be binding on absent class members.

Third, one of the attributes --

QUESTION: Well, they clearly will not be binding if you do not have a class-wide arbitration. You are foreclosing the opportunity to get a class-wide binding adjudication by resisting the class action.

MR. SPOONER: What I am saying is we would not -- I interpreted your question to say would we think it was a good idea to have such a procedure and --

QUESTION: You say, for example, one of the issues is whether the disclosure is adequate. If you give them some form book that says how you are going to do your accounting or something I presume you give everybody the same book, and the arbitratory will look

it over and say it either is or is not an adequate disclosure and that would end it. Maybe I oversimplify the thing.

MR. SPOONER: It is not as simple as that because when a franchise is sold the disclosure document is only the first step. You sit down with every person and you explain it to them.

You have face-to-face meetings. They have the opportunity to talk to other franchisees. You cannot --

QUESTION: To the extent that it depends on oral negotiations obviously you could not have a class-wide arbitration.

MR. SPOONER: We sould certainly resist the notion of a class-wide arbitration both on the traditional grounds on which class actions are opposed plus on the broader grounds that I have outlined.

I would like to reserve the remainder of my time for rebuttal if I may.

CHIEF JUSTICE BURGER: Mr. Wells.

ORAL ARGUMENT OF JOHN F. WELL, ESQ.,

ON BEHALF OF APPELLEES

MR. WELLS: Mr. Chief Justice, and may it please the Court:

I would like to begin discussing the problem that Mr. Schooner discussed first, namely, the question

raised by the claim that the Federal Arbitration Act preempts any claims litigated under the franchise, that is, preempts the anti-waiver clause in the California franchise investment law. But before addressing the question of preemption there is a preliminary issue that needs to be resolved and needs to be addressed by this Court, and that is whether the arbitration clause in question in fact and in law is broad enough to include the claims under the California franchise invesment law.

The preliminary question was decided in the trial court in this case against arbitration. He concluded that the clause in question was not intended to and did not reach claims under the statute.

The District Court of Appeals disagreed with him, and reversed that part of his decision. That decision was set aside by the Supreme Court's grant of a hearing so that decision was vacated.

The California Supreme Court expressly declined to discuss that issue because it passed straight to the preemption issue and held that the franchise investment law claims are not arbitrable under the anti-waiver clause in the franchise investment law, a clause copied from the Federal Securities. It interpreted that clause in the same way that this Court

did in Wilko v. Swan and concluded that the California legislature intended to provide a special judicial forum for claims under that Act just as in the securities law and then went on to conlude that the Federal Arbitration Act was not inconsistent therewith because Congress had announced or enacted similar policies to the franchise investment law in securities cases and others.

QUESTION: Do you think that interferes with the rights of individual parties to pick their own forum by contract?

MR. WELLS: To the extent only that the California Supreme Court -- Excuse me. The California legislation as interpreted by the California Supreme Court has decided that a certain class of citizens need protection from their own waiver for arbitration agreement because the statute provides that parties may not waive their rights under this statute. To that extent, yes, parties are foreclosed from entering into binding arbitration agreements as they might relate to claims under the franchise investment law.

QUESTION: In a case strictly in the federal courts, Berman v. Zepotowich neither of you cite, this Court discussed that subject and came to the conclusion that parties dealing at arms length could make binding contracts for arbitration.

MR. WELLS: That is right, of course. That is, of course, the thrust of the Federal Arbitration Act. It is the thurst of the California Arbitration Act, and I think most states have similar statutes which overrule the old common law rule that agreements to arbitrate are not enforceable because they house the courts of jurisdiction.

There is no question but what the policy of the federal government as exemplified in the Federal Arbitration Act and the policy of the government of the State of California as exemplified by its arbitration statute is that generally speaking agreements to arbitrate future disputes are valid and enforceable except on grounds that might invalidate contracts generally.

Congress and the state legislature in fact the legislatures I am told by the amicus briefs some 38 states have enacted legislation in the securities field which the franchise investment law is very analogous to which incude that same provison that persons who bring claims under these remedial statutes are not obliged to arbitrate those claims. They are guaranteed their day in court, a judicial forum.

That is the policy of the Congress, and that is the policy of the state legislatures. More than that

the Congress has specifically encouraged the states to pass parallel and concurrent securities regulations statutes.

The Securities Act specifically provides for concurrent jurisdiction on issues of securities violations by the state and the federal government. Of coruse, the extent that Congress and the Securities Exchange Commission have occupied the field, any legislation to the contrary by a state would be invalid.

But these state statutes are essentially the same as the federal statutes in purpose and in effect, and quite apart from encouraging forum shopping the conclusion if the Supreme Court of California's decision is upheld, the decision that Southland is asking for is the one that would encourage forum shopping because as I understand their position it is that while Congress may have a policy and may include anti-waiver provisions in its securities statute in order to protect the person who is in the weaker bargaining position and ensure him his day in court, the state legislatures who are encouraged to pass these concurrent and overlapping securities statutes are not entitled to pursue that same policy.

That would result in the same claim that came

into the federal court being not arbitrable but if it was brought in the state court under the state securities law it would be required to be arbitrated. Back to the question of the preliminary inquiry which I think this Court must address before it reaches, shall we say, the merits of the preemption claim.

The clause in question -- The Supreme Court of California specifically declined to rule on that issue, but it is an issue that was in the case. It was always contended by us that this clause does not include claims under the franchise investment law for this reason, and I think it is a very valid reason.

The arbitrator has only the power that is given him by the arbitration agreement. He is not a court. He can only do what the parties have agreed that he may do, and in this case although the preamble section or the introductory section of this clause says that he may arbitrate all issues which arise out of or relate to the agreement while you might say that is broad enough to embrace claims under the franchise investment law because they have a relationship to the agreement it goes on and gives him the authority only to award damages for breach of the agreement.

There is nothing in the arbitration agreement which gives him any authority to award damages for

misrepresentations leading up to the agreement that are required by the franchise investment law, and that is a respect in which this arbitrator could not enforce the provisions of the franchise investment law.

QUESTION: You say the superior court found to that effect?

MR. WELLS: That is right. The superior court, the judge in superior court said, "I find that this clause is not broad enough to include claims under the franchise investment law."

He said, "I also think that if it did those claims would not be arbitrable for the reasons that were later adopted by the Supreme Court." But he clearly indicated as one of his grounds for that ruling that he thought the agreement would not reach claims under the franchise investment law.

Furthermore, another clause in another part of the arbitration clause provides that nothing herein shall authorize the arbitrator to vary or modify or supplement any of the terms of this contract. Now that flies in the face of the remedies under the franchise investment law one of which is that if the disclosure statement is misleading or false, the required disclosure statement, the prefranchise disclosure statement, the court may rescind. One of the remedies

is rescision of the franchise agreement.

That is a remedy that the arbitrator would not be able to enforce. So the result would be that the Plaintiffs here would be giving up more than and they would be waiving more than their right to a judicial forum. They would be waiving substantive claims, rights that have been given them by the legislature under this statute.

That, of course, is one of the reasons that the federal courts including this Court have decided in a line of cases that there are certain types of claims, remedial statutes which were intended to protect persons in a weaker bargaining position such as the securities laws that those claims are not required to be artibrated by the Federal Arbitration Act. One of the reasons for that is that arbitrators are peculiarly not well suited.

Arbitration is not a good place to enforce important rights set forward in a statute that is complicated. It parts from the common law. It gives the parties benefits that they would not have at common law. It provides certain --

QUESTION: I have great problem with your constant argument about you cannot waive rights. I do not know of any rights you cannot waive.

MR. WELLS: Well, I think you --

QUESTION: You can waive federally protected constitutional rights. You can waive a right to trial by jury.

MR. WELLS: Well, I know that the --

QUESTION: I can understand the arbitral statements can do it, but I think you are saying that they just cannot waive them at all.

MR. WELLS: According to the provision in the Corporate Securities Act of the State of California as interpreted by the California Supreme Court, one may not waive the right to a judicial forum as a place tc make a claim under that statute. That same clause was so interpreted by this Court in Wilko v. Swan when that clause was found in the Securities Act of 1933.

I thought that there was no issue left as to whether that was not an appropriate decision that parties may not waive by means of an arbitration agreement executed prior to the event prior to the dispute arising the right tc a judicial forum.

There is -- Leaving the matter of the preliminary inquiry as to the interpretation of the arbitration clause and turning for a moment to the question assuming for the sake of argument which we may do that the arbitration clause did not reach these

claims under the franchise investment law, now the question becomes in light of the California Supreme Court's decision that such claims are not arbitrable is that somehow preempted by the Federal Arbitration Act? That is a question really of whether there is a conflict between the federal law and policy and the state law and policy.

Our position on that is that there is no such conflict. Each has the same proarbitration policy as represented by the Federal Arbitration Act.

The state courts are every bit as zealous in protecting, that is the California courts at least, are every bit as zealous in protecting the rights to arbitrate under a pre-dispute arbitration agreements as are the federal courts. The behavior of the courts in this case is a good example of that because we attacked the arbitration agreement when it was asserted as a basis for preventing or going forward with a class action on grounds that Southland had waived their rights under the statute and on evidence which was very strong in some of these cases of waiver because Southland had gone ahead and litigated the case in the courts and taken depositions for weeks and months in certain of the cases. The California courts nevertheless held in this case that there was no waiver of the right to

arbitrate.

When presented with the adhesion contract argument in this case, the California court leaned over backwards to protect the rights of the parties to arbitrate. Although finding that this arbitration clause was in an adhesion contract, the California Supreme Court nevertheless refused to say that it was invalid and unenforceable unless perhaps it would be so if it had the effect of defeating the effect, the right to a class remedy.

By the same token both jurisdictions, the federal courts and the state courts, have the same policy the same set of laws in the field of securities regulation, franchise regulation and others that recognize that in certain situations where you are dealing with important statutory rights whether it be under the securities laws, anti-trust laws, Fair Labor Standards Act, bankruptcy laws notwithstanding the strong policy in favor of arbitration these are claims that are not suited to arbitration. Arbitration is not appropriate, and it is not the federal policy under the Federal Arbitration Act to require arbitration in those cases.

So there is no conflict really between the policy of the federal government and the policy of the

state government, and nothing about the decision of the California Supreme Court here is in any way inconsistent with or in conflict with the policy of the federal government. If this case had come up under the Federal Securities Act rather than the California franchise investment law, that very same anti-waiver clause would have been upheld by this Court under the doctrine of Wilko v. Swan.

There is no reason --

QUESTION: Mr. Well, can I ask you a question? I must confess I am not sure I thoroughly understand this argument. I know it runs through the California Supreme Court opinion.

Would it really be a different case if California said we really do not like arbitrations at all but we understand we have a duty to honor contracts under the federal statute but we do not have to honor this one because of our own franchise invesment law? Would that make the issue any different?

You seem to rely heavily on the fact that California generally has a policy similar to the federal policy.

MR. WELLS: Yes, I do.

QUESTION: Would it matter if they had a policy hostile to the federal policy?

MR. WELLS: If they had a statute that reenacted the common law, if they repealed the California Arbitration Act and said --

QUESTION: Supposing they had a statute that said we do not want to arbitrate anything more than the federal government requires us to, and we do not think they require us in all events to arbitrate this particular class of claims.

MR. WELLS: That would be the same case we have here I think.

QUESTION: Then I do not see the force of their argument that their general policy is very similar to the federal policy.

MR. WELLS: Maybe I did not understand the question, Justice Stevens. I thought you said if the California statute said we will enforce those arbitration agreements the Federal Arbitration Act requires us to enforce.

QUESTION: Right, and no more because we really do not like arbitration.

MR. WELLS: I do not think that the California courts' policy with respect to arbitrating disputes that are not in Congress would have anything to do with the case so long as the claim before the court at that time was a claim under the franchise investment law which is

directly analogous to, in fact it derives from the federal policy in the securities regulation field because they copied the anti-waiver clause right from that --

QUESTION: Well, let me put a similar question a different way. Supposing they had ruled that contracts of adhesion are something we do not like in California, therefore, we will never enforce an arbitration clause in a contract of adhesion. I think have argued something close to that.

MR. WELLS: That is right.

QUESTION: Could they have accepted that argument consistently with the Federal Arbitration Act?

MR. WELLS: Yes, I think they could because the Federal Arbitration Act says that all agreements to arbitrate shall be valid, irrevocable and enforceable save on grounds for the revccation of contracts generally at law or in equity. To us as we understand that it means that if the ground for refusing to enforce the arbitration agreement is a ground applicable to contracts generally and as a part of a general contract law then the Federal Arbitration Act does not reach that.

It does not require that agreement to be enforced. So there are various situations under general

contract law, and I think the law of the State of California would apply to that. There is a whole area here where if the Federal Arbitration Act is going to be given the effect of federal law, substantive law but recognizing that it includes many procedural aspects as does the state statute then there is going to be a question do we apply the federal law to this particular issue that goes to the arbitrability of the contract or do we apply the state law.

Those are very nice questions. I think it is sufficient for this case to observe that the effect of these federal decisions exempting certain types of claims from the operation of the arbitration statute is to define the scope of the Federal Arbitration Act.

The scope of that Act is to reach out and require arbitration when people have agreed to arbitrate most of the time but not always. There is a certain class of cases where it does not apply.

Those cases have been described by this Court and the other federal courts from time to time. They are the bankruptcy cases and the anti-trust cases and the securities regulation cases and the Fair Labor Standards Act cases.

Those are a class of cases that the Federal Arbitration Act does not apply to, and in our view the

only rational interpretation of the Federal Arbitration Act when applied to state law claims is that if they are in that same category of claims if they are directly analogous to those claims that the Federal Arbitration Act does not reach on the federal side the Federal Arbitration Act should not then reach them on the state side.

That is buttressed. It seems to me it becomes a kind of a fortiori case where you are dealing with the very sensitive duality federal state problem here because here you have a state legislature in the exercise of its police power enacting a remedial statute for the benefit of its citizens which will apply to some extent in cases in interstate commerce. That will be necessarily the case becasue everything has some effect on interstate commerce and in the course of doing so adopt a policy which is identical to that of the Congress.

In the area of selecting the forum for the adjudication of state created rights as this Court has recognized in the recent case of Northern Pipeline against Marathon the power of Congress is very minimal. It seems to us that if anything the Federal Arbitration Act would reach not as far and would stop short. We are dealing with state legislatures who have declared in

this particular situation our citizens are entitled to a judicial forum where that was true on the federal side.

But in any case we have a case that is exactly analogous to Wildo v. Swan and these other federal cases.

Finally, there is the matter if I may now turn to the other side of the case, that is, the set of issues that come here under the common law claims assuming now for the sake of argument again that some claims are going to be arbitrated in this case whether they be claims under the federal franchise investment law or the common law claims.

Now the question that Southland raises is since the arbitration agreement in question is covered by the Federal Arbitration Act is this notion of the California Supreme Court that there can be a class-wide arbitration something that is so contrary to the very nature of an arbitration as a method for dispute resolution that it must violate the Supremacy Clause of the United States Constitution since the Federal Arbitration Act would preempt any state policy to the contrary.

Now on that issue I have several things to say about that, but the most important thing is that issue does not belong here. I do not believe that it raises

any significant federal question.

It was an issue that was never raised. The preemption argument on the issue of class-wide arbitration was never raised by Southland in the trial court or in the Supreme Court of the State of California.

To be sure it was recognized by both sides that the Federal Arbitration Act, at least the substantive provisions thereof, would cover the question of arbitrability, that is, that it applied to this contract since it affected commerce. Our position was then and it is now and has always been that it really does not make any difference on the substantive side whether the Federal Arbitration Act or the state Arbitration Act applied because we find no difference between them.

We have found no case or statement of policy interpreting the California Arbitration Act that is any different from the statements and interpretations of this or the other federal courts in interpreting the Federal Arbitration Act. It is very clear that state courts apply their own procedures in enforcing the Arbitration Act.

That was done in this case. You look to the California Court of Civil Procedure to determine how to

go about filing a motion to compel arbitration or to obtain a judgment on the basis of an arbitration award.

There are various things in both of these statutes that are appropriate in the procedures of that court. Here in the state court you do not apply the Rules of Federal Procedure nor if you are in the federal court vica versa.

But the question of -- So the only extent to which Southland ever referred to or treated this as a federal question in the California courts was to recognize that the Federal Arbitration Act, and they claimed that on the issue of whether or not you could have a class arbitration they represented to the California courts that that was a question to be decided under state law and that since there was no authority for it in the California Code of Civil Procedure that it should not be done.

We responded to the same question by the District Court of Appeals as to which law applied by saying that it did not matter. We could find no difference between the two. We assumed that California law would apply and argued by analogy that the Fderal Rules of Civil Procedure would provide some guidance to the California courts in developing a class remedy just as the California courts have looked to Rule 23 of idd

Federal Rules in developing the class remedy generally in court actions.

So first and foremost it was never raised. It is not discussed. The issue of preemption, the contention that the Federal Arbitration Act preempts this and prevents the Supreme Cout of the State of California from remanding this case to the trial court to consider the desirability of a hybrid kind of class arbitration was never raised as a federal issue as a constitutional questiod below

But even if it were not only is there no final judgment there is not any judgment of any kind except the remand to the trial court to consider the alternative ways to deal with the fact that we have conflicting policies that the California courts reccgnize as important, the importance of preserving the parties' rights to arbitration if they have agreed to arbitrate and the importance of providing a class remedy for persons in the position of these franchisees when dealing with their franchisor, a large corporation like Southland.

It is a kind of situation that is perfect for the class remedy. If there can be no class remedy then one of two things will happen.

Either there will be a large number of

individual arbitrations or as Southland hopes there will be a handful of arbitrations because other people do not know they have a claim. But the class remedy -- The California Supreme Court said in that situation if the effect of the arbitration clause is going to be to defeat the class remedy then perhaps the arbitration clause under general principles of contract law as we understand them should be declared invalid because of the principles applicable to adhesion contracts.

So it sent the entire thing back to the trial court who had not considered any of these issues to decide among the alternatives. Shall there be consolidation of arbitrations which is clearly recognized by the federal rules and the California ccurt says would also be available under the California Code of Civil Procedure?

Should there be a single arbitration or some class arbitration under court supervision? That is a possibility.

Possibly the arbitration clause should be stricken or it should be voided because of the principles applicable to adhesion contracts. A hearing will have to be held.

Evidence will have to be taken. A trial judge will have to consider what to do. In that posture it

seems to me that it would not be wise for this Court to try to deal with the constitutional claim that somehow objectives or policies under the Federal Arbitration Act have been interfered with and the preemption doctrine should apply.

Unless there are further questions, that will conclude my presentation.

CHIEF JUSTICE BURGER: Do you have anything further, Mr. Spooner?

You have two minutes remaining.

ORAL ARGUMENT OF MARK J. SPOONER, ESQ.,

ON BEHALF OF APPELLANTS

QUESTION: Mr. Spooner, before you begin supposing that Southland in this case instead of dealing with franchisees had been dealing with new employees and had handed to each one when they came to work an agreement to arbitrate any claim of injury arising out of or in the course of their employment and then one of them sustained an injury and went to the Industrial Accident Commission in California and Southland pleaded you have to arbitrate this and the California court said no we just do not allow anything except Industrial Accident Commission proceedings for industrial injury. Do you think the Federal Arbitration Act would require arbitration to prevail there?

MR. SPOONER: Well, the first question would be whether that employment agreement involved interstate commerce. If it did not then the Federal Arbitration Act --

QUESTION: I would assume that it would apply.

MR. SPOONER: The second question would be whether a provision in Section 1 of the Federal Arbitration Act would exempt this class of case from the scope of the federal statute. Section 1 provides that it shall not be applicable to the contracts of workers engaged in seamen's contracts and other interstate transactions.

The scope of that exemption for workers claims has never been construed by this Court. It might be construed not to apply to that situation.

QUESTION: Well, assume that was not exempt.

MR. SPOONER: If it was not exempt and if the contract satisfied the general doctrines of contract formation, it was not forced upon them by undue means then our position would be that the federal Act controls and the agreement should be enforced.

The Plaintiffs argue here that there are federal situations in which certain types of claims have been held not to be appropriate for arbitration and they try to suggest that there is some sort of a broad

exemption for statutory claims. That simply is not the case.

This Court has held in only a very few situations that particular federal claims are not suited for arbitration, and it has done that only after carefully analyzing congressional intent in the particular statute involved.

Thank you, Your Honor.

CHIEF JUSTICE BURGER: Thank you, gentlemen.

The case is submitted.

(Whereupon, at 2:05 p.m., the case in the above-entitled matter was submitted.)

CERTIFICATION

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SOUTHLAND CORPORATION, ET AL., Appellants v. RICHARD D. KEATING, ET AL. # 82-500

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BY Diane Hammond

(REPORTER)