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SUPREME COURT
STATE OF WASHINGTON

2006 JUL 24 P 1:01 No. 77406-4

BY C. J. MERRITT

~~SUPREME COURT OF THE STATE OF WASHINGTON
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**DOUG SCOTT, LOREN TABASINKE, SANDRA TABASINSKE,
PATRICK OISHI, JANET OISHI, et al.,**

Petitioners,

v.

CINGULAR WIRELESS,

Respondent.

PETITIONERS' STATEMENT OF ADDITIONAL AUTHORITIES

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STATEMENT OF ADDITIONAL AUTHORITIES

Pursuant to RAP 10.8, Petitioners submit this statement of additional authorities to provide the Court with two recent decisions.

In *Schwartz v. Alltel Corp.*, No. 86810 (Ohio Ct. App. June 29, 2006), the Ohio Court of Appeals held that the arbitration clause in Alltel's wireless contract, which prohibits class treatment or consolidation of claims, is unconscionable under Ohio law. The *Schwartz* court first held that the arbitration clause is substantively unconscionable. Slip Op. at 10–12. The court noted that, “[b]y eliminating a consumer’s right to proceed through a class action, the arbitration clause directly hinders the consumer protection purposes of the [Ohio Consumer Sales Protection Act].” Slip. Op at 10. The court further noted that, “[b]y prohibiting its customers from filing suit as a class, Alltel prevents the cost effective use of class action litigation that can end abusive practices by large corporations in those instances in which individual claims are ineffective.” Slip Op. at 11. That holding is relevant to Petitioners’ argument that the class action ban in Cingular’s consumer contract is unconscionable under Washington law because it would effectively serve as an exculpatory clause. Appellants’ Opening Br. (Ct. App.) at 19–29; Appellants’ Reply Brief on the Merits (Ct. App.) at 6–8; Mot. for Disc. Rev. at 6–10.

Second, the *Schwartz* court held that Alltel's arbitration clause, because it was drafted by the stronger party and contained small, hard-to-read print, is procedurally unconscionable. Slip Op. at 12–13. That holding is relevant to Petitioners' argument that Cingular's arbitration clause is procedurally unconscionable. Opening Br. at 43–50; Mot. for Disc. Rev. at 11–13.

In *Wong v. T-Mobile U.S.A.*, No. 05-73922 (E.D. Mich. July 20, 2006), the U.S. District Court for the Eastern District of Michigan held that T-Mobile's arbitration clause, which contained an unseverable class action ban, was unenforceable because class actions are necessary for the vindication of consumers' rights under the state consumer protection statute. Slip Op. at 3–8. The court noted: "Defendant makes much of the fact that it contributes toward plaintiffs' arbitration costs, but in order for arbitration to be feasible, the amount at issue must also exceed the value in time and energy required to arbitrate a claim. Defendant is alleged to have bilked its customers out of millions of dollars, though only a few dollars at a time. Plaintiff's damages are a paltry \$19.74, hardly enough to make arbitration worthwhile. Class actions were designed for situations like this." Slip Op. at 8. That holding is relevant to Petitioners' argument that the class action ban in Cingular's consumer contract would effectively serve as an exculpatory clause, and thus is unconscionable. Appellants'

Opening Br. (Ct. App.) at 19–29; Appellants’ Reply Brief on the Merits
(Ct. App.) at 6–8; Mot. for Disc. Rev. at 6–10.

Respectfully submitted this ____ July, 2006.

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[Cite as *Schwartz v. Alltel Corp.*, 2006-Ohio-3353.]

COURT OF APPEALS OF OHIO, EIGHTH DISTRICT
COUNTY OF CUYAHOGA
No. 86810

EDWARD SCHWARTZ, :
 :
 Plaintiff-Appellee : JOURNAL ENTRY
 :
 vs. : AND
 :
 ALLTEL CORPORATION, : OPINION
 :
 Defendant-Appellant :
 :
 :
 DATE OF ANNOUNCEMENT JUNE 29, 2006
 OF DECISION :
 :
 :
 CHARACTER OF PROCEEDING : Civil appeal from
 : Common Pleas Court
 : Case No. CV-453730
 :
 JUDGMENT : AFFIRMED
 :
 DATE OF JOURNALIZATION :

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MARY EILEEN KILBANE, J.:

{¶ 1} Alltel Corporation ("Alltel") appeals the decision of the trial court denying its motion to stay litigation pending arbitration. Alltel argues the trial court erred in finding that the parties did not enter into an agreement to arbitrate, that the agreement was procedurally and substantively unconscionable, that any offending provisions should have been severed and that federal law governed the arbitration provision. For the following reasons, we affirm the decision of the trial court.

{¶ 2} On August 24, 2000, Edward Schwartz ("Schwartz") read an Alltel advertisement in his *Cleveland Plain Dealer*. Alltel advertised cellular phone service for "Unlimited Anytime Minutes only \$49.99 for life." Alltel's advertisement did not limit the service plan's duration but informed readers that additional

roaming charges may apply.

{¶ 3} In September 2000, Schwartz visited his local Alltel store to inquire about the advertised service plan. Alltel employees presented Schwartz with Alltel's standard form contract, which Alltel had prepared in advance. Schwartz signed up for an Alltel plan for the contracted rate of \$49.95 per month with a roaming fee of \$.59 per minute. However, in the Notes/Special Situation section of the contract was the following handwritten passage:

"\$49.95 unlimited local air time for life as long as customer remains on rate plan with Alltel."

{¶ 4} The handwritten terms in the Notes/Special Situation section of Schwartz's service contract identically matched Alltel's *Cleveland Plain Dealer* advertisement, which Schwartz read on August 24, 2000.

{¶ 5} The service agreement contained the following provision in small print on the reverse side of the document:

"Any dispute arising out of this Agreement or relating to the Services and Equipment must be settled by arbitration administered by the American Arbitration Association. Each party will bear the cost of preparing and prosecuting its case. We will reimburse you for any filing or hearing fees to the extent they exceed what your court costs would have been if your claim had been resolved in state court having jurisdiction. The arbitrator has no power or authority to alter or modify these Terms and Conditions, including the foregoing Limitation of Liability section. All claims must be arbitrated individually, and there will be no consolidation or class treatment of any claims. This

provision is subject to the United States Arbitration Act."

{¶ 6} The service agreement also contained a provision limiting the liability of Alltel, which read:

"Our liability regarding your use of the services or equipment, or the failure of or inability to use the services or equipment is limited to the charges you incur for services or equipment during the affected period. This means we are not liable for any incidental or consequential damages (such as lost profits or lost business opportunities), punitive damages or exemplary damages, such as attorney fees."

{¶ 7} Alltel placed the arbitration provision of the agreement on the back page of a one-page, legal-size agreement, in a light-gray small font, at the very end of the page. Alltel also placed the limitation of liability provision on the back of the agreement in the same light-gray small font but this time in capital letters.

Alltel placed both provisions among other boilerplate, contractual language.

{¶ 8} Additionally, above the signature line, Alltel placed an explicit acknowledgment that the consumer understands and accepts the "terms and conditions on both sides" of the agreement. Finally, Alltel also included a "Notes/Special Situations" section that allows parties to write in additional terms. At the time of the agreement, this section contained the above-quoted handwritten

phrase, "\$49.95 unlimited local air time for life as long as customer remains on rate plan with Alltel." Schwartz signed the agreement without writing in any new additional terms.

{¶ 9} In January 2001, some four months later, Alltel sent Schwartz a letter informing him that Alltel would be raising his rates from the contracted rate of \$49.95 per month to \$59.95 per month for unlimited local calling, due to the "increased cost of doing business." The letter also informed Schwartz that Alltel raised Schwartz's roaming rate from \$.59 per minute to \$.99 per minute. On November 20, 2001, Schwartz filed the instant class action lawsuit against Alltel alleging breach of contract, violation of the Ohio Consumer Sales Practices Act ("CSPA") and fraudulent inducement.

{¶ 10} In response to the lawsuit, Alltel filed a motion to stay litigation pending binding arbitration. Schwartz filed a brief in opposition raising the argument that the arbitration provision of the agreement was unconscionable. Before the trial court rendered a decision, Alltel and Schwartz filed several motions, including motions for leave to file reply and sur-reply briefs and motions to strike. After negotiating, the parties agreed that the trial court would decide the arbitration issue solely based on Alltel's motion to stay, Schwartz's brief in opposition, and Alltel's reply brief. The trial court heard oral arguments on November 22, 2002.

{¶ 11} On July 21, 2005, the trial court issued its written

opinion denying Alltel's motion to stay litigation pending binding arbitration.¹ In its decision, the trial court found Alltel's arbitration provision procedurally and substantively unconscionable.

{¶ 12} Alltel appeals, raising the five assignments of error contained in the appendix to this opinion.

{¶ 13} In its first assignment of error, Alltel argues: "The Trial Court Erred in Finding there was no Agreement to Arbitrate." This assignment of error lacks merit.

{¶ 14} This assigned error is unusual in that Alltel argues that *if* the trial court based its decision to deny arbitration on the finding that there was no agreement to arbitrate, the trial court erred. In making this argument, Alltel quotes the following sentence from the trial court's opinion: "[the] agreement to arbitrate was not voluntary in a real and genuine sense."

{¶ 15} This court has reviewed the trial court's opinion and order and finds that the trial court based its decision to deny arbitration on a finding of procedural and substantive unconscionability, on public policy grounds and on the basis that the contract was adhesive in nature. The trial court did not base its decision on the conclusion that the agreement to arbitrate did

¹An order granting or denying a stay of an action pending arbitration is a final appealable order pursuant to R.C. 2711.02(C).

not exist.

{¶ 16} Accordingly, Alltel's first assignment of error is overruled.

{¶ 17} In its second and third assignments of error, Alltel argues that the trial court erred in concluding that the arbitration agreement was procedurally and substantively unconscionable. Because these assignments of error utilize identical standards of review, this court will address them contemporaneously.

{¶ 18} When addressing whether a trial court has properly granted a motion to stay litigation pending arbitration, this court applies an abuse of discretion standard. *Carter Steel & Fabricating Co. v. Danis Bldg. Constr. Co.* (1998), 126 Ohio App.3d 251, 254-55. An abuse of discretion connotes more than an error of law or judgment. Instead, it implies the trial court's judgment was unreasonable, arbitrary or unconscionable. *Blakemore v. Blakemore* (1983), 5 Ohio St.3d 217, 219. Absent an abuse of that discretion, an appellate court may not substitute its judgment for that of the trial court. *Pons v. Ohio State Med. Bd.*, 66 Ohio St.3d 619, 621, 1993-Ohio-122.

{¶ 19} However, when an appellate court is presented with purely legal questions, it applies a de novo standard of review. *Akron-Canton Waste Oil, Inc v. Safety-Kleen Oil Servs., Inc.* (1992), 81 Ohio App.3d 591, 602. Under a de novo standard of review, an

appellate court does not give deference to a trial court's decision. *Akron v. Frazier* (2001), 142 Ohio App.3d 718, 721.

{¶ 20} In the instant case, Schwartz challenges the enforceability of the arbitration clause in this contract, asserting that it is unconscionable.

{¶ 21} The issue of unconscionability is a question of law. *Ins. Co. of North America v. Automatic Sprinkler Corp.* (1981), 67 Ohio St.2d 91, 98. Accordingly, this court must conduct a factual inquiry into the particular circumstances of the transaction in question. *Id.* Such a determination requires a case-by-case review of the facts and circumstances surrounding the agreement. *Vincent v. Neyer* (2000), 139 Ohio App.3d 848, 854-56. Because this case involves legal questions, we will apply a de novo standard of review.

{¶ 22} Initially we note that arbitration is encouraged as a method of dispute resolution, and a presumption favoring arbitration arises when the claim in dispute falls within the arbitration provision. *Williams v. Aetna Fin. Co.*, 83 Ohio St.3d 464, 471, 1998-Ohio-294. R.C. 2711.01(A) sets forth Ohio's public policy favoring arbitration and provides as follows:

"A provision in any written contract, except as provided in division (B) of this section, to settle by arbitration a controversy that subsequently arises out of the contract, or out of the refusal to perform the whole or any part of the contract, or any agreement in writing between two or more persons to submit to arbitration any controversy existing between them at the time of the

agreement to submit, or arising after the agreement to submit, from a relationship then existing between them or that they simultaneously create, shall be valid, irrevocable, and enforceable, except upon grounds that exist at law or in equity for the revocation of any contract."

{¶ 23} An arbitration clause may be legally unenforceable if the clause is not applicable to the matter at hand, if the parties did not agree to the clause in question, or if the arbitration clause is found to be unconscionable. *Ida May Fortune v. Castle Nursing Home*, Holmes App. No. 05 CA 1, 2005 Ohio-6195.

"Unconscionability refers to the absence of a meaningful choice on the part of one of the parties to a contract, combined with contract terms that are unreasonably favorable to one party [Citation omitted.] Accordingly, unconscionability consists of two separate concepts: (1) substantive unconscionability, which refers to the commercial reasonableness of the contract terms themselves, and (2) procedural unconscionability, which refers to the bargaining positions of the parties. [Citation omitted.]

"Substantive unconscionability involves those factors which relate to the contract terms themselves and whether they are commercially reasonable. Because the determination of commercial reasonableness varies with the content of the contract terms at issue in any given case, no generally accepted list of factors has been developed for this category of unconscionability. However, courts examining whether a particular limitations clause is substantively unconscionable have considered the following factors: the fairness of the terms, the charge for the service rendered, the standard in the industry, and the ability to accurately predict the extent of future liability. [Citations omitted]"

"Procedural unconscionability involves those factors bearing on the relative bargaining position of the

contracting parties, e.g., 'age, education, intelligence, business acumen and experience, relative bargaining power, who drafted the contract, whether the terms were explained to the weaker party, whether alterations in the printed terms were possible, whether there were alternative sources of supply for the goods in question. [Citation omitted.]"

Fortuna, supra.

{¶ 24} In order to negate an arbitration clause, a party must establish a quantum of both substantive and procedural unconscionability. *Small v. HCF of Perrysburg, Inc.*, 159 Ohio App.3d 66, 2004-Ohio-5757.

{¶ 25} In concluding that the arbitration agreement was substantively unconscionable, the trial court found the contractual language was unconscionable because it limited the rights of consumers to file as a class, it did not put a consumer on notice as to his rights regarding future liability and it prohibited any award of attorney fees. We agree with the trial court's conclusions.

{¶ 26} By eliminating a consumer's right to proceed through a class action, the arbitration clause directly hinders the consumer protection purposes of the CSPA. *Eagle v. Fred Martin Motor Co., et al.*, 157 Ohio App.3d 150, 2004-Ohio-829. The United States Supreme Court has expressed the importance of class actions:

"The use of the class-action procedure for litigation of individual claims may offer substantial advantages for named plaintiffs; it may motivate them to bring cases that for economic reasons might not be brought otherwise.
*** The financial incentive that class actions offer ***

is a natural outgrowth of the increasing reliance on the 'private attorney general' for vindication of legal rights[.]" *Deposit Guaranty Natl. Bank v. Roper* (1980), 445 U.S. 326, 338, 100 S.Ct. 1166.

{¶ 27} Additionally, R.C. 1345.09(F)(2) grants attorney fees for any violation of Ohio's CSPA; and yet Alltel's limitation of liability section expressly forbids an award of attorney fees.

{¶ 28} In response to this argument, Alltel argues that the agreement provides for reimbursement of fees to the extent that they exceed what court costs would have been if the claim had been resolved in a state court having jurisdiction. Moreover, Alltel claims that even though the limitation of liability provision of the agreement prohibits an award of attorney fees, an arbitrator could still award statutory attorney fees. These arguments are without merit.

{¶ 29} By prohibiting its customers from filing suit as a class, Alltel prevents the cost effective use of class action litigation that can end abusive practices by large corporations in those instances in which individual claims are ineffective. Additionally, the arbitration provision specifically strips an arbitrator of any authority to alter or modify the terms of the arbitration provision or the limitation of liability section.

{¶ 30} Because Alltel's arbitration provision eliminates the right to proceed through a class action and prohibits an award of attorney fees that are statutorily authorized, the arbitration

clause invades the policy considerations of the CSPA. See R.C. 1345.09(F)(2). This limitation of consumer rights found within the arbitration provision establishes a quantum of substantive unconscionability.

{¶ 31} We must now determine whether the arbitration agreement is procedurally unconscionable. When concluding that the agreement to arbitrate was procedurally unconscionable, the trial court made the following findings: the agreement was adhesive; Alltel drafted the contract; Alltel never explained the terms to Schwartz; and the experience of Schwartz in similar situations was less than that of Alltel. We agree with the trial court's conclusion.

{¶ 32} As stated above, the factors to consider are the "bargaining position of the contracting parties, including age, education, intelligence, business acumen, experience in similar transactions, whether the terms were explained to the weaker party and who drafted the contract." *Eagle*, supra.

{¶ 33} Alltel argues that Schwartz has failed to present any evidence of procedural unconscionability. Alltel claims that the only evidence of any alleged procedural unconscionability was Schwartz's affidavit, which counsel withdrew. Though Schwartz's counsel did withdraw the affidavit, the record contains other evidence of procedural unconscionability.

{¶ 34} Primarily we note the inherent disparity of the bargaining position of Schwartz and Alltel. Schwartz, a consumer,

contracted with Alltel, a multi-billion dollar corporation, for the purchase of a cellular telephone and service. Though we are unaware of how often Schwartz engaged in contracts of this nature, it is clear that for Alltel, this was a common occurrence. Additionally, when Schwartz expressed interest in the advertised deal, an Alltel employee presented him with Alltel's pre-printed form. The form itself contained small, hard-to-read print and contained margin-to-margin boilerplate, contractual language. As stated above, Alltel placed the arbitration provision at the very bottom of the back side of the agreement, without calling any attention to the provision.

{¶ 35} Moreover, the agreement for service was adhesive in nature. Alltel presented the agreement to Schwartz on a take-it-or-leave-it basis. To receive the advertised offer, Schwartz had to sign Alltel's pre-printed form contract, which contained the arbitration provision. Finally, Schwartz was not represented by counsel when he signed the agreement.

{¶ 36} Accordingly, we find that sufficient evidence of procedural unconscionability existed at the time Schwartz signed the agreement with Alltel. We further find that the trial court did not err when it determined that the agreement was substantively and procedurally unconscionable.

{¶ 37} Alltel's second and third assignments of error are overruled.

{¶ 38} In its fourth assignment of error, Alltel argues that the trial court erred in ignoring the agreement's severability provision.² We disagree.

{¶ 39} Though Alltel's service agreement contained a severability provision, when the cumulative effect of multiple illegal provisions "taints" the overall agreement and prevents a court from enforcing that agreement, severability is improper. *Scovill v. WSYX/ABC*, 425 F.3d 1012 (C.A.6, 2005). See, also, *Alexander v. Anthony Internatl. L. P.*, 341 F.3d 256, 261 (C.A.3, 2003) ("The cumulative effect of so much illegality prevents us from enforcing the arbitration agreement. Because the sickness has infected the trunk, we must cut down the entire tree.").

{¶ 40} Schwartz presented enough evidence to show that the agreement in this case contained unenforceable provisions so overwhelming as to "taint" the rest of the agreement. Schwartz has shown both substantive and procedural unconscionability through improper limitation of consumer rights and remedies, the adhesive nature of the service agreement, and the circumstances surrounding his signature of the agreement.

{¶ 41} Accordingly, we find that the trial court did not err in

² **"No Waiver; Severability:** If we do not enforce any right or remedy available under this Agreement, that failure is not a waiver. If any part of this Agreement is held invalid or unenforceable, the remainder of this Agreement will remain in force."

striking the entire arbitration agreement.

{¶ 42} Alltel's fourth assignment of error is overruled.

{¶ 43} In its fifth and final assignment of error, Alltel argues that the trial court erred in ignoring controlling federal law governing the arbitration provision. This assignment of error lacks merit.

{¶ 44} Alltel bases this argument on the trial court's lack of citations to federal cases and the Federal Arbitration Agreement ("FAA"). However, the trial court did cite to federal authority in its opinion. Additionally, we have previously found that the trial court properly determined that the arbitration provision of the agreement was unconscionable. That the trial court did not reference the FAA in its opinion, does not mean that the trial court did not consider the act in making its proper decision. When Alltel referenced the FAA several times throughout this initial discovery process, it placed the trial court on notice of its reliance on the act. Finally, Alltel provides this court with no authority to support its proposition that because the trial court did not reference sufficient federal case law and the FAA, its decision to deny the motion to stay pending arbitration was improper.

{¶ 45} Alltel also argues in this assigned error that the trial court erred in not applying the Federal Communication Act of 1934 ("FCA"). However, Alltel raises this issue for the first time on

appeal and has thus waived all but plain error. *Goldfuss v. Davidson*, 79 Ohio St.3d 116, 1997-Ohio-401. In appeals of civil cases, the plain error doctrine is not favored and may be applied only in the extremely rare case involving exceptional circumstances where error, to which no objection was made at the trial court, seriously affects the basic fairness, integrity, or public reputation of the judicial process and thereby challenges the legitimacy of the underlying judicial process itself. *Id.* at syllabus. In response to the waiver argument, Alltel claims that it did make this argument in the trial court below, that it specifically argued "federal substantive law of arbitration" governed Schwartz's claims and required arbitration. This argument is unpersuasive. If Alltel wanted to argue the applicability of the FCA on appeal, it was Alltel's duty to raise this argument below, not merely reference any federal law of arbitration. Accordingly, Alltel waives all but plain error and we decline to find plain error in this case.

{¶ 46} Alltel's fifth assignment of error is overruled.

{¶ 47} The judgment of the trial court is affirmed.

It is ordered that appellee shall recover of appellant costs herein taxed.

The court finds that there were reasonable grounds for this appeal.

It is ordered that a special mandate issue out of this court directing the Cuyahoga County Common Pleas Court to carry this judgment into execution.

A certified copy of this entry shall constitute the mandate pursuant to Rule 27 of the Rules of Appellate Procedure.

MARY EILEEN KILBANE
JUDGE

JAMES J. SWEENEY, P.J., And

DIANE KARPINSKI, J., CONCUR

N.B. This entry is an announcement of the court's decision. See App.R. 22(B), 22(D) and 26(A); Loc. App.R.22. This decision will be journalized and will become the judgment and order of the court pursuant to App.R. 22(E), unless a motion for reconsideration with supporting brief, per App.R. 26(A) is filed within ten (10) days of the announcement of the court's decision. The time period for review by the Supreme Court of Ohio shall begin to run upon the journalization of this court's announcement of decision by the clerk per App.R. 22(E). See, also, S.Ct.Prac.R. II, Section 2(A)(1).

Appendix

Assignments of Error:

"I. The trial court erred in finding there was no agreement to arbitrate.

II. The trial court erred in finding the agreement was procedurally unconscionable.

III. The trial court erred in finding the agreement was substantively unconscionable.

IV. The trial court erred in ignoring the agreement's severability provision.

V. The trial court erred in ignoring controlling federal law governing the arbitration provision."

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

CHUN WING WONG,

Plaintiff,

v.

T-MOBILE USA, INC.,

Defendant.

Case No. 05-73922

Honorable Nancy G. Edmunds

ORDER DENYING DEFENDANT'S MOTION TO COMPEL ARBITRATION [4]

Plaintiff Chun Wing Wong brought this proposed class action lawsuit based on Defendant T-Mobile USA's apparent practice of overcharging its cellular telephone customers. As to Plaintiff individually, Defendant wrongfully overcharged only a small sum of money, but overall, Plaintiff alleges, Defendant may have wrongfully reaped millions of dollars from its customers.

Now before the Court is Defendant's Motion to Compel Arbitration pursuant to the cellular service contract between Plaintiff and Defendant. Importantly, Defendant's contract protects it from any sort of class action, and thus allows Defendant to overcharge its customers without substantial risk of liability.

For the reasons discussed below, this Court finds that the class action waiver in Defendant's contract is unenforceable. Because the contract prohibits class-wide arbitration, the Court DENIES Defendant's Motion.

I. Background

The facts of this case do not appear to be in serious dispute. In 2003, Plaintiff purchased a cellular telephone from Defendant and the parties entered into a contract. Part of the contract provided that in exchange for a monthly fee of \$4.99, Defendant would provide Plaintiff with “unlimited T-Zones,” a feature including “unlimited Internet, email and Mobile Web content.” Nevertheless, Defendant charged Plaintiff additional fees for use of the internet, email, and mobile phone content. On several occasions, Plaintiff requested a refund of the money. While Defendant concedes that Plaintiff was overcharged in error, Defendant has refused to refund some of the money on account of Plaintiff’s failure to object to the charges within the limitations period. Plaintiff notes that while his actual damages are only \$19.74, in the aggregate, Defendant “has probably collected millions of dollars improperly.” (Br. of Pl. 8.)

The service contract between Plaintiff and Defendant made arbitration of disputes mandatory and contained a class action waiver. In April of 2003, however, a federal district court in California struck Defendant’s class action waiver provision and sent the case for class-wide arbitration. *Gatton v. T-Mobile USA, Inc.*, 2003 U.S. Dist. LEXIS 25922 (C.D. Cal. Apr. 18, 2003). Perhaps troubled by the prospect of class-wide arbitration, Defendant revised the arbitration agreement as follows:

CLASS ACTION WAIVER. WHETHER IN COURT, SMALL CLAIMS COURT, OR ARBITRATION, YOU AND WE MAY ONLY BRING CLAIMS AGAINST EACH OTHER IN AN INDIVIDUAL CAPACITY AND NOT AS A CLASS REPRESENTATIVE OR A CLASS MEMBER IN A CLASS OR REPRESENTATIVE ACTION. NOTWITHSTANDING SEC. 22, IF A COURT OR ARBITRATOR DETERMINES IN A CLAIM BETWEEN YOU AND US THAT YOUR WAIVER OF ANY ABILITY TO PARTICIPATE IN CLASS OR REPRESENTATIVE ACTIONS IS UNENFORCEABLE UNDER APPLICABLE LAW, THE ARBITRATION AGREEMENT WILL NOT APPLY, AND YOU

AND WE AGREE THAT SUCH CLAIMS WILL BE RESOLVED BY A COURT OF APPROPRIATE JURISDICTION, OTHER THAN A SMALL CLAIMS COURT.

(Br. of Pl. Ex. 5.) Thus, while arbitration remains the agreed-upon means to resolve the present dispute, the parties have also agreed that if this Court finds the class action waiver unenforceable, the case shall be resolved here, rather than in an arbitral forum.

Plaintiff's Class Action Complaint alleges five causes of action: (I) Violation of the Michigan Consumer Protection Act ("MCPA"), (II) Breach of Contract/Express Warranty, (III) Fraud, (IV) Unjust Enrichment/Restitution/Disgorgement, and (V) Injunctive and Declarative Relief Including Reformation of Contract and for an Accounting.

II. Discussion

As Plaintiff points out, the first issue before the Court is whether the class action waiver is enforceable. If not, the parties have agreed to settle this dispute in this forum, and the Court need not go further.

Plaintiff argues that the class action waiver is unenforceable as contrary to the explicit policies set forth in the MCPA, which expressly grants the right to bring and participate in class action litigation. Mich. Comp. Laws § 445.911(3). Defendant argues that because the right to class actions is not a *substantive* right, but a procedural one, an arbitration agreement may dispose of this right. Indeed, Defendant notes, "[t]he whole point of arbitration is to provide for a quick, inexpensive resolution by foregoing a whole panoply of procedures available to litigants in court." (Br. of Def. 15.) In any event, Defendant contends, the MCPA does not apply here, since that statute exempts conduct authorized under law, and the federal government regulates the cellular industry.

A. Class Action Waiver

The Federal Arbitration Act ("FAA"), under which Defendant brings this Motion, provides that the arbitration clause should be enforced "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. In *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614 (1985), the Supreme Court read this statute to encourage the enforcement of arbitration agreements, even where, as here, a plaintiff raises a statutory claim:

The "liberal federal policy favoring arbitration agreements" . . . is at bottom a policy guaranteeing the enforcement of private contractual arrangements: the Act simply "creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate." "[The] preeminent concern of Congress in passing the Act was to enforce private agreements into which parties had entered," a concern which "requires that we rigorously enforce agreements to arbitrate." . . . There is no reason to depart from these guidelines where a party bound by an arbitration agreement raises claims founded on statutory rights. . . .

...

By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum. It trades the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition of arbitration

Id. at 625-28 (internal citations and footnotes omitted). Although the plaintiffs in *Mitsubishi* argued that arbitration would undermine the deterrent purposes of the statutes upon which their lawsuit was based, the Court held that "so long as the prospective litigant effectively may vindicate its statutory cause of action in the arbitral forum, the statute will continue to serve both its remedial and deterrent function." *Id.* at 637.

In *Rembert v. Ryan's Family Steakhouses, Inc.*, 596 N.W.2d 208 (Mich. Ct. App. 1999), which the parties agree to be a key precedent, the Michigan Court of Appeals relied

on the above language from *Mitsubishi* in addressing whether public policy considerations could preclude the arbitration of statutory claims. The court read *Mitsubishi* as follows:

[T]he Court held that if the parties had agreed to arbitrate statutory claims, the agreement should be enforced unless . . . the agreement foreclosed effective vindication of statutory rights. . . .

[T]he basic rationale . . . is twofold. First the Court endorsed the principle that an agreement to arbitrate a statutory claim does not constitute waiver of substantive rights. Second, the Court recognized that a statute will serve both its remedial and deterrent functions as long as the prospective litigant can vindicate his statutory cause of action in the arbitral forum.

596 N.W.2d at 218-19 (citing *Mitsubishi*, 473 U.S. at 628). Thus, the *Rembert* court held that an arbitration agreement is unenforceable if it “is drafted in a way that effectively waives the plaintiff’s substantive rights or remedies or so structures the procedures as to make it impossible for the plaintiff to ‘effectively vindicate his statutory cause of action’” *Id.* at 225 (internal citations omitted).

This reading finds support in a recent First Circuit Court of Appeals case. In *Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006), the court issued an exhaustive opinion addressing an arbitration agreement between a cable provider and its customers which prohibited class actions. Although the plaintiffs had brought suit under state and federal antitrust laws, rather than consumer protection laws, the analysis is helpful here.

The *Kristian* court recognized the federal policy favoring arbitration agreements, but also acknowledged an important need for class actions. As the Supreme Court has instructed, “the policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights.” *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (quoting *Mace v. Van Ru Credit Corp.*, 109 F.3d 338, 344 (7th Cir. 1997)). Another court

has wisely cautioned that “[t]he realistic alternative to a class action is not 17,000,000 individual suits, but zero individual suits, as only a lunatic or a fanatic sues for \$30.00.” *Carnegie v. Household Int’l, Inc.*, 376 F.3d 656, 661 (7th Cir. 2004).

In light of the importance of class actions, the *Kristian* court stated, “While . . . the class action . . . [i]s a procedure for redressing claims—and not a substantive or statutory right in and of itself—we cannot ignore the substantive implications of this procedural mechanism.” 446 F.3d at 54.

If the class mechanism prohibition here is enforced, Comcast will be essentially shielded from private consumer antitrust enforcement liability, even in cases where it has violated the law. Plaintiffs’ will be unable to vindicate their statutory rights. Finally, the social goals of federal and state antitrust laws will be frustrated because of the “enforcement gap” created by the de facto liability shield.

Id. at 61. The court concluded that “the provision[] of the arbitration agreements . . . barring class arbitration are invalid because they prevent the vindication of statutory rights under state and federal law.” *Id.* at 29.

This Court recognizes that the First Circuit’s approach is not universally accepted. As the *Kristian* court noted, the Third, Fourth, Seventh, and Eleventh Circuit Courts of Appeal have enforced class action prohibitions in consumer arbitration clauses. *Id.* at 78-79 (citing *Johnson v. W. Suburban Bank*, 225 F.3d 366, 374 (3d Cir. 2000); *Snowden v. Checkpoint Check Cashing*, 290 F.3d 631, 638 (4th Cir. 2002); *Livingston v. Assocs. Fin., Inc.*, 339 F.3d 553, 559 (7th Cir. 2003); *Randolph v. Green Tree Fin. Corp.*, 244 F.3d 814, 819 (11th Cir. 2001)). The Court is not aware of any Sixth Circuit case addressing this precise issue.

Two federal district court cases in Michigan are helpful, however. One recent case holds that the preclusion of class actions does not render an arbitration agreement substantively unconscionable. *Copeland v. Katz*, 2005 U.S. Dist. LEXIS 31042, at *11-12 (E.D. Mich. Nov. 28, 2005). While the question of substantive unconscionability is related, it is distinct from the issue presented here. Moreover, *Copeland* did not involve the MCPA, which expressly provides for class actions.

Lozada v. Dale Baker Oldsmobile, 91 F. Supp. 2d 1087 (W.D. Mich. 2000), is more directly on point. In *Lozada*, the court applied *Rembert* to the MCPA and an arbitration agreement including a class action waiver. The court found the class action waiver unenforceable:

[U]nder the Michigan Consumer Protection Act, the availability of class recovery is explicitly provided for and encouraged by statute. See Mich. Comp. Laws § 445.911(3) (expressly permitting aggrieved person to bring class action for claims brought pursuant to the MCPA). Because the arbitration agreement prohibits the pursuit of class relief, it impermissibly waives a state statutory remedy.

Id. at 1105 (citing *Rembert*, 596 N.W.2d at 230).

Defendant asks this Court to reject *Lozada*, arguing that it has misinterpreted the holding in *Rembert*:

What the *Rembert* court in fact held was that, in the context of statutory employment discrimination claims, “the arbitration agreement [must] not waive the *substantive* rights and remedies of the statute. . . .” The right to a class action, however, is not a substantive right or remedy provided by the MCPA (which is not an employment-related statute in any event). Rather, it is a *procedural* right.

(Br. of Def. 14-15.) Defendant reads *Rembert* too narrowly, however, replacing the following critical language with an ellipse: “and the arbitration procedures are fair so that

the employee may effectively vindicate his statutory rights.” 596 N.W.2d at 226. Despite Defendant’s attempt to ignore it, this critical language controls the present case.

Whether the right to a class action is a substantive or a procedural one, it is certainly necessary for the effective vindication of statutory rights, at least under the facts of this case. Defendant makes much of the fact that it contributes toward plaintiffs’ arbitration costs, but in order for arbitration to be feasible, the amount at issue must also exceed the value in time and energy required to arbitrate a claim. Defendant is alleged to have bilked its customers out of millions of dollars, though only a few dollars at a time. Plaintiff’s damages are a paltry \$19.74, hardly enough to make arbitration worthwhile. Class actions were designed for situations just like this. The MCPA’s class action mechanism is essential to the effective vindication its statutory cause of action.

B. MCPA Preemption

The discussion above assumes that Plaintiff has a statutory cause of action, like the plaintiffs in *Rembert*, *Lozada* and *Kristian*. Plaintiff’s only statutory claim falls under the MCPA, but Defendant argues that its conduct is exempt from the MCPA. If Defendant is correct, the MCPA would not apply, and the class-action waiver could not run afoul of that statute. In other words, the MCPA would not render the arbitration agreement unenforceable.

The MCPA contains an exemption for a “transaction or conduct specifically authorized under laws administered by a regulatory board or officer acting under statutory authority of this state or the United States.” Mich. Comp. Laws § 445.904(1)(a). The key Michigan precedent interpreting this provision is *Smith v. Globe Life Insurance Co.*, 597 N.W.2d 28 (Mich. 1999), in which the Michigan Supreme Court concluded that

when the Legislature said that transactions or conduct “specifically authorized” by law are exempt from the MCPA, it intended to include conduct the legality of which is in dispute. Contrary to the “common-sense reading” of this provision by the Court of Appeals, we conclude that the relevant inquiry is not whether the specific misconduct alleged by the plaintiffs is “specifically authorized.” Rather, it is whether the general transaction is specifically authorized by law, regardless of whether the specific misconduct alleged is prohibited.

Id. at 38.

Recently, this Court had occasion to review the MCPA and the implications of the *Smith* case. In *Flanagan v. Altria Group*, 2005 U.S. Dist. LEXIS 24644 (E.D. Mich. Oct. 25, 2005), the plaintiff relied on the MCPA to claim that a cigarette manufacturer had unlawfully misled consumers in its labeling and advertising practices. The defendant, relying on *Smith*, argued that the MCPA did not apply, since the federal government permitted and regulated cigarette labeling and advertising.

As the *Flanagan* opinion suggests, the issue was a difficult one.¹ After analyzing a comprehensive federal regulatory scheme at issue, the Court concluded that because the

¹The Court cited a commentary lamenting *Smith*'s effect on what was once “one of the broadest and most powerful consumer protection acts in the country. . . . As a result of [*Smith*], the MCPA has entered a new era. Indeed, there may be little left of the power to protect consumers that the legislature had in mind when it passed the act.” Gary M. Victor, *The Michigan Consumer Protection Act: What's Left after Smith v. Globe?*, 82 Mich. B. J. 22, 23-25 (2003). The Court also agreed with the Michigan Court of Appeals's decision in *Smith* “that under ‘a common-sense reading’ of the MCPA, ‘authorized’ should not include ‘illegal.’” 2005 U.S. Dist. LEXIS 24644, at *21 (quoting *Smith v. Globe Life Ins. Co.*, 565 N.W.2d 877, 884 (Mich. Ct. App. 1997), *rev'd*, 597 N.W.2d 28). But the Court recognized that “that is not the law in Michigan,” and that “the Michigan courts’ liberal definition of ‘specifically authorized’ under the MCPA’s exemption provision” left very little room for consumer lawsuits under the MCPA. Recently, a panel of the Michigan Court of Appeals has “question[ed] the wisdom of . . . *Smith*,” noting that it “liberally interpreted the phrase ‘transaction or conduct specifically authorized’ to include any activity or arrangement permitted by statute.” *Hartman & Eichhorn Bldg. Co. v. Dailey*, 701 N.W.2d 749, 753 (Mich. Ct. App. 2005), *leave granted*, 712 N.W.2d 724 (Mich. 2006).

defendant's "general transaction' was the labeling and advertising of its cigarettes," and because federal law "establishes a comprehensive Federal program to deal with cigarette labeling and advertising," the defendant's conduct was exempt from the MCPA. *Id.* at *22 (quoting 15 U.S.C. § 1331). This finding relied on a factual comparison with *Smith* and a number of other cases interpreting the MCPA exemption.

In *Smith*, the conduct at issue was the sale of credit life insurance. The court held that the conduct was protected because the defendant had, pursuant to a state statute, submitted the necessary application and certificate of insurance forms to the State Commissioner of Insurance, and had implicitly been approved for the policy. *Id.* at 36-37. In *Kraft v. Detroit Entertainment, L.L.C.*, 683 N.W.2d 200 (Mich. Ct. App. 2004), the plaintiff alleged fraud based on the deceptive use of slot machines. The court found this claim exempt because the operation of slot machines was regulated and specifically authorized by the Michigan Gaming Control Board, whose administrative rules "specifically authorized defendants to operate the slot machines at issue" *Id.* at 204-05. And in *Newton v. Bank West*, 686 N.W.2d 491 (Mich. Ct. App. 2004), the plaintiffs alleged that a bank had improperly charged mortgage fees. The court found it "abundantly clear" that banks making residential mortgage loans "are engaged in transactions 'specifically authorized' under laws administered by officers acting under both state and federal statutes." *Id.* at 493-94.

In addition to these state cases, this Court cited three federal cases decided on similar grounds. *Burton v. William Beaumont Hosp.*, 373 F. Supp. 2d 707, 720-22 (E.D. Mich. 2005) (claims based on hospital billing practice exempt because state statute governed health facility billing practices); *Mills v. Equicredit Corp.*, 294 F. Supp. 2d 903,

910 (E.D. Mich. 2003) (improper lending practices claim exempt because defendant bank “was a licensed mortgage lender under a Michigan law that was regulated by the Commissioner of the Office of Financial and Insurance Services of the Department of Consumer and Industry Services”); *Wheeling, Inc. v. Stelle*, 2000 U.S. Dist. LEXIS 8628, at *18-19 (E.D. Mich. 2000) (securities fraud claim exempt because the “sale of securities is regulated by the Michigan Uniform Securities Act, which is administered by the Corporation and Securities Bureau of the Michigan Department of Commerce”).

The Court noted, however, that not every decision has favored defendants. Two pre-*Smith* cases are particularly instructive. In *Attorney General v. Diamond Mortgage Co.*, 327 N.W.2d 805 (Mich. 1982), which *Smith* distinguished but declined to overrule, 597 N.W.2d at 37-38, the defendant was a licensed real estate broker sued for conduct related to mortgage lending. The Michigan Supreme Court held the relevant conduct was “mortgage writing,” which was not “specifically authorized” under the defendant’s real estate broker’s license, and thus was not exempt from the MCPA:

While the license generally authorizes Diamond to engage in the activities of a real estate broker, it does not specifically authorize the conduct that plaintiff alleges is violative of the Michigan Consumer Protection Act, nor transactions that result from that conduct. . . . For this case, we need only decide that a real estate broker’s license is not specific authority for all the conduct and transactions of the licensee’s business.

327 N.W.2d at 811.

Another case apparently left undisturbed by *Smith* is *Baker v. Arbor Drugs, Inc.*, 544 N.W.2d 727 (Mich. Ct. App. 1996), in which the Michigan Court of Appeals made clear that in order to be protected, the conduct at issue—what *Smith* termed the “general transaction”—must fall within the purview of the regulatory agency:

We do not agree with defendant that it is exempt from the MCPA because it is governed by a regulatory board, the Michigan Board of Pharmacy. It is true that the MCPA does not apply to a transaction or conduct specifically authorized under laws administered by a regulatory board or officer. This exemption does not apply in this case because the alleged violative conduct falls outside the realm of the regulatory commission. Here, plaintiff is claiming that defendant's advertising . . . violates the MCPA. Advertising is not within the purview of the Pharmacy Board's regulatory powers. Therefore, plaintiff's claim that defendant's advertising . . . violates the MCPA falls outside the realm of the regulatory commission and . . . the MCPA does not apply.

Id. at 732 (internal citations omitted).

These cases demonstrate that while *Smith* unquestionably broadened the MCPA's exemption for conduct authorized by a government agency, it did not abrogate the statute entirely. Even if a defendant is licensed or regulated, it may remain liable under the MCPA for conduct outside the scope of its license or the pertinent regulations. In other words, "specifically authorized" does not simply mean "not prohibited." To conclude otherwise would be to create a gap in enforcement in those areas not covered by government regulation.

Applying these principles to the present case, the Court must determine what the "general transaction" was. Defendant argues, "The general transaction at issue here—the provision of wireless communications services—is subject to comprehensive federal regulation." (Br. of Def. 17.) Defendant essentially makes the same argument as the defendant pharmacy in *Baker*, which sought protection for all of its conduct pursuant to regulation by the Michigan Board of Pharmacy, though advertising fell outside of the Board's authority. Just as in *Baker*, Defendant's description is far too broad.

Plaintiff, on the other hand, states that he "is not complaining about the reasonableness of the rates charged by Defendant—a subject clearly preempted by the

Federal Communications Act—but rather Defendant’s deception and failure to provide the benefits promised.” (Br. of Pl. 21 n.6.) Plaintiff therefore wishes to describe the pertinent transaction simply as Defendant’s wrongful acts, but as the court in *Smith* explained, the focus is not on the “specific misconduct alleged,” but on the “general transaction.” 597 N.W.2d at 38. Thus, Plaintiff also misses the mark.

In truth, several general transactions take place under the umbrella of providing cellular services, but this case concerns only one: billing. Plaintiff alleges that Defendant double-billed him for a service he had already paid for. The Court must therefore determine whether Defendant’s billing practices are “specifically authorized.”

In arguing that they are, Defendant cites the Federal Communications Act, which asserts federal control over all interstate radio communications. See 47 U.S.C. § 151 *et seq.* Defendant also cites the Federal Communications Commission’s “pervasive body of regulations governing virtually every aspect of wireless communications” (Br. of Def.18), such as cellular service requirements, geographic coverage, emissions, and licensing requirements. See 47 C.F.R. § 22.901, 22.911, 22.913, 22.917, 22.929. While these regulations are extensive, none of them govern the billing practices of cellular telephone companies.

More persuasively, Defendant notes that a federal statute requires that charges for any radio-based communications be reasonable. See 47 U.S.C. § 201, 202. Furthermore, the FCC has created the Wireless Telecommunications Bureau, which “develops, recommends and administers the programs and policies for the regulation of the terms and conditions under which communications entities offer domestic wireless telecommunications services” 47 C.F.R. § 0.131. Among its duties, this bureau

“[r]egulates the charges, practices, classifications, terms and conditions for, and facilities used to provide, wireless telecommunications services.” 47 C.F.R. § 0.131(d). Thus, according to the regulations that Defendant cites, the FCC appears to take an active role in regulating cellular telephone contracts.

Plaintiff takes issue with this characterization, however, and offers a wealth of authority painting a much different picture. In 1993, for example, the Federal Communications Act’s preemption provision was amended to provide that while state and local governments may not regulate the rates charged for cellular telephone service, the Act “shall not prohibit a State from regulating the other terms and conditions of commercial mobile services.” 47 U.S.C. § 332(c)(3)(A). The FCC itself has interpreted this section as follows:

We do not agree . . . that state contract or consumer fraud laws relating to the disclosure of rates and rate practices have generally been preempted with respect to [cellular providers]. Such preemption by Section 332(c)(3)(A) is not supported by its language or legislative history. . . . [T]he legislative history of Section 332 clarifies that billing information, practices and disputes—all of which might be regulated by state contract or consumer fraud laws—fall within “other terms and conditions” which states are allowed to regulate. Thus, state law claims stemming from state contract or consumer fraud laws governing disclosure of rates and rate practices are not generally preempted under Section 332.

In re Southwestern Bell Mobile Systems, Inc., 14 F.C.C.R. 19898, 19908 (Nov. 24, 1999) (footnotes omitted). The FCC’s consumer information website also makes clear, in its “commonly asked questions” section, that it does not regulate contractual matters between providers and customers:

I’m having billing problems with my cellular provider; who can help me?

The FCC does not regulate contractual arrangements with cellular providers, but does handle complaints about wireless service.

FCC Consumer & Governmental Affairs Bureau, <http://www.fcc.gov/cgb/cellular.html>.

Another federal district court, applying the Connecticut Unfair Trade Practices Act, found that

the Federal Communications Act expressly reserves to the states the ability to regulate "terms and conditions of commercial mobile services" other than their rates. 47 U.S.C. § 332(c)(3)(A). Therefore . . . , there is no alternative statutory scheme, either in Connecticut or at the federal level, to govern the non-rate setting business practices of [cellular] carriers.

In re Conn. Mobilecom, Inc., 2003 U.S. Dist. LEXIS 23063, at *15-16 (S.D.N.Y. Dec. 23, 2003).

Although this case is tangentially related to Defendant's rates, and state regulation of rates is preempted, 47 U.S.C. § 332(c)(3)(A), Plaintiff does not contest those rates generally. Rather, Plaintiff contends that Defendant double-billed him for a service he had already paid for. Thus, as described above, this is a dispute over Defendant's billing practices, an area over which the FCC has expressly arrogated to the states through laws such as the MCPA.

The "general transaction" at issue here was not "specifically authorized under laws administered by a regulatory board or officer acting under statutory authority of this state or the United States." Mich. Comp. Laws § 445.904(1)(a); *Smith*, 597 N.W.2d at 38. Therefore, Defendant's alleged misconduct is not exempt from the MCPA.

III. Conclusion

This case illustrates the importance of both the Michigan Consumer Protection Act and its class action mechanism. Because the class action waiver in Defendant's contract prevents the effective vindication of Plaintiff's statutory rights under the MCPA, it is

unenforceable. The parties have agreed that upon such a finding, this case shall not be subject to arbitration.

Being fully advised in the premises, having read the pleadings, and for the reasons set forth above, the Court hereby DENIES Defendant's Motion to Compel Arbitration.

s/Nancy G. Edmunds
Nancy G. Edmunds
United States District Judge

FILED AS ATTACHMENT
TO E-MAIL

Dated: July 20, 2006

I hereby certify that a copy of the foregoing document was served upon counsel of record on July 20, 2006, by electronic and/or ordinary mail.

s/Carol A. Hemeyer
Case Manager

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