9-2015

Section 4: Business Law

Institute of Bill of Rights Law, William & Mary Law School

IV. Business

In This Section:

Spokeo, Inc. v. Robins

13-1339

Ruling Below: *Robins v. Spokeo, Inc.*, 742 F.3d 409 (9th Cir. Cal. 2014)

The Circuit panel reversed the district court's dismissal, based on Article III standing, of an action alleging willful violations of the Fair Credit Reporting Act.

The panel held that the individual plaintiff had Article III standing to sue a website's operator under the Fair Credit Reporting Act for publishing inaccurate personal information about himself. The panel also held that law of the case did not limit the district court in its final order, and it was free to reconsider its own prior ruling on standing , where the district court had neither been divested of jurisdiction nor submitted this case to the jury.

Question Presented: Whether Congress may confer Article III standing upon a plaintiff who suffers no concrete harm, and who therefore could not otherwise invoke the jurisdiction of a federal court, by authorizing a private right of action based on a bare violation of a federal statute.

Thomas ROBINS, individually and on behalf of all others similarly situation
Plaintiffs
v.
SPOKEO, INC., a California corporation
Defendants

United States Court of Appeals for the Ninth Circuit

Decided on February 4, 2014

[Excerpt; some citations and footnotes omitted]

O'SCANNLAIN, Circuit Judge:

We must decide whether an individual has Article III standing to sue a website's operator under the Fair Credit Reporting Act for publishing inaccurate personal information about himself.

I

Spokeo, Inc. operates a website that provides users with information about other individuals, including contact data, marital status, age, occupation, economic health, and wealth level. Thomas Robins sued Spokeo for willful violations of the Fair Credit Reporting Act (FCRA), related to its website. Although he asserted that Spokeo's website contained false information about him, Robins's allegations of injury were sparse.

Spokeo moved to dismiss Robins's original complaint for lack of subject-matter jurisdiction on the ground that Robins lacked standing sufficient under Article III of the United States Constitution.

On January 27, 2011, the district court ruled that Robins had failed to allege an injury in fact because he had not alleged "any actual or imminent harm." The court characterized Robins's allegations as simply "that he has been unsuccessful in seeking employment, and that he is concerned that the inaccuracies in his report will affect his ability to obtain credit, employment, insurance, and the like." The district court noted that "[a]llegations of possible future injury do not satisfy the [standing] requirements of Art. III" and dismissed the complaint without prejudice.

Robins thereafter filed his First Amended Complaint (FAC). Similar to the original complaint, the FAC alleged willful violations of the FCRA. For example, the website allegedly described Robins as holding a graduate degree and as wealthy, both of which are alleged to be untrue. Robins, who is unemployed, described the misinformation as "caus[ing] actual harm to [his] employment prospects." Remaining unemployed has cost Robins money as well as caused "anxiety, stress, concern, and/or worry about his diminished employment prospects."

Again, Spokeo moved to dismiss for lack of subject-matter jurisdiction on the ground that Robins lacked standing under Article III. On May 11, the district court denied the motion and concluded that Robins had alleged a sufficient injury in fact, namely Spokeo's "marketing of inaccurate consumer reporting information about" Robins. The court also ruled that the injury was traceable to Spokeo's alleged violations of the FCRA and that the injury was redressable through a favorable court decision.

On September 19, after Spokeo moved to certify an interlocutory appeal, the district court reconsidered its previous ruling on standing. It then ruled, contrary to its May 11 order, that Robins failed to plead an injury in fact and that any injuries pled were not traceable to Spokeo's alleged violations, dismissing the action. Robins timely appealed.

II

On appeal, Robins first argues that the law-of-the-case doctrine prohibited the district court from revisiting its own May 11 decision. In *United States v. Smith*, however, we held that the law-of-the-case doctrine does not apply "to circumstances where a district court seeks to reconsider an order over which it has not been divested of jurisdiction." In this case, the district court was not divested of jurisdiction prior to its September 19 order.

Although *United States v. Alexander* held that the law-of-the-case doctrine precluded a district court from reconsidering an evidentiary issue after a mistrial, we distinguished *Alexander* in *Smith* and do so again here. The rule from *Alexander* applies only to cases in which a submission to the jury separates the two decisions.

Here, because the district court had neither been divested of jurisdiction nor submitted this case to the jury, it was free to reconsider its own prior ruling. The law-of-the-case doctrine did not limit the district court.

III

Robins next argues that the FAC sufficiently alleges Article III standing and that the May 11 ruling was correct. The FAC indeed alleges violations of various statutory provisions. Robins contends that because these provisions are enforceable through a private cause of action, they create statutory rights that he has standing to vindicate in court.

The district court properly recognized that it would not have subject-matter jurisdiction if Robins did not have standing. The district court also correctly identified the three components of standing: (1) the plaintiff "has suffered an 'injury in fact' that is (a) concrete and particularized and (b) actual or imminent, not conjectural or hypothetical";
(2) "the injury is fairly traceable to the challenged action of the defendant"; and (3) "it is likely, as opposed to merely speculative, that the injury will be redressed by a favorable decision." Although more may be required at later stages of the litigation, on a motion to dismiss, "general factual allegations of injury resulting from the defendant's conduct may suffice."

A

In standing cases that analyze statutory rights, our precedent establishes two propositions. First, Congress's creation of a private cause of action to enforce a statutory provision implies that Congress intended the enforceable provision to create a statutory right. Second, the violation of a statutory right is usually a sufficient injury in fact to confer standing.

Spokeo contends, however, that Robins cannot sue under the FCRA without showing actual harm. But the statutory cause of action does not require a showing of actual harm when a plaintiff sues for willful violations.

The scope of the cause of action determines the scope of the implied statutory right. When, as here, the statutory cause of action does not require proof of actual damages, a plaintiff can suffer a violation of the statutory right without suffering actual damages.

B

Of course, the Constitution limits the power of Congress to confer standing. This constitutional limit, however, does not prohibit Congress from "elevating to the status of legally cognizable injuries concrete, *de facto* injuries that were previously inadequate in law."

The issue before us is whether violations of statutory rights created by the FCRA are "concrete, *de facto* injuries" that Congress can so elevate. We are not the first Court of Appeals to face this question. In *Beaudry*, the Sixth Circuit considered whether an FCRA plaintiff suing under 15 U.S.C. § 1681n had sufficiently alleged an injury in fact by alleging a violation of the FCRA. The court identified two constitutional limitations on congressional power to confer standing. First, a plaintiff "must be 'among the injured,' in the sense that she alleges the defendants violated *her* statutory rights." Second, the statutory right at issue must protect against "individual, rather than collective, harm." The *Beaudry* court held that the plaintiff satisfied both of these requirements.

Robins is in the same position. First, he alleges that Spokeo violated *his* statutory rights, not just the statutory rights of other people, so he is "among the injured." Second, the interests protected by the statutory rights at issue are sufficiently concrete and particularized that Congress can elevate them. Like "an individual's personal interest in living in a racially integrated community" or "a company's interest in marketing its product free from competition," Robins's personal interests in the handling of his credit information are individualized rather than collective. Therefore, alleged violations of Robins's statutory rights are sufficient to satisfy the injury-infact requirement of Article III.

In addition to injury in fact, of course, standing requires causation and redressability. Where statutory rights are asserted, however, our cases have described the standing inquiry as boiling down to "essentially" the injury-in-fact prong. When the injury in fact is the violation of a statutory right that we inferred from the existence of a private cause of action, causation and redressability will usually be satisfied. First, there is little doubt that a defendant's alleged violation of a statutory provision "caused" the violation of a right created by that provision. Second, statutes like the FCRA frequently provide for monetary damages, which redress the violation of statutory rights. Therefore, Robins has adequately pled causation and redressability in this case.

IV

For the foregoing reasons, Robins adequately alleges Article III standing.

REVERSED AND REMANDED.

“9th Circuit Revives FCRA Suit Against Spokeo Site”

Law360
Kurt Orzeck
February 4, 2014

The Ninth Circuit on Tuesday revived a putative class action accusing “people search engine” Spokeo.com of willfully violating the Fair Credit Reporting Act by publishing false information about a Virginia man, saying he had constitutional standing to bring the complaint.

Reversing a California federal judge's dismissal of Thomas Robins' suit against Pasadena-based Spokeo Inc., which compiles information from various online and offline sources into reports and sells them to subscribers, the appeals court said the alleged violations of his statutory rights sufficiently satisfied Article III's injury-in-fact requirement.

Robins claimed he had suffered an actionable injury because the site provided prospective employers with inaccurate personal information about him and didn't exercise its responsibilities as a consumer reporting agency with fairness. He seeks to represent a class of individuals in a similar situation.

Spokeo attorneys countered that there was no allegation that “something scandalous” was spread about Robins or that he actually lost employment as a result of the allegedly inaccurate information.

The Ninth Circuit ruled Tuesday that a showing of actual harm isn't needed when a plaintiff sues for willful FCRA violations.

“The scope of the cause of action determines the scope of the implied statutory right. When, as here, the statutory cause of action does not require proof of actual damages, a plaintiff can suffer a violation of the statutory right without suffering actual damage,” the court said.

Robins filed suit in July 2010, alleging that a significant portion of the consumer report Spokeo had compiled about him was incorrect, including his employment status, marital status, age, educational background, number of children, “economic health” and “wealth level.” The profile also contained a picture of someone else, he claimed.

Spokeo violated the FCRA by failing to take reasonable steps to ensure that the information was accurate, according to the suit.

A California federal judge granted Spokeo's motion to dismiss in January 2011, citing lack of standing. He ruled that Robins had “failed to allege that defendant caused him any actual or imminent harm” and his allegations of possible future injury did not satisfy standing requirements.

Robins argued to the Ninth Circuit in November that U.S. District Judge Otis D. Wright II erred in finding that he hadn't alleged an injury-in-fact.

The three-judge panel agreed, saying Robins' personal interests in the handling of his credit information were individualized rather than collective, thus he had standing under Article III.

The Tuesday opinion also noted that Robins had adequately pled causation and redressability, which are also required for standing. The defendant's alleged violation of a FCRA statutory provision caused the violation of a right created by that provision, and the FCRA provides for monetary damages that redress statutory-right violations, according to the appeals court said.

Steven Woodrow of Edelson PC, which is representing Robins, told Law360 on Tuesday that the Ninth Circuit decision is a victory for consumer rights.

"The FCRA was passed because [the U.S.] Congress recognized that recklessly spreading false information about people to their potential creditors and employers is harmful in its own right and that consumers shouldn't have to prove the actual damages they've suffered," he said. "The opinion recognizes the same thing and gives thousands of job and credit seekers who've had false information reported about them their day in court."

"SCOTUS to Decide if 'Unharmed' Plaintiffs Have Right to Sue"

Reuters
Alison Frankel
April 27, 2015

Just about a year ago, the U.S. Supreme Court decided not to hear a case involving a class action against a couple of Midwestern banks that didn't post both of the required notices on its ATM machines. The banks' petition for certiorari raised the same question that had piqued the Supreme Court's interest in the 2011 case *First American Financial v. Edwards*: Can Congress confer constitutional standing on otherwise uninjured consumers by giving them a private right of action? But the justices mysteriously dismissed First American on the last day of their term in 2012 and were unwilling to revisit the tough question of Congress and consumers' right to sue in the ATM case, prompting me to ask in a column if the Supreme Court had lost its zeal to curb consumer class actions.

That may have been premature. On Monday, the justices granted the search site Spokeo's petition for certiorari in *Spokeo v. Robins*, a case in which the 9th U.S. Circuit Court of Appeals upheld the certification of a class of consumers who claimed Spokeo owes them statutory damages for violations of the Fair Credit Reporting Act. Spokeo's counsel of record, Andrew Pincus of Mayer Brown, framed the question presented as broadly as it was in Edwards and the ATM case: "Whether Congress may confer Article III standing upon a plaintiff who suffers no concrete harm, and who therefore could not otherwise invoke the jurisdiction of a federal court, by authorizing a private right of action based on a bare violation of a federal statute?"

As Mayer Brown emphasized in its petition – and as amici including eBay, Facebook and Google underscored – the Supreme Court's answer to that question will impact not just class actions brought under the Fair Credit Reporting Act but also cases citing the Telephone Consumers Protection Act, the Americans With Disabilities Act, the Truth in Lending Act and a half-dozen other federal laws authorizing consumers to sue for statutory damages. Big businesses have been complaining for years that these laws give plaintiffs and their lawyers an unfair advantage because they can assert statutory damages claims for hundreds of millions of dollars on behalf of thousands of consumers who suffered no concrete harm.

If the Supreme Court sides with Spokeo and holds that otherwise uninjured plaintiffs can't sue for money damages based on statutory violations, big businesses will have another reason to fete Pincus, whose 2011 high court win in *AT&T Mobility v. Concepcion* upheld the validity of mandatory arbitration clauses with class action waivers. "This is an important issue that the court should address and now it will," Pincus told me.

Pincus' opponent in the Spokeo case is Deepak Gupta of Gupta Beck – who also represented class members in the *Concepcion* case. In his brief opposing certiorari, Gupta argued both that the Supreme Court need not answer the abstract question Spokeo posed and that the named plaintiff in the class action against the search site had suffered actual harm when Spokeo published inaccurate personal information about him. (Among other things, the site said he was married when he was not.) Gupta was traveling and unavailable for comment but previously told me the distinction between injury-in-fact and injury-in-the-law is "philosophically incoherent."

In granting certiorari, the Supreme Court overruled the suggestion of the U.S. solicitor general, who argued against review of the case in a brief the justices solicited. The Justice Department – which had previously urged the Supreme Court not to take the 2011 *Edwards* case that the court ended up dismissing – walked back in the *Spokeo* brief from its argument that Congress has a broad right to a private right to sue. Instead, the SG's brief claimed that lawmakers can elevate rights grounded in common law to statutory causes of action. "De facto injuries that were previously inadequate in law" can be transformed by Congress into "legally cognizable injuries," according to the brief, when the law merely codifies longstanding principles of harm.

I'm expecting to see a lot of amicus firepower on both sides of the *Spokeo* case. The future of consumer class actions is at stake.

“Supreme Court Weighs Right to Sue in Spokeo Case”

The Wall Street Journal
Jacob Gershman
April 27, 2015

The Supreme Court on Monday agreed to hear a case that could potentially make it easier for plaintiffs to bring class-action lawsuits against Internet companies for allegedly violating consumer data and privacy laws.

The dispute involves a lawsuit against people-search site Spokeo Inc. over information it posted about an unemployed Virginia man. The plaintiff, Thomas Robins, says Spokeo got wrong details about his age, wealth, employment status and education level, portraying him as more educated and wealthier than he really was.

Those alleged errors, he claims, hurt his employment prospects, causing him “economic, reputational, and emotional” injuries. A trial court dismissed his case, a decision that the Ninth U.S. Circuit Court of Appeals reversed last year, ultimately landing the case in the country’s top court.

The lawsuit, which is seeking class action status, alleges violations of the Fair Credit Reporting Act, a federal law that regulates credits bureaus and sets standards over how consumer credit information is collected, stored and shared.

Lawyers for Spokeo deny the violations, arguing that they’re not a consumer reporting agency, but an Internet search engine, and thus fall outside the scope of the law. But they also argue that Mr. Robins doesn’t have the right to get a court to hear his case because he hasn’t suffered a concrete harm — a constitutional bar that plaintiffs must meet — but merely alleges “speculative anxiety and concern about what might happen.”

It’s that second argument that has piqued the high court’s interest.

Mr. Robins says his injuries are more than speculative. His lawyers say he has “clearly alleged concrete and particularized injuries: economic harm to his employment prospects.” But they go further, arguing that the alleged statutory violations themselves are a sufficient basis to get a day in court.

Deepak Gupta, an attorney for Mr. Robins, didn’t immediately have a comment on Monday. Mr. Robins is also represented by Edelson PC, a law firm founded by Jay Edelson, a class-action attorney who has made a career taking tech companies to court.

A ruling in favor of Mr. Robins could have huge implications for large Internet companies that have millions of users by carving out a more elastic right to sue and giving Congress more power to define the judiciary’s role in settling disputes.

While the specific lawsuit concerns Spokeo, tech companies like Google, Facebook and Yahoo are keeping a close eye on the case. A single violation of the federal consumer law can go up to $1,000, which could translate into a much bigger figure in a class action.

Spokeo, in a statement, said it's pleased that the high court "decided to consider this important constitutional issue raised by our petition: whether the Constitution permits class actions seeking millions or billions of dollars even though class members have not suffered any injury."

"No Injury? No Problem"

The National Law Review
Paul Scrudato, Brittany Robbins & Thomas Crispi
May 31, 2015

The Supreme Court recently granted certiorari in *Spokeo v. Robins*, a case that has the potential to redefine standing in federal court. The Ninth Circuit's February 2014 decision permitted plaintiff Thomas Robins to establish standing under the Fair Credit Reporting Act ("FCRA") with nothing more than a speculative injury. This contravenes Supreme Court precedent, which finds standing when a plaintiff suffers a harm that is actual, distinct, palpable, and concrete; attenuated and hypothetical injuries do not constitute an injury-in-fact. The implications of the Ninth Circuit's holding in *Spokeo v. Robins* has grabbed the attention of companies in nearly every industry. Their concern, as expressed by the U.S. Chamber of Commerce – granting standing to plaintiffs who have not suffered an injury-in-fact will open the flood gates to no-injury class actions brought under statutes that authorize a private right of action. But, in truth, the implications to businesses could extend beyond this.

Robins initiated a putative class action against Spokeo for violating the FCRA. Spokeo aggregates data from phone books, social networks, marketing surveys, real estate listings, business websites, and other sources into an online database. The FCRA regulates consumer information – including consumer credit information – that is collected, disseminated, and used in consumer reports. Spokeo allegedly posted false information about Robins' wealth, education, and marital status. Robins claims that these misrepresentations will negatively affect his credit, insurance and employment prospects. While the Ninth Circuit found that Robins had not suffered actual damages, it ultimately held that the statutory FCRA violation satisfied Article III's injury-in-fact requirement. The Supreme Court has granted cert to determine "[w]hether Congress can create Article III standing by authorizing a remedy for a bare statutory violation."

The FCRA engenders dozens of federal class actions each year. That number has jumped since the Ninth Circuit's decision — 29 FCRA class actions were filed in the first four months of 2014. Many federal statutes authorize a private right of action. For example, internet firms interact with millions of individuals and are subject to numerous federal statutes with private rights of action. Facebook, eBay, Google, and Yahoo! expressed concern in their amicus brief that, under the Ninth Circuit's holding, if any of these users was "willing (or enticed by a plaintiff's attorney) to allege that a generalized practice or act violated a law providing a private cause of action and statutory damages, then she could launch a putative class action on behalf of herself and millions of other 'similarly situated' users . . . [and] pursue a multi-billion dollar statutory damages claim despite the lack of injury . . . ."

What do no-injury class actions mean for manufacturers? It could mean lawsuits based on "defective products" that allegedly violate a state or federal statute but have not caused any harm. For example, the food and beverage and cosmetic industries are often accused of misleading consumers through false advertising, labeling, and packaging. ConAgra was sued under the Magnuson-Moss Warranty Act and state consumer protection laws for advertising its cooking oils, which were made from GMOs, were 100% natural. And Maybelline was sued under state consumer fraud and consumer protection acts because its "Super Stay" lipstick allegedly didn't stay on the advertised 10-14 hours. Under *Robins*, plaintiffs in these no-injury, statutory-based class actions would not need to establish that they were physically injured to survive a standing challenge. Will creative plaintiff lawyers be able to craft an argument that extends the no-injury standing rule in *Robins* to non-statutory violations?

The Sixth, Eighth, and Ninth Circuits permit statutory violations to confer standing whereas the Second, Fourth, and Federal Circuits require plaintiffs to prove an injury-in-fact. Tune in for oral arguments this Fall.

Federal Energy Regulatory Commission v. Electric Power Supply Association

14-840

Ruling Below: *FERC v. Electric Power Supply*, 753 F.3d 216 (D.C. Cir. 2014)

Electric Power Supply Association and four other energy industry associations ("Petitioners") petition the court for review of a final rule by the Federal Energy Regulatory Commission ("FERC" or "the Commission") governing what FERC calls "demand response resources in the wholesale energy market." The rule seeks to incentivize retail customers to reduce electricity consumption when economically efficient. Petitioners complain FERC's new rule goes too far, encroaching on the states' exclusive jurisdiction to regulate the retail market. The U.S. Court of Appeals, D.C. Circuit, ruled in favor of Petitioners, stating that FERC had overextended its reach, pursuant to 16 U.S.C.S. § 824(b)(1).

Question Presented: Whether the Federal Energy Regulatory Commission reasonably concluded that it has authority under the Federal Power Act, 16 U.S.C. 791a *et seq*., to regulate the rules used by operators of wholesale--electricity markets to pay for reductions in electricity consumption and to recoup those payments through adjustments to wholesale rates.

ELECTRIC POWER SUPPLY ASSOCIATION
Petitioner
v.
FEDERAL ENERGY REGULATORY COMMISSION
Respondent

The United States Court of Appeals, for the District of Columbia Circuit

Decided on May 23, 2014

[Excerpt; some footnotes and citations omitted]

BROWN. ***Circuit Judge*****:**

Under the Federal Power Act ("FPA" or "the Act") the Commission is generally charged with regulating the transmission and sale of electric power in interstate commerce. The FPA "split[s] [jurisdiction over the sale and delivery of electricity] between the federal government and the states on the basis of the type of service being provided and the nature of the energy sale." Section 201 of the Act empowers FERC to regulate "the sale of electric energy at wholesale in interstate commerce." Thus, "FERC's jurisdiction over the sale of electricity has been specifically confined to the wholesale market."

The Commission concedes that "demand response is a complex matter that lies at the confluence of state and federal jurisdiction." [Order 745]. For more than a decade, FERC has permitted demand-side resources to participate in organized wholesale markets, allowing Independent System Operators (ISOs) and Regional Transmission Organizations (RTOs) to use demand-side resources to meet their systems' needs for wholesale energy, capacity, and ancillary services. As this court has noted, Congress in 2005 declared "the policy of the United States that time-based pricing and other forms of demand response . . . shall be encouraged . . . and unnecessary barriers to demand response participation in energy, capacity and ancillary service markets shall be eliminated." The Commission has issued dozens of orders on demand-side resource participation, and ISOs and RTOs maintaining economic demand response programs could file tariffs with the Commission and accept bids for ancillary services and from aggregators of retail customers directly into the wholesale energy markets.

Order 745 establishes uniform compensation levels for suppliers of demand response resources who participate in the "day-ahead and real-time energy markets." The order directs ISOs and RTOs to pay those suppliers, including aggregators of retail customers, the full locational marginal price (LMP), or the marginal value of resources in each market typically used to compensate generators. The Commission conditioned the payment of full LMP on the ability of a demand response resource to replace a generation resource and required demand response to be cost effective. Cost effectiveness would be determined by a newly devised "net benefits test," which FERC directed ISOs and RTOs to implement. FERC acknowledged that the cost of payments to retail customers to encourage reduced energy consumption would have to be subsidized by load-serving entities participating in the wholesale market. Finally, the rule allocated the costs of demand response payments proportionally to all entities that purchase from the relevant energy markets during times when demand response resources enter the market. Commissioner Moeller dissented, arguing the Commission's retail customer compensation scheme conflicted both with FERC's efforts to promote competitive markets and with its statutory mandate to ensure supplies of electric energy at just, reasonable, and not unduly preferential or discriminatory rates.

Requests for rehearing and clarification were filed by ISOs, RTOs, state regulatory commissions, trade associations, publicly owned utilities, transmission owners, suppliers, and others. The Commission, in another 2–1 decision, confirmed its approach and Petitioners filed timely petitions for review.

The Administrative Procedure Act (APA) directs us to "hold unlawful and set aside agency action . . . in excess of statutory jurisdiction, authority, or limitations." "FERC is a creature of statute" and thus "has no power to act unless and until Congress confers power upon it." If FERC lacks authority under the Federal Power Act to promulgate a rule, its action is "plainly contrary to law and cannot stand."

We address FERC's assertion of its statutory authority under the familiar Chevron doctrine. The question is "whether the statutory text forecloses the agency's assertion of authority." If, however, the statute is silent or ambiguous on the specific issue, we must defer to the agency's reasonable construction of the statute.

FERC claims when retail consumers voluntarily participate in the wholesale market, they fall within the Commission's exclusive jurisdiction to make rules for that market. Petitioners protest that retail sales of electricity are within the traditional and "exclusive jurisdiction of the States" and regulating consumption by retail electricity customers is a regulation of retail, not wholesale, activity. The problem, Petitioners say, is the Commission has no authority to draw retail customers into the wholesale markets by paying them not to make retail purchases.

Initially, we note the regulations have a single definition of "demand response"—a "reduction in the consumption of electric energy by customers from their expected consumption in response to an increase in the price of electric energy or to incentive payments designed to induce lower consumption of electric energy." High retail rates will reduce demand. Conversely, if consumers are paid to reduce demand, prices fall. FERC acknowledges the first case, "price-responsive demand" is a "retail-level" demand response." In contrast, FERC dubs a reduction in the consumption of energy in response to incentive payments a "wholesale demand response." The Commission draws this distinction between "wholesale demand response" and "retail demand response" in an attempt to narrow the logical reach of its rule. Demand response resources do not actually sell into the market. Demand response does not involve a sale, and the resources "participate" only by declining to act.

As noted, and as the Commission concedes, demand response is not a wholesale sale of electricity; in fact, it is not a sale at all. Thus, FERC astutely does not rely exclusively on its wholesale jurisdiction under § 201(b)(1) for authority.

Instead, FERC argues §§ 205 and 206 grant the agency authority over demand response resources in the wholesale market. These provisions task FERC with ensuring "all rules and regulations affecting . . . rates" in connection with the wholesale sale of electric energy are "just and reasonable." Thus, the Commission argues it has jurisdiction over demand response because it "directly affects wholesale rates."

We agree with the Commission that demand response compensation affects the wholesale market. Because of the direct link between wholesale and retail markets, a change in one market will inevitably beget a change in the other. Reducing retail consumption—through demand response payments—will lower the wholesale price. Demand response will also increase system reliability. Because incentive-driven demand response affects the wholesale market in these ways, the Commission argues §§ 205 and 206 are clear grants of agency power to promulgate Order 745.

The Commission's rationale, however, has no limiting principle. Without boundaries, §§ 205 and 206 could ostensibly authorize FERC to regulate any number of areas, including the steel, fuel, and labor markets. FERC proposes the "affecting" jurisdiction can be appropriately limited to "direct participants" in jurisdictional wholesale energy markets. But, as this case demonstrates, the directness of participation may be a function of the richness of the incentives FERC commands. The commission's authority must be cabined by something sturdier than creative characterizations. The "direct participant" theory also assumes FERC can "lure" non-jurisdictional resources into the wholesale market in the first place to create jurisdiction, which is the heart of the Petitioners' challenge.

The limits of §§ 205 and 206 are best determined in the context of the overall statutory scheme. Congressional intent is clearly articulated in § 201's text: FERC's reach "extend[s] only to those matters which are not subject to regulation by the States."

States retain exclusive authority to regulate the retail market. Absent a "clear and specific grant of jurisdiction" elsewhere, the agency cannot regulate areas left to the states. The broad "affecting" language of §§ 205 and 206 does not erase the specific limits of § 201.1. Indeed, the Commission agrees its jurisdiction to regulate practices "affecting" rates does not "trump[] the express limitation on its authority to regulate non-wholesale sales." Otherwise, FERC could engage in direct regulation of the retail market whenever the retail market affects the wholesale market, which would render the retail market prohibition useless.

In addition, if FERC's arguments are followed to their logical conclusions, price-responsive demand response—retail demand response in "FERC speak"—would also affect jurisdictional rates in the same way as the type of demand response at issue in FERC's rule here, and FERC's authority regarding demand response would be almost limitless. Although the current rule leaves price-responsive demand untouched, nothing would stop FERC from expanding this regulation and encroaching further on state authority in the future.

Thus, FERC can regulate practices affecting the wholesale market under §§ 205 and 206, provided the Commission is not directly regulating a matter subject to state control, such as the retail market.

The fact that the Commission is only "luring" the resource to enter the market instead of requiring entry does not undercut the force of Petitioners' challenge. The lure is change of the retail rate. Demand response—simply put—is part of the retail market. It involves retail customers, their decision whether to purchase at retail, and the levels of retail electricity consumption. If FERC had directed ISOs to give a credit to any consumer who reduced its expected use of retail electricity, FERC would be directly regulating the retail rate. At oral argument, the Commission conceded crediting would be an impermissible intrusion into the retail market. Ordering an ISO to compensate a consumer for reducing its demand is the same in substance and effect as issuing a credit. Thus, while it is true demand response can occur in two ways—through a response to either price change or incentive payments—nothing about the latter makes it "wholesale." A buyer is a buyer, but a reduction in consumption cannot be a "wholesale sale." FERC's metaphysical distinction between price-responsive demand and incentive-based demand cannot solve its jurisdictional quandary.

Nor does FERC's reliance on a statement of congressional policy from the Energy Policy Act of 2005 save its rule. FERC insists its actions "are consistent with Congressional policy requiring federal level facilitation of demand response, because this final rule is designed to remove barriers to demand response participation in the organized wholesale energy markets FERC's reliance on this language is perplexing; if anything, the policy statement supports the opposite conclusion, that Congress intended demand response resources to be regulated by states, as part of the retail market.

The Energy Policy Act of 2005 confirms the national policy of encouraging and facilitating "the deployment of [time-based pricing and other demand response] technology and devices that enable electricity customers to participate in such pricing and demand response systems . . . and [eliminating] unnecessary barriers to demand response participation in energy, capacity and ancillary service markets." As an initial matter, even if § 1252(f) supports FERC's authority, the Commission cannot rely on the section for an independent source of power. Policy statements like § 1252(f) "are just that—statements of policy. They are not delegations of regulatory authority." Thus, the relevant sections of the Energy Policy Act of 2005 can only be used to "help delineate the contours of statutory authority." And here, those contours do not encompass federal regulation of demand response.

FERC latches onto the language in § 1252(f) requiring elimination of "unnecessary barriers to demand response participation in energy . . . service markets" to support its claim that Order 745 advances congressional policy. In Order 745, however, FERC went far beyond removing barriers to demand response resources. Instead of simply "removing barriers," the rule draws demand response resources into the market and then dictates the compensation providers of such resources must receive.

We think the title of the section is noteworthy: "Federal *Encouragement* of Demand Response Devices." "To encourage" is not "to regulate." Although the title is "not dispositive of the provision's meaning," "it is not too much to expect that it has something to do with the subject matter" of the section. And here, "review of the statutory text reveals that [the title] has everything to do with the subject matter." See id. The section dictates demand response is to be "encouraged" and "facilitated," not directly regulated as Order 745 proposes.

This is obvious when § 1252(f) is read in tandem with § 1252(e), "Demand Response and Regional Coordination," which declares it the "policy of the United States to encourage States to coordinate, on a regional basis, State energy policies to provide reliable and affordable demand response services to the public." This language underscores that states, not the Commission, regulate demand response. Indeed, § 1252(e) goes on to note FERC should "provide technical assistance to States and regional organizations . . . in . . . developing plans and programs to use demand response to respond to peak demand or emergency needs." The Commission is also to prepare an annual report, assessing demand response resources. Thus, the Energy Policy Act clarifies FERC's authority over demand response resources is limited: its role is to assist and advise state and regional programs.

Even more importantly, the Energy Policy Act statements show Congress understood the importance of demand response resources to the wholesale market—an importance Petitioners do not dispute. Yet, despite this significant impact on the wholesale market, Congress left regulation of this aspect of retail demand up to the states, rather than to the federal government.

Because the Federal Power Act unambiguously restricts FERC from regulating the retail market, we need not reach Chevron step two. But even if we assumed the statute was ambiguous—as Judge Edwards argues, we would find FERC's construction of it to be unreasonable for the same reasons we find the statute unambiguous. Because FERC's rule entails direct regulation of the retail market—a matter exclusively within state control—it exceeds the Commission's authority.

Alternatively, even if we *assume* FERC had statutory authority to execute the Rule in the first place, Order 745 would still fail because it was arbitrary and capricious.

Under the APA, we must set aside orders that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." In particular, "it most emphatically remains the duty of this court to ensure that an agency engage the arguments raised before it."

A review of the record reveals FERC failed to properly consider—and engage—Commissioner Moeller's reasonable (and persuasive) arguments, reiterating the concerns of Petitioners and other parties, that Order 745 will result in unjust and discriminatory rates. Moeller argued Order 745 "overcompensat[es]" demand response resources because it "requires that demand resource[s] be paid the full LMP plus be allowed to retain the savings associated with [the provider's] avoided retail generation cost." The Commission then responded that demand response resources are comparable to generation resources and should therefore receive the same level of compensation. Yet comparable contributions cannot be the reason for equal compensation, when generation resources are incomparably saddled with generation costs. Nor can FERC justify its current overcompensation by pointing to past undercompensation. Although we need not delve now into the dispute among experts, the potential windfall to demand response resources seems troubling, and the Commissioner's concerns are certainly valid. Indeed, "overcompensation cannot be just and reasonable," and the Commission has not adequately explained how their system results in just compensation.

The Commission cannot simply talk around the arguments raised before it; reasoned decisionmaking requires more: a "direct response," which FERC failed to provide here. Thus, if FERC thinks its jurisdictional struggles are its only concern with Order 745, it is mistaken. We would still vacate the Rule if we engaged the Petitioners' substantive arguments.

Ultimately, given Order 745's direct regulation of the retail market, we vacate the rule in its entirety as *ultra vires* agency action.

For the reasons set forth above, we vacate and remand the rulings under review.

So ordered.

EDWARDS, *Senior Circuit Judge*, dissenting:

Under the Federal Power Act, regulatory authority over the nation's electricity markets is bifurcated between the States and the federal government. In simplified terms, the Federal Energy Regulatory Commission ("FERC" or "Commission") has authority over wholesale electricity sales but not retail electricity sales, with the latter solely subject to State regulation. The consolidated petitions before the court call on us to parse this jurisdictional line between FERC's wholesale jurisdiction and the States' retail jurisdiction – a line which this court and the Supreme Court have recognized is neither neat nor tidy.

Petitioners challenge Order 745, a rule imposing certain compensation requirements on the administrators of the nation's wholesale electricity markets. The rule requires these wholesale-market administrators – called Regional Transmission Organizations ("RTOs") and Independent System Operators ("ISOs") – to compensate so-called "demand response resources" at a specified price when certain conditions are met. As relevant here, "demand response resources" are essentially electricity consumers, often bundled together by a third-party aggregator, who agree to reduce their electricity consumption in exchange for incentive payments. The pun scattered throughout the record is that while generators produce megawatts, consumers produce "negawatts." In effect, Order 745 requires that, at certain times, megawatts and negawatts receive the same amount of payment in wholesale markets, an amount called the "locational marginal price" or "LMP."

Although the challenged rule requires ISOs and RTOs to pay demand response resources a specified compensation (LMP), this requirement is applicable only when two conditions are met: (1) when the demand response resource is capable of balancing supply and demand in the wholesale market, and (2) when compensating the demand response resource is cost-effective under a "net benefits test" prescribed by the rule. The specific mechanics of these conditions and of the "net benefits test" are less important than what they accomplish. The critical point here is that, because of the specified conditions, Order 745 requires compensation of demand response resources *only when* their participation in a wholesale electricity market actually lowers the market-clearing price for wholesale electricity.

With these basics in hand, it is easy to see why FERC stated in its rulemaking that "jurisdiction over demand response is a complex matter that lies at the confluence of state and federal jurisdiction." On one view, the demand response resources subject to the rule directly affect the wholesale price of electricity. That is, the final rule's conditions operate to ensure that every negawatt of forgone consumption receiving compensation reduces both the quantity of electricity produced and its wholesale price. Focusing on this direct effect – direct, it bears repeating, because under the rule's conditions *all* demand response resources receiving compensation reduce the market-clearing price – it is easy to conceive of Order 745 as permissibly falling on the *wholesale* side of the wholesale-retail jurisdictional line. On another view, however, the electricity not consumed thanks to the rule's compensation payments would have been consumed first in a retail market.

Focusing on the market in which the consumption *would have occurred* in the first instance, one can conceive of Order 745 as impermissibly falling on the *retail* side of the jurisdictional line.

The task for this court, of course, is not to divine from first principles whether a demand response resource subject to Order 745 is best considered a matter of wholesale or retail electricity regulation. Rather, our task is one of statutory interpretation within the familiar *Chevron* framework. The Commission has interpreted the Federal Power Act to permit it to issue Order 745. And it falls to this court to determine whether the Act unambiguously "sp[eaks] to the precise question," (Chevron step one), and, if not, whether the Commission's interpretation is a permissible construction of the statute (Chevron step two).

Though the rule and its operation are highly technical, the primary jurisdictional issue raised in these consolidated petitions turns on a rather straightforward question of statutory interpretation: whether a promise to forgo consumption of electricity that would have been purchased in a retail electricity market unambiguously constitutes a "sale of electric energy" under section 201(b)(1) of the Federal Power Act. 16 U.S.C. § 824(b)(1). If so, the Commission lacked jurisdiction to issue Order 745 because section 201(b)(1) of the Act states, in relevant part, that the "provisions of this subchapter shall apply . . . to the sale of electric energy at wholesale in interstate commerce, but . . . *shall not apply to any other sale of electric energy*."

The statute, to my mind, is ambiguous regarding whether forgone consumption constitutes a "sale" under section 201(b)(1). Because of this ambiguity, the Act is also ambiguous as to whether a rule requiring administrators of wholesale markets to pay a specified level of compensation for such forgone consumption constitutes "direct regulation" of retail sales that would contravene the limitations of section 201. Because the Act is ambiguous regarding FERC's authority to require ISOs and RTOs to pay demand response resources, we are obliged to defer under *Chevron* to the Commission's permissible construction of "a statutory ambiguity that concerns the scope of the agency's statutory authority (that is, its jurisdiction)."

Absent an affirmative limitation under section 201, there is no doubt that demand response participation in wholesale markets and the ISOs' and RTOs' market rules concerning such participation constitute "practice[s] . . . affecting" wholesale rates under section 206 of the Act. Petitioners' arguments to the contrary ignore the direct effect that the ISOs' and RTOs' market rules have on wholesale electricity rates squarely within FERC's jurisdiction. The Commission has authority to "determine the just and reasonable . . . practice" by setting a level of compensation for demand response resources that, in its expert judgment, will ensure that the rates charged in wholesale electricity markets are "just and reasonable." It was therefore reasonable for the Commission to conclude that it could issue Order 745 under the Act's "affecting" jurisdiction.

In addition to challenging FERC's jurisdiction, Petitioners argue that its decision to mandate compensation equal to the LMP was arbitrary and capricious. Petitioners believe that the LMP overcompensates demand response resources since they also realize savings from not having to purchase retail electricity. The Commission, Petitioners insist, should have set the compensation level at the LMP minus the retail cost of the forgone electricity. But the Commission's decision in this regard was reasonable and adequately explained.

For these reasons, explained below in greater detail, I respectfully dissent.

I. BACKGROUND

A. The Problem

To understand this case, one must appreciate the scope and significance of the problem FERC sought to address in Order 745. Three characteristics of the nation's electricity market go a long way toward framing the problem. *First*, electricity, unlike most commodities, cannot be stored for later use. There must instead be a continual, contemporaneous matching of supply to meet current electricity demand. *Second*, not all power plants are created equal: some are efficient and cheap; others, inefficient and expensive. *Third*, most retail consumers are charged a fixed price for electricity that does not adjust in the moment to temporary spikes in the cost of producing electricity.

The first two characteristics, in tandem, cause significant fluctuations in the cost of supplying electricity at different times of day. During periods of regular electricity consumption, only the efficient and cheap power plants need be deployed. But at hours of peak usage (*e.g.*, a summer afternoon in Washington, D.C. when countless air conditioners toil against the humidity and heat), the suppliers of electricity must marshal the least efficient and most costly power plants to match the soaring demand for electricity. It is because electricity cannot be efficiently stored that these periods of peak demand must be met with new generation and not stockpiled supply.

In a perfect market, or even in a well-functioning market, the skyrocketing cost of producing additional electricity at hours of peak usage would be reflected in temporarily higher prices charged to consumers. In turn, this increased price would reduce the megawatts of electricity demanded, as some individuals and businesses would, for example, turn off their air conditioners to save money. The market would thereby reach an efficient equilibrium.

But here is where the third characteristic of electricity markets comes in. Retail electricity prices are generally regulated to remain constant over longer periods of time. That is, consumers do not pay different amounts during different hours of the day, notwithstanding the sharply vacillating cost of producing electricity. Electricity demand thus does not respond to time-sensitive price signals. As a result, there are times when people and businesses consume electricity that costs more to produce than it is worth to them to consume. This is inefficient.

Wholesale electricity markets, which are under FERC's jurisdiction, suffer the same inefficiency. Since retail demand is not price-responsive, the aggregate amount of electricity demanded in the wholesale market by the entities that serve retail customers is also uncoupled from the time-specific price of supplying electricity. In economic terms, the demand for electricity in the wholesale market is inelastic.

The Commission recognizes the problem. As it observed in its order denying requests for rehearing of Order 745,

> [a] properly functioning market should reflect both the willingness of sellers to sell at a price and the willingness of buyers to purchase at a price. In an RTO- or ISO-run market, however, buyers are generally unable to directly express their willingness to pay for a product at the price offered. As discussed later, RTOs and ISOs cannot isolate individual buyers' willingness to pay which results in extremely inelastic demand.

B. FERC's Solution

Having identified a problem in the wholesale electricity market, the Commission has a statutory obligation to do what it can to fix it. That is because FERC is charged under the Federal Power Act with ensuring that wholesale electricity rates are "just and reasonable." It must ensure that all "rates and charges made, demanded, or received by any public utility for *or in connection with* the . . . sale of electric energy subject to the jurisdiction of the Commission" are "just and reasonable." And when FERC determines that a "practice . . . affecting" such a rate is unjust or unreasonable, it must itself determine and fix "the just and reasonable . . . practice . . . to be thereafter observed."

Consistent with its statutory duty and in view of the market distortions caused by inelastic wholesale demand, the Commission has initiated a series of reforms to open wholesale markets to "demand response resources." For our purposes, "demand response resources" are resources that are capable of reducing "the consumption of electric energy by customers from their expected consumption in response . . . to incentive payments designed to induce lower consumption of electric energy." Put simply, demand response resources agree not to purchase electricity in exchange for payment.

The basic premise of FERC's demand-response reforms is that there are two ways that wholesale-market administrators (*i.e.*, ISOs and RTOs) can balance wholesale supply and demand: by increasing the supply of electricity or by decreasing the demand for it. An ISO or RTO reduces wholesale demand when it pays a demand response resource because that resource will forgo electricity consumption in the retail market, which, in turn, will lead to fewer megawatts of electricity being demanded in the aggregate in that ISO's or RTO's wholesale market. At certain times (*e.g.*, summer afternoons in Washington, D.C.), paying incentive payments to induce consumers not to consume electricity may be cheaper than paying generators to produce more power; negawatts, in such circumstances, are the cheaper alternative. And because, functionally, there is little difference to wholesale-market administrators between a megawatt and a negawatt (both assist equally in the administrator's task of bringing wholesale demand and supply into equipoise), demand response resources are capable of competing directly with traditional generation resources so long as the appropriate market rules are in place.

For some years now, FERC has recognized that the direct participation of demand response resources in wholesale markets improves the functioning of these markets in several respects. First, it lowers wholesale prices because "lower demand means a lower wholesale price." Second, it mitigates the market power of suppliers of electricity because they have to compete with demand response resources and adjust their bidding strategy accordingly. Third, demand response "enhances system reliability," for example, by "reducing electricity demand at critical times (e.g., when a generator or a transmission line unexpectedly fails)."

The benefits of demand response participating in wholesale markets are beyond reproach. Commissioner Moeller, who dissented in Order 745, put it best:

> While the merits of various methods for compensating demand response were discussed at length in the course of this rulemaking, nowhere did I review any comment or hear any testimony that questioned the benefit of having demand response resources participate in the organized wholesale energy markets. On this point, there is no debate. The fact is that demand response plays a very important role in these markets by providing significant economic, reliability, and other market-related benefits.

It is no surprise, then, that FERC has initiated a series of reforms to open up its markets to demand response, on the theory that doing so helps to ensure "just and reasonable" wholesale rates by improving how these markets function in the three ways just mentioned.

In particular, in Order 719 FERC required ISOs and RTOs to "accept bids from demand response resources in RTOs' and ISOs' markets for certain ancillary services on a basis comparable to other resources" and, in certain circumstances, to "permit an aggregator of retail customers . . . to bid demand response on behalf of retail customers directly into the organized energy market." But FERC placed an important condition on this requirement; ISOs and RTOs were required to accept bids from demand response "unless not permitted by the laws or regulations of the relevant electric retail regulatory authority." Finally, recognizing that "further reforms may be necessary to eliminate barriers to demand response in the future," FERC further ordered ISOs and RTOs to "assess and report on any remaining barriers to comparable treatment of demand response resources that are within the Commission's jurisdiction."

And further reforms were indeed necessary. Prior to issuing Order 745, ISOs and RTOs had differing practices concerning the level of compensation to be paid to demand response resources in their markets. The Commission found that many ISOs and RTOs undercompensated demand response resources in certain circumstances. It reached this finding in light of existing barriers to demand response participation in wholesale markets, including "the lack of market incentives to invest in enabling technologies that would allow electric customers and aggregators of retail customers to see and respond to changes in marginal costs of providing electric service as those costs change."

Order 745 sought to correct the undercompensation problem by mandating that ISOs and RTOs pay demand response resources the same market price that they pay to generators, *i.e.,* LMP. But it limited this compensation requirement to circumstances where two specific conditions are met. LMP-compensation would be required only when (1) "the demand response resource [is] able to displace a generation resource in a manner that serves the RTO or ISO in balancing supply and demand," and (2) "the payment of LMP . . . [is] cost-effective, as determined by [a] net benefits test."

FERC understood that it had authority to correct the undercompensation problem because, in the absence of adequate compensation, too few demand response resources affirmatively bid into the wholesale markets. And such participation is necessary for the market to function rationally and reach "just and reasonable" rates. As FERC stated:

> We find, based on the record here that, when a demand response resource has the capability to balance supply and demand as an alternative to a generation resource, and when . . . paying LMP to that demand response resource is shown to be cost-effective as determined by the net benefits test described herein, payment by an RTO or ISO of compensation other than the LMP is unjust and unreasonable. When these conditions are met, we find that payment of LMP to these resources will result in just and reasonable rates for ratepayers.

II. ANALYSIS
A. Jurisdiction

Petitioners argue that Order 745 is "in excess" of FERC's "statutory jurisdiction." We evaluate this contention under *Chevron* and defer to FERC's permissible construction of its authorizing statute, regardless of "whether the interpretive question presented is 'jurisdictional.'" The proper question is thus whether the Act *unambiguously* forecloses FERC from issuing Order 745 under its "affecting" jurisdiction.

FERC's explanation of its jurisdiction under the Federal Power Act is straightforward and sensible. FERC has the authority and responsibility to correct any "practice . . . affecting" wholesale electricity rates that the Commission determines to be "unjust" or "unreasonable." In its view, the ISOs' and RTOs' rules governing the participation of demand response resources in the nation's wholesale electricity markets are "practices affecting [wholesale electricity] rates." That is, an ISO's or RTO's market rules governing how a demand response resource may compete in its wholesale market, including the terms by which a demand response resource is to be compensated in the market, are "practices affecting" that wholesale market's rates for electricity. And FERC has determined that an ISO's or RTO's "practice" is unjust and unreasonable to the degree that it inadequately compensates demand response resources capable of supplanting more expensive generation resources. As explained above, FERC has found that demand response improves the functioning of wholesale markets by (1) lowering the wholesale price of electricity, (2) exerting downward pressure on generators' market power, and (3) enhancing system reliability.

FERC's explanation is consistent with our case law. In *Connecticut*, we considered whether FERC has jurisdiction to review an ISO's capacity charges. Capacity is not electricity but the ability to produce it when needed, and in *Connecticut* the ISO had established a market where capacity providers – generators, prospective generators, and demand response resources – competitively bid to meet the ISO's capacity needs three years in the future. Generation, like retail sales, is expressly the domain of State regulation under section 201, and the petitioners argued that by increasing the overall capacity requirement the ISO was improperly requiring the installation of new generation resources. We disagreed and held that FERC had "affecting" jurisdiction under section 206 because "capacity decisions . . . affect FERC-jurisdictional transmission rates for that system without directly implicating generation facilities." That the capacity requirement helped to "find the right price" was enough of an effect to satisfy section 206.

Petitioners' specific arguments against FERC's exercising jurisdiction are unpersuasive. *First*, Petitioners note that section 201 of the Act establishes a clear jurisdictional line between "the sale of electric energy at wholesale in interstate commerce," which is properly the subject of FERC's jurisdiction, and "any other sale of electric energy." According to Petitioners, the Commission has transgressed this line because it "has ordered ISOs and RTOs to pay *retail customers* for reducing their retail purchases of electricity."

But this argument mischaracterizes the rule and papers over a key ambiguity. First, the mischaracterization: Petitioners are wrong inasmuch as they imply that FERC requires *all* ISOs and RTOs to pay demand response resources a minimum level of compensation (LMP). The compensation requirement promulgated in Order 745 does not apply unless an ISO or RTO "has a tariff provision permitting demand response resources to participate as a resource in the energy market." And the regulation's requirement that ISOs and RTOs accept bids from demand response resources comes with a key caveat: the requirement applies "unless not permitted by the laws or regulations of the relevant electric retail regulatory authority." In other words, there is a carve-out from the compensation requirement for ISOs and RTOs in States where local regulatory law stands in the way. Thus, the Order preserves

State regulation of retail markets. This is hardly the stuff of grand agency overreach.

More fundamentally, Petitioners' argument founders on a statutory ambiguity they ignore. Section 201 makes clear that FERC may regulate "the *sale* of electric energy at wholesale in interstate commerce" but not "any other sale of electric energy." (emphasis added). The demand response at issue here is forgone consumption, which is no "sale" at all. Perhaps the phrase "any other sale of electric energy" could be interpreted to include *non*-sales that *would have been* sales in the retail market, but it certainly does not *require* such a reading. It is reasonable to categorize demand response as neither a retail sale nor wholesale sale under the Federal Power Act. And on this understanding, section 201 "says nothing about" FERC's power to review compensation rates for demand response in wholesale electricity markets.

Nor is Petitioners' argument under section 201 made any stronger by reference to subsection (a). This prefatory subsection states that while "Federal regulation . . . of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest," federal regulation should "extend only to those matters which are not subject to regulation by the States." But the Supreme Court has made clear that "the precise reserved state powers language in § 201(a)" is a "*mere policy declaration* that cannot nullify a clear and specific grant of jurisdiction, *even if the particular grant seems inconsistent with the broadly expressed purpose.*"

The most that can be said of section 201 is that it commits regulation of retail *sales* to the States and regulation of wholesale *sales* to the Commission. And while it is true that the forgone consumption would have been purchased in the first instance in the retail market, it does not follow from this fact that non-consumption constitutes an "other sale" under section 201(b). There was no sale, period. And the statute does not give a clear indication that Congress intended to foreclose FERC from regulating non-sales that have a direct effect on the wholesale markets under FERC's jurisdiction.

Even assuming that the Federal Power Act requires demand response resources to be considered inextricably part of retail "sales" subject solely to State regulation, Order 745 does not engage in the type of "direct regulation" that would violate section 201. Order 745 does not require anything of retail electricity consumers and leaves it to the States to decide whether to permit demand response. All Order 745 says is that *if* a State's laws permit demand response to be bid into electricity markets, and *if* a demand response resource affirmatively decides to participate in an ISO's or RTO's wholesale electricity market, and if that demand response resource would in a particular circumstance allow the ISO or RTO to balance wholesale supply and demand, and *if* paying that demand resource would be a net benefit to the system, *then* the ISO or RTO must pay that resource the LMP. That is it. This requirement will no doubt affect how much electricity is consumed by a small subset of retail consumers who elect to participate as demand response resources *in wholesale markets*. But that fact does not render Order 745 "direct regulation" of the retail market. Authority over retail rates and over whether to permit demand response remains vested solely in the States.

In this respect, Order 745 is similar to the capacity rule in *Connecticut* that we found did not directly regulate generation facilities. Even though increasing the capacity requirement incentivized the procurement of additional resources, including new generation facilities, to meet the higher requirement, we recognized that States retained their ultimate authority over the construction of new generation facilities. And because the capacity requirements could be met in other ways aside from building new generators (*e.g.*, through demand response or capacity contracts), it was irrelevant that "public utilities . . . overwhelmingly responded to [increased capacity requirements] by choosing to allow construction of new facilities over other alternatives." The lesson of *Connecticut* is that FERC can indirectly incentivize action that it cannot directly require so long as it is otherwise acting within its jurisdiction – and that doing so does not constitute impermissible direct regulation of an area reserved to the States. So too here: Order 745 may encourage more demand response, but States retain the ultimate authority to approve the practice.

Second, Petitioners argue that the FERC's "affecting" jurisdiction under sections 205 and 206 of the Act "does not extend so far as to allow the Commission to regulate directly the retail services that are expressly carved out from the scope of its jurisdiction." To a large degree, this argument simply rehashes Petitioners' erroneous reading of section 201 and fails for the reasons just described. Demand response resources are promises to forgo consumption of electricity and therefore are not retail "sales." This is not changed by the fact that forgone consumption would have taken place in the first instance in a retail market. Because of this, the Commission's asserting "affecting" jurisdiction over demand response does not, as Petitioners suggest, "nullify[]" a limitation set forth in section 201.

To be sure, section 206 cannot be read to displace *unambiguous* jurisdictional limits imposed by section 201(b). Suppose, for example, that FERC issued a rule requiring ISOs and RTOs to condition all wholesale sales of electricity on load-serving entities' agreeing to charge retail customers with real-time pricing that adjusted hourly for variations in the cost of producing electricity. Such a rule would unambiguously regulate each retail "sale" because it would mandate a particular form of compensation for *actual* – not counterfactual – retail sales. Thus, while price-responsive retail pricing would no doubt "affect" the wholesale rate, FERC could not claim jurisdiction under sections 205 and 206 because the subchapter which includes these sections "shall not apply to any other sale of electric energy." This example plainly differs from the present case because demand response resources are forgone sales or non-sales, and therefore it is at best ambiguous whether the limitation in section 201(b) applies.

To bolster their case, Petitioners invoke the specter of limitless federal authority if FERC is permitted to exercise "affecting" jurisdiction to issue Order 745. They caution that "the Commission's expansive interpretation of its 'affecting' jurisdiction would allow it to regulate any number of activities – such as the purchase or sale of steel, fuel, labor, and other inputs influencing the cost to generate or transmit electricity – merely by redefining the activities as 'practices' that affect wholesale rates."

This argument cannot carry the day because it ignores at least two important limits. It first ignores section 201's limit proscribing any "direct regulation" of retail sales (which would bar the hypothetical rule, discussed above, in which FERC tries to mandate that retail sales have dynamic, time-responsive pricing). It also ignores the limitations we announced in *CAISO*. There, we held that FERC exceeded its jurisdiction when it replaced the board members of an ISO on the theory that the composition of the ISO's board was a "practice . . . affecting [a] rate" under section 206(a). We held that "section 206's empowering of the Commission to assess the justness and reasonableness of practices affecting rates of electric utilities is limited to those methods or ways of doing things on the part of the utility that *directly affect* the rate or are closely related to the rate, not all those remote things beyond the rate structure that might in some sense indirectly or ultimately do so."

These limits foreclose the parade of horribles marshaled by Petitioners. Like replacing the ISO's board of directors in *CAISO*, FERC could not, consistent with Circuit precedent, regulate markets in steel, fuel, labor, and other inputs for generating electricity, which constitute "remote things beyond the rate structure that might in some sense indirectly or ultimately" affect the wholesale rate of electricity.

Order 745 passes the *CAISO* test quite comfortably because the demand response resources subject to the rule have a quintessentially "direct" effect on wholesale rates. The rule's compensation requirement applies *only when* an ISO or RTO can use the demand response resource in lieu of a generation resource to balance supply and demand, *and only when* paying a demand response resource is cost-effective under the rule's net benefits test. Order 745 thus does not purport to regulate demand response writ large; its compensation requirement applies only when the demand response by definition alters the wholesale electricity price. That is about as "direct" an effect and as clear a "nexus" with the wholesale transaction as can be imagined. There can be little doubt that FERC has the authority to review the justness and reasonableness of rates that are so closely connected with the healthy functioning of its jurisdictional markets; this, as we said in *Connecticut*, is the "heartland of the Commission's section 206 jurisdiction."

Third, Petitioners argue that the Commission's orders exceed its jurisdiction because "they unreasonably interfere with existing state and local programs addressing retail customer 'demand response.'" Any such effect, however, is merely incidental. As the Commission correctly observed, Order 745 "does not directly affect retail-level demand response programs, nor does it require that demand response resources offer into the wholesale market only. Indeed, the organized wholesale energy markets can and do operate simultaneously with retail-level programs . . . .” FERC’s reforms in Order 745 run on a parallel track with State-level reforms. And to the degree that FERC’s reforms incidentally affect parallel State-level initiatives, that does not render FERC’s actions improper.

* * *

To summarize: FERC’s jurisdiction turns on two issues: (1) whether demand response is a retail “sale” or is otherwise unambiguously committed to State regulation under the Federal Power Act, and (2) whether sections 205 and 206 clearly grant jurisdiction to FERC to regulate how wholesale-market administrators compensate demand response resources that “directly affect” wholesale prices. Unless we inject quasi-philosophy into our *Chevron* analysis (what is the sound of one hand clapping? what is the true nature of a sale that was never made? of megawatts never consumed?), I think it clear that the Federal Power Act does not precisely address the first question; forgone consumption is not unambiguously a “sale,” nor does the statute dictate that demand response be treated solely as a matter of retail regulation. And the second question is resolved, in my view, by the terms of Order 745 which narrowly apply *only* to demand response resources that by definition directly affect the wholesale rates of electricity. This falls squarely within the Commission’s “affecting” jurisdiction. The proper course for this court is to defer to the Commission’s well-reasoned and permissible interpretation of its authority under the statute.

B. Level of Compensation

Petitioners also argue that Order 745 is arbitrary and capricious under 5 U.S.C. § 706(2)(A). In reviewing such claims, we consider whether FERC “examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choice made.” We also afford significant deference to FERC in light of the highly technical regulatory landscape that is its purview. Indeed, “the Commission enjoys broad discretion to invoke its expertise in balancing competing interests and drawing administrative lines.” And we “afford great deference to the Commission” in cases involving ratemaking decisions as the “statutory requirement that rates be ‘just and reasonable’ is obviously incapable of precise judicial definition.” Finally, to the extent that the Commission bases its actions on factual findings, such findings are conclusive if supported by substantial evidence.

Petitioners’ chief complaint is that Order 745 sets the required compensation level for demand response at the LMP (recall: locational marginal price). LMP equals “the marginal value of an increase in supply or a reduction in consumption at each node within” an ISO’s or RTO’s wholesale market, and is the compensation generation resources generally receive. Petitioners complain that demand response resources already get the benefit of the forgone expense of retail electricity (abbreviated in the record as “G”). Therefore, Petitioners contend that, under FERC’s rule, demand response resources effectively receive a “double payment”: LMP plus G. Br. of Pet’rs at 47. According to Petitioners, requiring LMP compensation thus results in unjust and discriminatory overcompensation of demand response resources.

It is of course true, as the majority observes, that FERC is "bounded by the requirements of reasoned decisionmaking." Therefore, FERC was required to provide a "direct response" to the Petitioners' and the dissenting Commissioner's concerns about overcompensation. This is precisely what the Commission did in carefully explaining how Order 745's setting compensation at the LMP was neither discriminatory nor unjust.

To begin with, FERC provided a thorough explanation for why compensating demand response at the LMP (and not LMP - G) was neither unjust nor over-compensatory. It explained that such compensation was necessary to encourage an adequate level of demand response participation in wholesale markets in light of existing market barriers. That last part – the market barriers – is the key. The Commission has identified numerous barriers preventing adequate participation of demand response in wholesale markets. Indeed, citing record evidence, the Commission explained that "the inadequate compensation mechanisms in place today in wholesale energy markets fail to induce sufficient investment in demand response resource infrastructure and expertise that could lead to adequate levels of demand response procurement." FERC further explained that "a lack of incentives to invest in enabling technologies can be addressed by making additional investment resources available to market participants" and that paying LMP "to demand response will provide the proper level of investment resources available for capital improvements." In view of these barriers, and the value of demand response participation to ensuring "just and reasonable" wholesale rates, the Commission concluded that LMP was the appropriate level of compensation.

FERC sums it up well:

> The Commission acknowledged that noted experts differed on whether paying LMP in the current circumstances facing the wholesale electric market is a reasonable price. In determining that LMP is the just and reasonable price to pay for demand response, the Commission examined some of the previously recognized barriers to demand response that exist in current wholesale markets. These barriers create an inelastic demand curve in the wholesale energy market that results in higher wholesale prices than would be observed if the demand side of the market were fully developed. The Commission found that paying LMP when cost-effective may help remove these barriers to entry of potential demand response resources, and, thereby, help move prices closer to the levels that would result if all demand could respond to the marginal price of energy.

With respect to the argument that utilizing the LMP is somehow discriminatory because incomparable resources are paid comparable amounts, the Commission offered reasonable grounds for treating demand response as comparable to generation resources. The Commission observed that, from the perspective of an ISO or RTO, a demand response resource was comparable to a generation resource inasmuch as demand response is equally capable of balancing wholesale supply and demand. This is not the sum total of the explanation, however. In the same section of its order, the Commission explained that "examining cost avoidance by demand response resources is not consistent with the treatment of generation. In the absence of market power concerns, the Commission generally does not examine each of the costs of production for individual resources participating as supply resources in the organized wholesale electricity markets." FERC continued: "we note that certain generators may receive benefits or savings in the form of credits or in other forms. In these cases, the generators realize a value of LMP plus the credit or savings, but ISOs or RTOs do not take such benefits or savings into account in determining how much to pay those resources." The point is that the comparability of compensation is assessed without regard to outside costs and credits; just as two generators are both compensated at the LMP even though only one might be receiving a tax credit for producing energy, so too with comparing demand response resources to generation resources. This was clearly explained, and it is reasonable.

This court has no business second-guessing the Commission's judgment on the level of compensation.

Whatever policy disagreements one might have with Order 745's decision to compensate demand response resources at the LMP (and there are legitimate disagreements to be had), the rule does not fail for want of reasoned decisionmaking. FERC's judgment is owed deference because it has put forth a reasonable multi-step explanation of its decision to mandate LMP compensation. First, responsive demand is a necessary component of a well-functioning wholesale market, and FERC understood that its obligation to ensure just and reasonable rates required it to facilitate an adequate level of demand response participation in its jurisdictional markets. Second, FERC concluded that market barriers were inhibiting an adequate level of demand response participation. Third, FERC concluded that mandating LMP would provide the proper incentives for demand response resources to overcome these barriers to participation in the wholesale market.

III. CONCLUSION

FERC had jurisdiction to issue Order 745 because demand response is not unambiguously a matter of retail regulation under the Federal Power Act, and because the demand response resources subject to the rule directly affect wholesale electricity prices. And the Commission's decision to require compensation equal to the LMP, rather than LMP - G, was not arbitrary or capricious. The majority disagrees on both points. The unfortunate consequence is that a promising rule of national significance – promulgated by the agency that has been authorized by Congress to address the matters in issue – is laid aside on grounds that I think are inconsistent with the statute, at odds with applicable precedent, and impossible to square with our limited scope of review. I therefore respectfully dissent.

“Supreme Court to Rule on Breaks for Cutting Peak-Demand Energy Use”

The Washington Post
Robert Barnes & Chris Mooney
May 4, 2015

The Supreme Court announced Monday that it will review whether a federal agency may require electric market operators to compensate customers who lower their consumption of electricity during peak demand hours.

The court said it would determine whether the Federal Energy Regulatory Commission (FERC) exceeded its statutory authority when in 2011 it adopted the approach, which is called “demand response.”

Environmentalists, the Obama administration and some large consumers say demand response is a key mechanism for getting people to use less energy overall and, therefore, producing fewer emissions of carbon dioxide or other harmful pollutants.

Total electricity demand varies greatly, and when it peaks — usually in the afternoon or evening each day, but also seasonally, such as on very hot days — power companies have to bring additional power plants online to service that peak load.

In doing so, the companies address the need for more electricity by adding more supply. But demand response also can reduce how much power people or companies use during these peak times.

FERC’s rule would have ensured that companies or individuals get compensated for voluntarily reducing their power usage at peak demand. “A market functions effectively only when both supply and demand can meaningfully participate,” FERC noted in promulgating the rule.

The agency also said in its brief to the Supreme Court, “Demand response, by decreasing the amount of power necessary to balance supply and demand, reduces the risk of system failures like blackouts and curbs the market power of generators.”

Electricity generators say that FERC’s proposed compensation is too generous and, more importantly, is a power grab that exceeds the authority Congress has given it.

“The Federal Power Act draws a ‘bright line’ distinction between state and federal jurisdiction over the regulation of sales of electric power,” said a brief filed by the Electric Power Supply Association, of which NRG Energy and Exelon Corp. are members.

Wholesale sales of electricity are subject to FERC’s jurisdiction, the association asserts, while retail sales are the exclusive province of the states.

A panel of the U.S. Court of Appeals for the District of Columbia Circuit agreed with the electricity producers on a 2-to-1 vote.

"Demand response — simply put — is part of the retail market," wrote Circuit Judge Janice Rogers Brown. "It involves retail customers, their decision whether to purchase at retail, and the levels of retail electricity consumption."

The Obama administration, supported by environmentalists and some large consumers, asked the Supreme Court to reconsider.

"To the extent demand response reduces prices, which we believe it does, all consumers benefit," says Steven Nadel, executive director of the American Council for an Energy-Efficient Economy.

A supporting brief filed by a group of large power consumers, including Alcoa and the University of Maryland at College Park, said that the benefits extend beyond those who take advantage of the program.

"Demand response benefits all end-use consumers by eventually reducing their electricity prices by billions of dollars per year," the brief said. "It also provides a reliable and effective mechanism for balancing the grid when demand spikes."

Justice Samuel A. Alito Jr. recused himself from the case, presumably because of a financial conflict. That means the case will be heard by an eight-member court in the term that begins in October, and a tie vote would keep the lower court's ruling in place.

The combined cases are *FERC v. Electric Power Supply Association* and *EnerNOC v. Electric Power Supply Association*.

“FERC Gets Top U.S. Court Hearing on Energy-Conservation Rule”

Bloomberg
Greg Stohr & Jonathan Crawford
May 4, 2015

The Obama administration will get a U.S. Supreme Court hearing as it tries to save a rule that rewards industrial consumers for cutting electricity use.

The rule, opposed by the power industry, benefits smart-grid companies such as EnerNOC Inc. that help large electricity consumers reduce their power usage during peak-demand hours. It’s also backed by large power consumers, including Alcoa Inc. and Wal-Mart Stores Inc., that are eyeing millions of dollars in energy savings.

A federal appeals court said the Federal Energy Regulatory Commission lacked authority to issue the rule. It requires wholesale-market operators to pay electricity users that cut consumption during high-demand periods at the same rate as generators that produce power. The practice, known as “demand response,” means stiffer competition for generators.

“It’s going to lead to a fair amount of uncertainty for quite some time,” William Scherman, a former FERC general counsel who now leads the energy, regulation and litigation practice at Gibson, Dunn & Crutcher LLP in Washington, said Monday by phone.

The court will consider the case in the nine-month term that starts in October, with arguments likely in November or December, and a decision by June 2016. FERC’s payment rule remains in effect.

Rejection of the rule would widen profits for NRG Energy Inc., FirstEnergy Corp., Exelon Corp., Dynegy Inc. and American Electric Power Co., the companies with the most wholesale electricity sales in PJM Interconnection LLC’s mid-Atlantic grid, Bloomberg Intelligence analyst Kit Konolige wrote in a note to clients Monday.

Mid-Atlantic Grid

The 13-state grid, which has the highest amount of demand response of all the regional markets, paid $17.7 million for consumers to cut their electricity use in 2014, according to Monitoring Analytics LLC, based in Eagleville, Pennsylvania, which oversees the market.

Advocates of demand response say it can cut air pollution and reduce the need to build additional power plants. Demand response helped the grid maintain reliable service when the system faced potential supply shortages during the Polar Vortex in January 2014, according to PJM.

“It’s a great day for demand response and consumers across the country,” Frank Lacey, a vice president at Comverge Inc., a demand-response company based in Norcross, Georgia, said in a phone interview. “We believe the court will hold that demand response is rightfully within the jurisdiction of FERC and consumers will continue to save billions of dollars annually because of the decision."

Power plant owners that opposed the FERC plan say it is too generous to energy consumers.

FERC's Authority

The court fight centers on the reach of FERC's authority. Federal law lets the commission regulate rates only at the wholesale level, leaving retail regulation in the hands of the states.

FERC and the Obama administration contend that the rule applies only to wholesale rates and to demand-response providers that are participating in that market. A divided federal appeals court in Washington rejected that reasoning, saying that demand response by definition "involves retail customers, their decision whether to purchase at retail and the levels of retail electricity consumption."

That appeals court decision was poised to take effect and void the rule had the Supreme Court not intervened.

Alito Recusal

Justice Samuel Alito didn't participate in the court's action today. As is customary, Alito gave no reasons, though his most recent financial-disclosure form indicated he owned at least $100,000 of OGE Energy Corp., a wholesale power company based in Oklahoma City.

Assuming Alito doesn't take part in the case, the administration will have to win the votes of five of the other eight justices to save the rule.

PJM said Monday it will include demand response in a power-capacity auction, expected to take place by August.

The auction will cover the 12 months starting in June 2018. Capacity auctions are intended to give power-plant owners an incentive to have their generators ready to run when needed. Aggregators of demand response also can be paid for assuring that customers are ready to shut down equipment or lights, reducing the need for plants to run.

"The demand response case being reviewed by the Supreme Court involves the energy market specifically. If the court applies the decision also to the capacity markets, as the generators have asked, as much as $100 million of annual net income would be at stake for Exelon," Konolige said.

The high court also will consider whether the appeals court was right to say FERC didn't adequately weigh whether the rule will lead to unjust rates.

The Supreme Court also will hear a related appeal filed by companies including EnerNOC and Johnson Controls Inc.'s EnergyConnect unit.

The cases are *FERC v. Electric Power Supply Association*, 14-840, and *EnerNOC v. Electric Power Supply Association*, 14-841.

“Electric Power Supply Ass’n v. FERC”

Harvard Law Review
March 10, 2015

The Federal Power Act splits jurisdiction over the electricity system between the Federal Energy Regulatory Commission (FERC), which regulates the wholesale market and transmission, and state regulators, which have authority over retail markets. However, the seeming clarity of this jurisdictional divide has been muddied by the recent advent of “demand response,” in which consumers are paid for reducing their energy consumption. Recently, in Electric Power Supply Ass’n v. FERC (EPSA), the D.C. Circuit vacated a FERC order that attempted to regulate the wholesale prices paid for demand response, on the basis that the order was beyond FERC’s jurisdiction due to its impermissible effect on retail markets. The breadth of the court’s holding risks confusion in the energy markets and unnecessarily limits FERC’s regulatory options.

Demand response offers a partial solution to inefficiencies in the electricity market. The typical organizational model for the electricity market makes a division between wholesale and retail sectors. The regional systems relevant to this case are run by “system operators,” independent entities responsible for ensuring that energy supplied in the system’s wholesale market meets the demand in the system’s retail market. Because the demand for electricity is not constant, at times of high demand system operators must buy power at high prices from less efficient generators. Due to the unresponsive nature of retail prices, consumers have little incentive to reduce consumption during these peak-demand periods. Demand response offers a partial solution. At times of peak consumption, system operators can reduce the overall cost of electricity in the system by paying consumers or groups of consumers, dubbed “demand response resources” (DRRs), to reduce their energy consumption.

FERC’s Order 745 attempted to address perceived problems with the compensation of demand response in the wholesale market. Though FERC had previously issued orders governing the structure of this market as a whole, Order 745 specifically addressed payments to DRRs. FERC found that the rates paid to DRRs by some electric system operators were too low to adequately incentivize the development of demand response. The Order mandated that, in certain circumstances, a system operator must pay to DRRs the same price for a forgone megawatt of consumption that the system operator would have paid a generator that had successfully bid that megawatt into the wholesale market. After notice and comment, Order 745 was passed by four of FERC’s five board members over the dissent of Commissioner Moeller. The Commission received numerous requests for rehearing, which it denied. Electric Power Supply Association, a trade group of power suppliers, petitioned the D.C. Circuit for review.

The D.C. Circuit vacated Order No. 745. Writing for the court, Judge Brown found that FERC had exceeded the bounds of its jurisdiction in issuing Order 745, and that Order 745 was "arbitrary and capricious." To analyze FERC's claim that it had jurisdiction over wholesale demand response, Judge Brown outlined the relevant statutory provisions. The Act contains two sources of agency power, and two prohibitions, relevant to the court's decision. Section 201(b)(1) grants FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce," but not over "any other sale," which is the domain of the states. Sections 205 and 206 contain a broad ancillary grant of power over "'all rules and regulations affecting . . . rates' in connection with the wholesale sale of electric energy." Finally, section 201(a) states that "FERC's reach 'extend[s] only to those matters which are not subject to regulation by the States.'" To determine whether FERC had jurisdiction to regulate the wholesale price of demand response, the court recognized that it must apply the Chevron test, determining first "whether the statutory text forecloses the agency's assertion of authority," and, if instead the statute was "silent or ambiguous," deferring to "the agency's reasonable construction."

The court began by analyzing the jurisdictional grants. FERC did not have jurisdiction under the "sale . . . at wholesale" language of section 201(b)(1) because demand response is a non-sale. Next, the court considered FERC's argument that it had jurisdiction under the sections 205 and 206 authorization to regulate practices "directly affect[ing] wholesale rates." The court accepted that wholesale demand response directly affects wholesale prices, but found that the Commission's characterization of its "affecting" jurisdiction "ha[d] no limiting principle," "could ostensibly authorize FERC to regulate . . . the steel, fuel, and labor markets," and would allow the agency to "'lure' non-jurisdictional resources into the wholesale market . . . to create jurisdiction" by requiring generous compensation.

To provide a limiting principle for sections 205 and 206, the court turned to the "overall statutory scheme." Noting that under section 201(a), FERC's "reach 'extend[s] only to those matters which are not subject to regulation by the States,'" the court reasoned that "[t]he broad 'affecting' language of §§ 205 and 206 does not erase the specific limits of § 201. Such limits could not come from section 201(b)(1)'s exclusion from regulation of "any other sale": demand response is not a sale. Instead, the "statutory scheme as a whole" showed that demand response, "while not necessarily a retail sale, is indeed part of the retail market, which . . . is exclusively within the state's jurisdiction." Finding that the Act unambiguously foreclosed FERC jurisdiction, the D.C. Circuit invalidated Order 745.

The court also held that the agency had acted arbitrarily and capriciously in issuing Order 745. FERC had failed, in light of Commissioner Moeller's "persuasive" argument that "overcompensation cannot be just and reasonable," to "adequately explain[]

how [Order 745] results in just compensation."

Judge Edwards dissented. He agreed that Order 745 appeared to fall under FERC's "affecting" jurisdiction, but thought that the limit the D.C. Circuit had previously read into sections 205 and 206 — that FERC could regulate only conduct with "direct" effects on wholesale prices — was sufficient. Because wholesale demand response directly affects wholesale prices, Order 745 was a valid exercise of FERC's "affecting" jurisdiction unless barred by section 201(b)(1)'s preclusion of FERC regulation of "any other sale of electric energy." As demand response could be reasonably construed not to be a sale, section 201(b)(1) did not unambiguously preclude regulation. Moreover, section 201(a) could not control because the Supreme Court had previously interpreted it to be a "mere policy declaration." As the Act did not speak unambiguously to the precise question of whether demand response was a retail sale, *Chevron* deference to FERC's interpretation of the jurisdictional grant was required.

Although the majority established new limits on sections 205 and 206, the preexisting limits of the Act and case law adequately cabined FERC's jurisdiction. The existence of these limits, the paucity of statutory grounding for a limiting principle, and the availability of an alternative holding all should have counseled the court either to have avoided announcing a limiting principle at all or to have delineated the limits of sections 205 and 206 more narrowly. Even assuming that FERC had overstepped in this instance, the potential breadth of the court's holding has caused uncertainty in the industry and has unduly foreclosed the possibilities of beneficial regulation.

The statutory grounding for the court's limiting principle was shaky; by looking to the "statutory scheme," the court derived a limiting principle from two provisions, neither of which would have provided that restriction alone. Although section 201(a) appears an appealing candidate to supply limits to FERC's jurisdiction, Supreme Court precedent forecloses this possibility. Section 201(a) "declare[s] that . . . Federal regulation . . . [is] to extend only to those matters which are not subject to regulation by the States." However, it begins a section entitled "[d]eclaration of policy; application of subchapter," and the Supreme Court has determined section 201(a) to be a "mere 'policy declaration.'" Had the court sought a jurisdictional limit in section 201(a) alone, the decision to deny Chevron deference to FERC would have been difficult to support: while (as the court recognized) a specific limit should trump a general grant of jurisdiction, it is not clear that section 201(a), a statement "of great generality," would *unambiguously* trump the general language of sections 205 and 206, even in light of a separate "retail sale" limit in section 201(b)(1). The court's reading of section 201(a) as part of a statutory scheme setting internal, implicit limits on sections 205 and 206 ignored the section's status as a general policy declaration.

Likewise, the court could not have relied solely upon section 201(b)(1)'s denial of

FERC jurisdiction over "any other sale[s]" than those "at wholesale." The problem in using section 201(b)(1) to limit the grant of "affecting jurisdiction" in sections 205 and 206 is that the plain meaning will not easily support it — section 201(b)(1) speaks of retail and wholesale "sales," not markets. A reliance on section 201(b)(1) to supply limits would also have been in tension with the court's own earlier reading of an identical term. The term "sale" is used both to grant and to limit FERC jurisdiction within the same sentence of section 201(b)(1): "[The Commission's jurisdiction] shall apply to . . . the sale of electric energy at wholesale in interstate commerce, but . . . shall not apply to any other sale of electric energy . . . ." In dismissing FERC's claim of section 201(b)(1) authority, the court relied on the plain meaning of "sale": "[D]emand response is not a wholesale sale of electricity; in fact, it is not a sale at all." If section 201(b)(1) were construed to limit FERC's jurisdiction over the retail market, it should logically also be construed to grant authority over the wholesale market. Because demand response falls somewhere between the two, section 201(b)(1) would not unambiguously preclude FERC regulation of wholesale demand response.

The court's search for limits led to a principle derived from the statutory scheme that nonetheless is in tension with the rest of the statute. As the court acknowledged, the plain text of sections 205 and 206 supports jurisdiction. Further, it is difficult to find in the statutory scheme a clear intent against demand response, which did not exist at the time of the Act's passage. In New York v. FERC, the Supreme Court made the same point about another emergent phenomenon, "unbundled transmissions." The Court reasoned that because unbundled transmissions "ha[d] been a recent development" and "ha[d] never been 'subject to regulation by the States,'" section 201(a) did not preclude FERC jurisdiction. The same argument applies to demand response — an emergent phenomenon not previously subject to state regulation.

The court had several options besides broadly holding that FERC lacks jurisdiction over demand response, even if it did not want to follow Judge Edwards in deferring to the agency. The fact that the court arrived at the alternative holding that Order 745 was arbitrary and capricious meant that the court did not need to reach the jurisdictional question at all. An alternative would have been to rule the present regulation ultra vires on very narrow grounds. In particular, the court recognized that FERC's "lur[ing]" of customers from the retail to the wholesale market through preferential rates was "the heart of the Petitioners' challenge. The court could have found that this way of attracting customers made the regulation an impermissible intrusion on the retail markets. Such a finding would have enabled the court to address the conduct that most troubled the petitioners, while still leaving room for wholesale demand response that did not distort retail customers' incentives.

The capaciousness of the court's decision to locate demand response unambiguously within the retail "market" has the potential to lead to jurisdictional confusion. As the case itself demonstrates, regulation that occurs at the first instance in the wholesale market can now be ruled ultra vires if it has an impermissibly direct effect on the retail market (unless it directly regulates a wholesale sale of electric energy). This result is problematic, given the court's recognition that "a change in one market will inevitably beget a change in the other." The development of both new technologies and FERC's regulatory program means that questions that do not neatly fall in one or the other of section 201(b)(1)'s categories are likely to arise more often. Already, FERC's entire system of wholesale demand response, widely agreed to be beneficial, is being challenged in a FERC hearing.

In EPSA, the court turned to the statutory scheme to infer a limiting principle that the provisions of the Federal Power Act taken individually did not provide. Given the statute's limitations for supplying such a principle, the court should have moved more carefully to limit the upheaval caused by its holding and to allow FERC greater room to maneuver in the face of technological change in the energy sector.

Tyson Foods Inc. v. Bouaphakeo

14-1146

Ruling Below: *Bouaphakeo v. Tyson Foods Inc*., 765 F.3d 791 (8th Cir. Iowa 2014)

Peg Bouaphakeo and other named plaintiffs are employees of Tyson Foods, Inc. They represent a class of employees at Tyson's meat-processing facility in Storm Lake, Iowa. They sued Tyson for not paying wages due under the Fair Labor Standards Act of 1938 (FLSA), 29 U.S.C. § 201 et seq., and the Iowa Wage Payment Collection Law (IWPCL), Iowa Code 91A.1 et seq. A jury returned a verdict for the class. Tyson appeals. Having jurisdiction under 28 U.S.C. § 1291, this court affirms.

Question Presented: (1) Whether differences among individual class members may be ignored and a class action certified under Federal Rule of Civil Procedure 23(b)(3), or a collective action certified under the Fair Labor Standards Act, where liability and damages will be determined with statistical techniques that presume all class members are identical to the average observed in a sample. (2) Whether a class action may be certified or maintained under Rule 23(b)(3), or a collective action certified or maintained under the Fair Labor Standards Act, when the class contains hundreds of members who were not injured and have no legal right to any damages.

Peg BOUAPHAKEO; Javier Frayre; Jose A. Garcia; Mario Martinez; Jesus A. Montes; Heribento Renteria, on behalf of themselves and all other similarly situated individuals, Plaintiffs–Appellees
v.
TYSON FOODS, INC.,
Defendant–Appellant

The United States Court of Appeals, Eighth Circuit

Decided on August 25, 2014

[Excerpt; some citations and footnotes omitted]

Before SMITH, BEAM, and BENTON, Circuit Judges.

I

The employees are current and former "gang-time" employees at Tyson's facility. The background is similar to that in *Lopez v. Tyson Foods, Inc.*, (adapted to the facts of this case):

To calculate the employees' compensable working time, Tyson measures "gang time"—when the employees are at their working stations and the production line is moving. The employees claim Tyson failed to provide FLSA overtime compensation for donning (putting on) personal protective equipment (PPE) and clothing before production and again after lunch, and for doffing (taking off) PPE and clothing before lunch and again after production. The PPE and clothing worn by individual employees vary depending on their role in the process. Tyson classifies items of PPE and clothing as either "unique" or "non-unique" to the meat-processing industry. The employees also seek compensation for transporting the items from lockers to the production floor.

In addition to "gang time," Tyson adds "K-code" time to each employee's paycheck. Before 2007, Tyson paid four minutes of K-code time per day to each [employee in a department where knives were used] in order to compensate for the donning and doffing of unique items. From [February] 2007 to [June] 2010, Tyson added [several minutes] per day for pre-and post-shift walking time required of the employee. Tyson does not record the actual time that employees perform any of these tasks.

The FLSA prohibits the employment of any person "for a workweek longer than forty hours unless such employee receives compensation for his employment in excess of the hours above specified at a rate not less than one and one-half times the regular rate at which he is employed." An employee who sues for unpaid overtime "has the burden of proving that he performed work for which he was not properly compensated." At one time, the Supreme Court defined work as "physical or mental exertion (whether burdensome or not) controlled or required by the employer and pursued necessarily and primarily for the benefit of the employer and his business." The Court then "clarified that 'exertion' was not in fact necessary for an activity to constitute 'work' under the FLSA."

Whether an employee's activity is "work" does not end the compensability analysis. In the Portal–to–Portal Act, Congress excluded some activities that might otherwise constitute work from the FLSA. The Act accepts two categories:

> (1) walking, riding, or traveling to and from the actual place of performance of the principal activity or activities which such employee is employed to perform, and
>
> (2) activities which are preliminary to or postliminary to said principal activity or activities, which occur either prior to the time on any particular workday at which such employee commences, or subsequent to the time on any particular workday at which he ceases, such principal activity or activities.

The Department of Labor has a "continuous workday rule," generally defining an employee's "workday" as "the period between the commencement and completion on the same workday of an employee's principal activity or activities." During the continuous workday, the compensability of all activities that otherwise satisfy the requirements of the FLSA is not affected by the Portal–to–Portal Act's exceptions. In *Alvarez*, the Supreme Court held that "during a continuous workday, any walking time that occurs after the beginning of the employee's first principal activity and before the end of the employee's last principal activity is excluded from the scope of [the Portal–to–Portal Act], and as a result is covered by the FLSA."

The employees sued in 2007, claiming that Tyson's K-code time was insufficient to cover compensable pre- and post-production line activities, violating the FLSA and IWPCL. The district court certified the FLSA claim as a collective action and the IWPCL claim as a Rule 23 class action. During a nine-day trial, plaintiffs proved liability and damages by using individual timesheets, along with average donning, doffing, and walking times calculated from 744 employee observations. The jury returned a verdict for the class of $2,892,378.70. With liquidated damages, the final judgment totaled $5,785,757.40.

II

Tyson argues that the district court erred in certifying the FLSA collective action—under 29 U.S.C. § 216(b)—and the IWPCL class—under Rule 23. Class certification is reviewed for abuse of discretion. A district court may certify a class under Rule 23(b) if "questions of law or fact common to class members predominate over any questions affecting only individual members," and "a class action is superior to other available methods for fairly and efficiently adjudicating the controversy." The FLSA allows named plaintiffs to sue "for and in behalf of themselves and other employees similarly situated." Plaintiffs may be similarly situated when "they suffer from a single, FLSA-violating policy, and when proof of that policy or of conduct in conformity with that policy proves a violation as to all the plaintiffs." A court may consider "(1) disparate factual and employment settings of the individual plaintiffs; (2) the various defenses available to defendant which appear to be individual to each plaintiff; [and] (3) fairness and procedural considerations."

According to Tyson, factual differences between plaintiffs-differences in PPE and clothing between positions, the individual routines of employees, and variation in duties and management among departments-make class certification improper. These differences, Tyson says, do not allow the class action to "generate common answers apt to drive the resolution of the litigation." *Wal–Mart Stores, Inc. v. Dukes*. Unlike *Dukes*, Tyson had a specific company policy—the payment of K-code time for donning, doffing, and walking—that applied to all class members. Unlike *Dukes*, class members worked at the same plant and used similar equipment. The time study showed that donning and doffing all equipment, plus walking, took an average of 18 minutes in the fabrication department and 21 minutes in the kill department. True, applying Tyson's K-code policy and expert testimony to "generate . answers" for individual overtime claims did require inference, but this inference is allowable under *Anderson v. Mt. Clemens Pottery Co*. While individual plaintiffs varied in their donning and doffing routines, their complaint is not "dominated by individual issues" such that "the varied circumstances . prevent 'one stroke' determination." The district court did not abuse its discretion in certifying the class.

Tyson also contends that the class should be decertified because evidence at trial showed that some class members did not work overtime and would receive no FLSA damages even if Tyson under-compensated their donning, doffing, and walking. Tyson exaggerates the authority for its contention.

At any rate, at Tyson's request, the jury was instructed, "Any employee who has already received full compensation for all activities you may find to be compensable is not entitled to recover any damages." Tyson's instruction directed the jury to treat plaintiffs with no damages as class members. It is "fundamental that where the defendant . 'invited error' there can be no reversible error."

III.

Tyson believes that plaintiffs improperly relied on a formula to prove liability. In Dukes, the Supreme Court disapproved of "Trial by Formula."

A sample set of the class members would be selected, as to whom liability for sex discrimination and the back-pay owing as a result would be determined in depositions supervised by a master. The percentage of claims determined to be valid would then be applied to the entire remaining class, and the number of (presumptively) valid claims thus derived would be multiplied by the average backpay award in the sample set to arrive at the entire class recovery-without further individualized proceedings.

Here, plaintiffs do not prove liability only for a sample set of class members. They prove liability for the class as a whole, using employee time records to establish individual damages. Using statistics or samples in litigation is not necessarily trial by formula.

Plaintiffs do rely on inference from average donning, doffing, and walking times, but they apply this analysis to each class member individually. Using this representative evidence is comparable to a jury applying testimony from named plaintiffs to find classwide liability. For the donning, doffing, and walking in *Mt. Clemens*, testimony from eight employees established liability for 300 similarly situated workers. To prove damages, the Court remanded for "the determination of the amount of walking time involved and the amount of preliminary activities performed" based on "whatever reasonable inferences can be drawn from the employees' evidence."

Tyson claims that plaintiffs presented insufficient evidence to prove damages classwide. This court "will not reverse a jury verdict for insufficient evidence unless 'after viewing the evidence in the light most favorable to the verdict, [it concludes] that no reasonable juror could have returned a verdict for the non-moving party.'" Tyson has no evidence of the specific time each class member spent donning, doffing, and walking. "[W]hen an employer has failed to keep proper records, courts should not hesitate to award damages based on the 'just and reasonable inference' from the evidence presented."

To prove damages, plaintiffs use individual timesheets, along with average times calculated from a sample of 744 observations of employee donning, doffing, and walking. Plaintiffs' expert testified that the sample was large for this type of study, representative, and approximately random. He testified that the study used “accepted procedure in industrial engineering.” Tyson's Director of Human Resources testified that K-code time did not include the donning and doffing of much non-unique PPE. Pay data—which came directly from Tyson—showed the amount of K-code time each individual received. Sufficient evidence existed to support a “reasonable inference” of class-wide liability.

Tyson asserts that even if sufficient evidence supported damages, plaintiffs' claims still fail because it is uncertain if any uncompensated work was performed, citing *Carmody v. Kansas City Board of Police Commissioners* only applies where the existence of damages is certain. Anderson allows uncertainty only for the amount of damages.”). In *Carmody*, the plaintiffs did not “produce[ ] evidence indicating any hours worked over forty hours per week . were never paid.” The plaintiffs “did not provide any evidence of actual damages because the testimony contained no reference to overtime hours that violated the FLSA.” Here, Tyson stipulates that “workers at the Storm Lake plant tend to work a significant amount of overtime on a weekly basis.” Plaintiffs show uncompensated overtime work by applying average donning, doffing, and walking times to employee timesheets. The evidence is “susceptible to [the] reasonable inference” that the jury's verdict is correct.

The judgment is affirmed.

BENTON, Circuit Judge, dissenting.

For two independent but somewhat factually related reasons, this case should be reversed, remanded and dismissed. First, under the circumstances of this litigation, neither the putative Fair Labor Standards Act (FLSA) collective action (the so-called federal class) nor the purported Iowa Wage Payment Collection Law (IWPCL) Rule 23(b)(3) class (the so-called state class) were eligible for class certification, either as a matter of fact or a matter of law. Second, Rule 23 state-law-based class actions are fundamentally different than collective actions authorized under the FLSA and may not be procedurally homogenized for trial as done in this case.

I. BACKGROUND

This litigation generally involves hourly production employees of Tyson Foods at its Storm Lake, Iowa, meat-processing facility. But, the dispute more basically involves six named (lead) plaintiff employees from the kill, cut and retrim departments of the Storm Lake operation who were paid their wages using, in part, Tyson's “gang-time” compensation system but who also claim to have been owed overtime pay resulting from disparate compensable work activities occurring at times other than while earning daily “gang time” kill, cut and retrim department production line compensation. The six attempt to assert two separate collective actions-a federal statutory action asserting violations of the FLSA, 29 U.S.C. §§ 201–219, and a state statutory action separately based upon the IWPCL, Iowa Code Chapter 91A.

This case was originally assigned to the Honorable Mark Bennett who conditionally "certified" a federal collective action class pursuant to 29 U.S.C. § 216(b) and a purported IWPCL state law class pursuant to Federal Rule of Civil Procedure 23(b)(3). Then, because the Honorable John Jarvey was already assigned to several comparable cases involving Tyson, this matter was transferred to Judge Jarvey for further pretrial and post-trial proceedings and for trial. The case has now been litigated and is before this panel on appeal.

II. DISCUSSION

A. The Federal FLSA Class

A collective action to recover damages permitted by the FLSA "may be maintained against any employer . in any Federal or State court of competent jurisdiction by anyone or more employees for and in behalf of himself or themselves and other employees similarly situated." However, "[n]o employee shall be a party plaintiff to any such action unless he gives his consent in writing to become such a party and such consent is filed in the court in which such action is brought."

The six named lead plaintiff employees who sought to establish this collective action bore the "burden of showing that the opt-in [consenting] plaintiffs are similarly situated to the lead plaintiffs." Judge Bennett, apparently recognizing the likely existence of numerous factors unrelated to the "gang-time" pay used to determine a given Tyson employee's regular wages-factors amply established by the evidence at trial-certified a "conditional" FLSA class consisting of employees from the kill, cut and retrim departments at the Tyson plant paid through the so-called gang-time compensation system within a discrete time period set forth in the certification. Indeed, the conditional certification related only to the three departments and the gang-time pay earned in the production line in those departments. No other regular or overtime pay calculation factors discussed at the merits portion of the trial (such as: individual employment codes, specific duties, wage-rate variations, knife wielding protections, sanitary clothing and equipment, part-time work, illness, injury, shift differentials, and routine production line overtime) were in any way incorporated as limitations on the use of the FLSA conditional class. The record reveals that this "conditional" designation was never withdrawn or modified at any time during or after the trial. According to the joint stipulation of facts by the parties, there were 444 employees who consented to be a part of this FLSA collective action class including the six named lead plaintiffs.

B. The IWPCL State Class

"'In order to obtain class certification, a plaintiff has the burden of showing that the class should be certified and that the requirements of Rule 23 are met.'" Judge Bennett, at the request of the same six named plaintiffs who sought creation of and joined the FLSA collective class, ultimately certified what he termed a "modified" 3,344–person putative Rule 23 state law class consisting of all "current and former employees of Tyson's Storm Lake, Iowa, processing facility who have been employed at any time from February 7, 2005, to the present, and who are or were paid under a 'gang-time' compensation system in the Kill, Cut or Retrim departments." This certification also included no other limiting or enhancing overtime pay calculation elements. The record discloses that this certification was likewise never further embellished or modified during or after trial.

The "gang-time system of payment" as referred to by Judge Bennett and defined by the evidence is a system where employees are paid from the time their production line starts to the time their production line ends. There is no contention by the named plaintiffs that the Storm Lake Tyson employees did not receive all wages due and owing for time worked during the production line gang-time pay periods. So, standing by itself, as it does in the class certifications, the gang-time production line classification means little in the context of proving at trial through evidence common to the class the overtime pay claims of the 3,344 members of the allegedly underpaid overtime class. Supreme Court and Eighth Circuit precedent demands otherwise.

To be certified for purposes of Rule 23(a), the collective groupings, that is the putative classes, must have been such that Tyson was positioned to assert its legitimately held common-to-the-class defenses against all members of the group who claimed to have earned unpaid overtime wages. In this same context, the class must have been limited to Tyson employees who could and did establish entitlement to overtime pay resulting from overtime work performed during compensable time, that is, work performed at times other than production line gang-time pay periods-periods for which all class members were already routinely, regularly, and unquestionably paid by Tyson in accordance with the law.

"In order to obtain class certification, a plaintiff has the burden of showing that the class should be certified and that the requirements of Rule 23 are met." While a Rule 23(b)(3) class was purportedly certified, any Rule 23 class may only be lawfully certified if the "trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied." Actual, not presumed, conformance with Rule 23(a) remains indispensable. Frequently, as in this case, " 'rigorous analysis' will entail some overlap with the merits of the plaintiff's underlying claim." Rule 23(a)'s four bedrock requirements are numerosity, commonality, typicality and adequate representation (here, a named plaintiff with standing). Commonality requires the plaintiff to demonstrate at the time of the merits hearing on the underlying claim-that all class members suffered the same injury. So, if the locution "injury" includes the measure of a class member's individual damages, as I believe it does, this class fails on that score alone.

The court majority apparently sees a pathway around plaintiffs' legal dilemma arising from the above-noted class formulation failures. Although acknowledging that class certification is improper when a "windfall" is conferred on some class members, ante at 7, the court makes the following observation:

At any rate, at Tyson's request, the jury was instructed, "Any employee who has already received full compensation for all activities you may find to be compensable is not entitled to recover any damages." Tyson's instruction directed the jury to treat plaintiffs with no damages as class members. It is "fundamental that where the defendant . 'invited error' there can be no reversible error."

Thus, says the court, Tyson "directed the jury to treat plaintiffs with no damages as class members." However, Tyson made no such class membership directive to the jury through its instructional request and *Beason* and *Steele* are wholly inapposite as case precedent for the court's faulty premise. The cases deal only with run-of-the-mill evidentiary matters, not waivers of legal principles. *Beason* simply opened the door to the making of a *Bruton* exception by permitting an admission from a non-testifying co-defendant, and *Steele* admitted otherwise inadmissible hearsay evidence to clarify and rebut an issue opened by the criminal defendant's cross-examination. Tyson, after vigorously resisting class action formulations at every turn in this litigation, and being denied, properly requested an instruction that the plaintiffs be held to their evidentiary burdens of proof.

C. The Merits

Fundamentally, as previously noted, this case emerges from two separate causes of action brought through a single federal court complaint—a federal law cause of action alleging liability leading to damages arising from violation of the FLSA and a state law cause of action alleging liability and damages arising from violation of the IWPCL. The burden of proof on all issues of statutory liability, injury and measure of damages rests squarely upon the shoulders of the named plaintiffs. In this case, gang-time pay is not in dispute. The plaintiffs contend, as does the court majority, that the overtime pay dispute involves time spent by a class of Tyson employees in doffing and donning various sanitary and personal protection equipment before and after the gang-time production line work has been completed each day.

Tyson's Storm Lake employees are required to wear a different combination of sanitary and protective gear. Those employees wearing knives to use in conjunction with their particular duties on a particular day are required to wear a combination of a plastic belly guard, mesh apron, mesh sleeve, plexiglass arm guard, mesh glove, Polar glove, membrane skinner gloves, Polar sleeves, "steel" for maintaining the knives and knife scabbards ("knife related gear"). Other workers are required to wear a hard hat, hairnet, beard net, earplugs, ear muffs, rubber or cotton gloves, and rubber or plastic aprons ("sanitary gear").

From 1998 until February 4, 2007, Tyson paid four extra minutes beyond production line time for all production employees, referred to as "K–Code" time. From February 4, 2007, to June 28, 2010, Tyson ceased paying non-knife-wielding employees for the time donning and doffing sanitary gear. From February 4, 2007, to June 28, 2010, Tyson paid knife-wielding employees between 4 to 8 minutes of KCode time, depending on the job, and employees who did not have a knife did not receive K–Code time payments.

Plaintiffs offered evidence at trial concerning a sample of putative class employees from Dr. Kenneth Mericle and Dr. Liesl Fox. Fox's calculation testimony fed off of Mericle's evidence concerning Rule 23 class damages for overtime pay. Fox testified, assuming Mericle's evidence was true, that at least 212 members of the purported class did not suffer any damages because the doffing and donning time, less the K–Code time "would not have been enough to kick them into overtime." Further, while the plaintiffs' evidence generally indicated some individual overtime damages ranging from a few cents to several thousand dollars, there were at least 509 workers whose injuries ranged from $0.27 to less than $100. And, the record discloses that the jury in returning only a single gross amount of damages verdict, as instructed, discounted plaintiffs' evidence by more than half, likely indicating that more than half of the putative class suffered either no damages or only a *de minimis* injury measured in cents rather than dollars. In spite of having the burden of proof, there was no evidence adduced by plaintiffs that established the number of purported class member employees fully compensated or not fully compensated by the K–Code payments already paid by Tyson. It is evident, however, that many class employees fit within each category and all were apparently included as beneficiaries of the single damages verdict returned by the jury.

Rule 23(a)(2) contemplates that "there are questions of law or fact common to the class." "Commonality requires the plaintiff to demonstrate that the class members have suffered the same injury. This does not mean merely that they have all suffered a violation of the same provision of law." Rather, "[t]heir claims must depend upon a common contention. That common contention, moreover, must be of such a nature that it is capable of class-wide resolution-which means that determination of its truth or falsity will resolve an issue that is central to the validity of each one of the claims in one stroke." "What matters to class certification is not the raising of common 'questions' . but, rather the capacity of a class-wide proceeding to generate common answers apt to drive the resolution of the litigation." That was not the case here. While it is true that all class members were subject to a common policy-gang-time payment-there is no "common answer," arising from the evidence concerning the individual overtime pay questions at issue in this case. Thus, this case with these classes cannot be resolved in "one stroke," given the differences in donning and doffing times, K–Code payments, abbreviated gang time shifts, absenteeism, sickness, vacation and a myriad of other relevant factors. The "rigorous" analysis of class certification in this case, which overlaps with the merits as required by *Dukes*, clearly discloses that the Rule 23 class claim does not comply with either rule or precedent and should have been decertified.

Finally, the wisdom of the Supreme Court's statement in *Symczyk*, that Rule 23 class actions and collective actions under the FLSA are fundamentally different and thus do not lend themselves to inextricably intertwined trials, as here, is well dramatized by this case. Here we have undifferentiated presentations of evidence, including significant numbers of the putative classes suffering no injury and members of the entire classes suffering wide variations in damages, ultimately resulting in a single-sum class-wide verdict from which each purported class member, damaged or not, will receive a pro-rata portion of the jury's one-figure verdict. Assuming that the district court could now re-open the proceedings in an effort to deal with an individual plaintiff's damages using the Mericle/Fox evidence, the exercise would be laborious, virtually unguided, and well outside of the limiting parameters the Supreme Court has, as a matter of law, placed upon use of the Rule 23 class action machinery.

III. CONCLUSION

From this result, I dissent.

“High Court Told to Kill Tyson Workers’ $5.8M Don-Doff Award”

Law360
Kurt Orzeck
March 27, 2015

Tyson Foods Inc. wants the U.S. Supreme Court to overturn a $5.8 million judgment awarded to a class of employees in a compensation dispute over time spent putting on and taking off protective gear, according to a court filing made public Friday.

In a petition for writ of certiorari, Tyson argued a district court shouldn’t have certified the class due to differences in the amount of time that employees spent on donning and doffing protective gear. The workers alleged that Tyson's so-called gang-time compensation system short-changed them on pay.

In August, a divided Eighth Circuit panel upheld a decision by U.S. District Judge John A. Jarvey that affirmed a jury verdict favoring the workers, saying he properly certified their claims under both the Fair Labor Standards Act and Iowa state law. In November, a divided Eighth Circuit declined Tyson’s rehearing bid.

Tyson argued in its Supreme Court petition, filed Mar. 19, that other circuit courts have held that a class can’t be certified if plaintiffs try to get an aggregate damages award by extrapolating from an allegedly fictional “average” class member.

“This court’s review is also needed to resolve the confusion among the lower courts on the question of whether a class may be certified when it includes uninjured class members,” Tyson said, adding that hundreds of employees in the suit allegedly didn’t work any overtime at all due to donning and doffing. “This court should grant review to resolve the confusion and put an end to this unlawful practice.”

The petition is the latest move in a suit that traces back to 2007, when workers at Tyson's meat-processing facility in Storm Lake, Iowa, claimed Tyson's policy didn't fully compensate them for pre- and post-production line activities, according to court documents.

In September 2011, an Iowa jury found that the plaintiffs had proven that the time they spent donning and doffing hard hats, work boots, hairnets, aprons, gloves and earplugs constituted an indispensable part of their work at Tyson plants. The verdict awarded the workers $2.9 million, and a subsequent ruling on liquidated damages upped the total final judgment to $5.8 million, according to court documents.

Citing the U.S. Supreme Court's landmark 2011 ruling in *Wal-Mart Stores Inc. v. Dukes*, Tyson argued on appeal that alleged differences in the donning and doffing times didn’t allow the class action to "generate common answers apt to drive the resolution of the litigation," according to court documents.

But the Eighth Circuit disagreed in August, saying that unlike *Dukes*, Tyson had a specific company policy that applied to all class members. Also in contrast to *Dukes*, the class members in the instant case worked at the same plant and used similar equipment, the panel said.

Though a majority of Eighth Circuit judges denied Tyson's rehearing request in November, six judges on the circuit said they would have granted a rehearing en banc or a panel rehearing.

Tyson argued in its Supreme Court petition that three production workers who testified at trial said they spent different amounts of time on donning- and doffing-related activities. A study showed a wide variation among the times, with employees spending between about a half-minute and 13 minutes donning equipment in the locker room pre-shift and between roughly two and nine minutes doffing and storing equipment post-shift, according to Tyson.

A Tyson spokesman told Law360 on Friday that the company was initially involved in this case because federal wage and hour laws are not precise in determining how to compensate certain activities.

"We’re now addressing another aspect of the case: whether there’s enough evidence for it to be considered a class action," he said. "Since even the federal courts of appeal are divided over what employees qualify to be part of such class action cases, we’ve asked the U.S. Supreme Court to get involved. We’re hopeful our request will be granted."

“Roberts Court to Review Wage Theft Class Action Case”

RH Reality Check
Jessica Mason Pieklo
June 8, 2015

The Supreme Court on Monday agreed to consider new limits on workers’ ability to collectively challenge pay and workplace issues under the Fair Labor Standards Act (FLSA).

The Roberts Court granted review in the case of *Tyson Foods v. Bouaphakeo,* a class action lawsuit against Tyson Foods Inc. over the pay of more than 3,000 employees at its Storm Lake, Iowa, pork processing plant. Peg Bouaphakeo, along with other Tyson employees challenged a series of practices, including Tyson’s refusal to provide overtime compensation for the time employees spent “donning (putting on) personal protective equipment (PPE)” and clothing before and again after lunch, and for doffing (removing) PPE and clothing before and after lunch.

The employees sued Tyson for failing to pay wages under the FLSA and Iowa Wage Payment Collection Law. A jury returned a verdict for the certified class of workers, ordering Tyson to pay $5.8 million in past wages and damages.

A federal appeals court affirmed the multimillion-dollar verdict against Tyson.

The Roberts Court on Monday agreed to step in and hear Tyson’s arguments that it should only have to defend against claims by workers who were injured by Tyson’s wage-and-hour violations, and not the entire certified class of workers in the lawsuit.

In other words, Tyson is not defending its actual labor practices but instead arguing the courts made a procedural error by allowing Bouaphakeo’s lawsuit to have been certified as a class action.

To support their petition for review to the Roberts Court, Tyson and other industry groups rely on the Roberts Court decision in *Wal-Mart v. Dukes*, a 2011 decision that revoked class action certification from what would have been one of the largest gender bias lawsuits of its kind. That decision significantly curtailed the scope of potential class action lawsuits under federal employment laws.

Industry groups hope to have similar success curtailing workers’ rights to bring class action lawsuits under the FSLA in *Bouaphekeo.*

A decision in favor of Tyson could have a wide-reaching effect. Like pay discrimination cases, wage-and-hour lawsuits often involve individual damages claims that may not amount to a lot of money compared to the time and expense involved in prosecuting those claims. Class action lawsuits in which workers can aggregate their claims and money damages, however, give workers leverage in fighting against wage theft as the aggregated damages can add up to multimillion-dollar verdicts, as it did against Tyson in *Bouaphakeo*.

Monday's decision to review the class-certification in *Bouaphakeo* may not be the only FLSA class action case the Roberts Court will hear next term.

The Court considered *Bouaphakeo* along with two other petitions, both filed by Walmart, challenging FLSA class action verdicts in Pennsylvania totaling more than $187 million. Despite considering the cases together, the Roberts Court on Monday took no action on the Walmart cases challenging class action certifications under the FLSA, which means the Court could be waiting to see how the arguments in Bouaphakeo unfold before deciding how broadly to review class action certification in wage theft claims.

"Game Changer?"

Seyfarth Shaw LLP
Richard Alfred, Patrick Bannon, and Esther Slater McDonald
June 9, 2015

The U.S. Supreme Court agreed yesterday to hear an appeal challenging a nearly $6.0 million judgment in a collective and class action case against Tyson Foods, Inc. In *Tyson Foods, Inc. v. Bouaphakeo*, a wage and hour collective and class action regarding the compensability of time spent donning and doffing, the Court will decide (1) whether liability and damages may be determined by statistical techniques that presume all class or collective members are similar; and (2) whether a class or collective action may include individuals who were not injured.

Case Background

Plaintiff employees brought a collective and class action against Tyson under the Fair Labor Standards Act ("FLSA") and a parallel state law. The plaintiffs alleged that they were entitled to damages because Tyson failed to pay them overtime for time spent "donning" and "doffing" personal protective equipment and walking to and from their work stations. The district court certified an FLSA collective and Rule 23 class based on its conclusions regarding the existence of common questions about whether those activities were "compensable 'work'" under the FLSA and the state law. At trial, the plaintiffs used statistical evidence of the average donning, doffing, and walking times for employees to prove liability and damages. The jury returned a verdict for the collective and class, and the final judgment totaled $5.8 million.

On appeal, Tyson contended that certification was improper because employees' individual routines varied and, thus, the litigation could not generate common answers apt to drive the resolution of the litigation as required under *Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541 (2011). Tyson pointed out that liability and damages were only inferred as to individual class members based on statistical evidence contrary to the Supreme Court's "Trial by Formula" prohibition in Dukes and the use of damages models that ignore the basis of defendant's alleged liability to each class member as required by *Comcast v. Behrend*, 133 S. Ct. 1426 (2013).

Tyson further argued that collective and class certification was inappropriate because some class members did not work any overtime and were thus not entitled to any damages. The Eighth Circuit Court of Appeals rejected these arguments, holding that liability and damages could be proven by inference and that issues relating to individual damages, or no damages at all, do not preclude certification.

Citing circuit splits on both issues presented, Tyson filed a petition for a writ of certiorari in March 2015 which was granted today.

Those issues, as stated in the cert petition, are:

(1) Whether differences among individual class members may be ignored and a class action certified under Federal Rule of Civil Procedure 23(b)(3), or a collective action certified under the Fair Labor Standards Act, where liability and damages will be determined with statistical techniques that presume all class members are identical to the average observed in a sample; and

(2) whether a class action may be certified or maintained under Rule 23(b)(3), or a collective action certified or maintained under the Fair Labor Standards Act, when the class contains hundreds of members who were not injured and have no legal right to any damages.

Potential Implications for Wage & Hour Collective and Class Actions

Even though employers have been facing an avalanche of wage and hour collective and class claims for more than a decade, the Supreme Court has had little to say in the wage and hour context about the procedures for litigating collective actions, class actions, or "hybrids" of the two. The potential for a game-changing ruling is a very important development for employers.

Courts have been divided about whether the mere allegation of a specific type of FLSA violation, allegedly affecting a group of employees, is sufficient to show that the employees are "similarly situated" within the meaning of Section 216(b), the main remedies provision of the FLSA. The issue that the Supreme Court has now agreed to hear–whether a collective can properly be certified where the alleged FLSA violation affected different employees differently and some not at all–is an important one, especially in "off-the-clock" FLSA cases.

The Tyson Foods case is especially fascinating because it involves a "hybrid" case, involving a Rule 23 opt-out class with several thousand members and an FLSA "collective" of 444 opt-in plaintiffs. The Supreme Court can be expected to address how its *Wal-Mart* and *Comcast* decisions–both arising under Rule 23–apply to FLSA collective actions as well as state law wage and hour class actions. The Court's prohibition in *Wal-Mart* of "trial by formula" has the potential to restrict the certification of collective actions, both initially and ultimately, to adjudicate cases with large numbers of plaintiffs with highly individualized claims.

DIRECTV, Inc. v. Imburgia

14-462

Ruling Below: *Imburgia v. DIRECTV, Inc.*, 225 Cal. App. 4th 338 (Cal. App. 2d Dist. 2014)

Plaintiff customer filed a class action complaint against defendant television service provider under the Consumer Legal Remedies Act (CLRA), Civ. Code, § 1750 et seq., and other state laws, and the Superior Court of Los Angeles County, California, denied the provider's motion to compel arbitration. The provider appealed.

The court of appeal held that the trial court properly denied the provider's motion to compel arbitration. The arbitration agreement was unenforceable because it expressly stated that the entire section would be unenforceable if the law of the customer's state would find the class action waiver unenforceable. California would have found the waiver unenforceable because CLRA expressly precludes waiver of the right to bring a CLRA class action. The reference to state law regarding enforceability of the class action waiver created a specific exception to the general provision that the arbitration agreement would be governed by the FAA and did not render that general provision meaningless. (Credit Lexis Nexis)

Question Presented: Whether the California Court of Appeal erred by holding, in direct conflict with the Ninth Circuit, that a reference to state law in an arbitration agreement governed by the Federal Arbitration Act requires the application of state law preempted by the Federal Arbitration Act.

Amy IMBURGIA et al.,
Plaintiffs and Respondents
v.
DIRECTV, INC.,
Defendant and Appellant

In the Court of Appeal of the State of California, Second Appellate District, Division One

Filed on April 7, 2014

[Excerpt; some citations and footnotes omitted]

APPEAL from an order of the Superior Court of Los Angeles County. John Shepard Wiley, Jr., Judge. Affirmed.

DIRECTV, Inc. moved to dismiss or stay this class action litigation and to compel arbitration. The superior court denied the motion. DIRECTV argues that the motion should have been granted under the United States Supreme Court's decision in *AT&T Mobility LLC v. Concepcion* (2011). We conclude that under the terms of the parties' arbitration agreement, the motion was correctly denied. We therefore affirm.

BACKGROUND

On September 17, 2008, Amy Imburgia filed a class action complaint against DIRECTV, alleging claims for unjust enrichment, declaratory relief, false advertising, and violation of the Consumer Legal Remedies Act (CLRA), the unfair competition law (UCL), and Civil Code section 1671, subdivision (d). Imburgia's claims were based on allegations that DIRECTV has improperly charged early termination fees to its customers. Kathy Greiner filed a similar class action complaint one day after Imburgia, and Imburgia and Greiner (hereafter plaintiffs) jointly filed a first amended complaint on March 16, 2009. Plaintiffs' lawsuit proceeded at the same time as a multidistrict litigation proceeding in federal court involving similar claims. DIRECTV moved to stay plaintiffs' state court action pending the outcome of the multidistrict litigation, but the superior court denied the motion.

Plaintiffs subsequently moved for class certification. On April 20, 2011, the superior court granted the motion in part and denied it in part, certifying a class as to one of plaintiffs' theories but denying certification as to others.

On April 27, 2011, the United States Supreme Court decided Concepcion, which held that the Federal Arbitration Act (FAA) preempts the rule of *Discover Bank v. Superior Court* (2005). *Discover Bank* held that under certain circumstances, class action waivers in consumer contracts are unconscionable and hence unenforceable.

On May 17, 2011, less than one month after the Court decided *Concepcion*, DIRECTV moved to stay or dismiss plaintiffs' action, decertify the class, and compel arbitration of plaintiffs' claims. DIRECTV explained that it had not moved to compel arbitration earlier because, in an unrelated case several years before plaintiffs filed this litigation, the Court of Appeal had held that the arbitration provision in DIRECTV's customer agreement was unenforceable under *Discover Bank.* Until *Concepcion* held that the FAA preempts the rule of *Discover Bank*, DIRECTV consequently believed that a motion to compel arbitration would be futile.

The relevant arbitration provision is contained in section 9 of DIRECTV's 2007 customer agreement. Section 9 provides that "any legal or equitable claim relating to this Agreement, any addendum, or your Service" will first be addressed through an informal process and, if the claim is not resolved informally, then "any Claim either of us asserts will be resolved only by binding arbitration" under JAMS rules. Under the heading "Special Rules," section 9 of the agreement provides as follows: "Neither you nor we shall be entitled to join or consolidate claims in arbitration by or against other individuals or entities, or arbitrate any claim as a representative member of a class or in a private attorney general capacity. Accordingly, you and we agree that the JAMS Class Action Procedures do not apply to our arbitration. If, however, the law of your state would find this agreement to dispense with class arbitration procedures unenforceable, then this entire Section 9 is unenforceable."

Section 10 of the 2007 customer agreement contains provisions addressing several miscellaneous matters, including the following provision concerning "Applicable Law": "The interpretation and enforcement of this Agreement shall be governed by the rules and regulations of the Federal Communications Commission, other applicable federal laws, and the laws of the state and local area where Service is provided to you. This Agreement is subject to modification if required by such laws. Notwithstanding the foregoing, Section 9 shall be governed by the Federal Arbitration Act."

Plaintiffs opposed the motion to compel arbitration on numerous grounds. The superior court denied the motion, and DIRECTV timely appealed.

STANDARD OF REVIEW

"On appeal from the denial of a motion to compel arbitration, 'we review the arbitration agreement de novo to determine whether it is legally enforceable, applying general principles of California contract law. We review the superior court's ruling, not its reasoning, and we consequently may affirm on the basis of any valid legal theory, regardless of whether the superior court relied on it.

DISCUSSION

In addition to stating that the parties waive their rights to bring class claims, section 9 of the 2007 customer agreement states that if "the law of your state would find this agreement to dispense with class arbitration procedures unenforceable, then this entire Section 9 is unenforceable." Plaintiffs argue that the law of California would find the class action waiver unenforceable because, for example, the CLRA expressly precludes waiver of the right to bring a class action under the CLRA. Plaintiffs conclude that the parties' entire arbitration agreement is unenforceable, pursuant to the agreement's express terms, because the law of plaintiffs' state would find the class action waiver unenforceable. We agree.

As all parties point out, the FAA "requires courts to enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms." The FAA's broad policy of enforcement of arbitration agreements according to their terms applies even to "agreements to arbitrate under different rules than those set forth in the [FAA] itself." Thus, if "parties have agreed to abide by state rules of arbitration, enforcing those rules according to the terms of the agreement is fully consistent with the goals of the FAA," even if application of the state rules would yield a different result from application of the FAA. Consequently, although it is impossible for parties to "'opt out' of FAA coverage in its entirety because it is the FAA itself that authorizes parties to choose different rules in the first place," it is in other respects permissible for the parties to "opt out of the FAA's default rules." In particular, a choice of law provision in an arbitration agreement is, in general, enforceable to the same extent as a choice of law provision in any other contract. We have previously held that the parties to a contract may choose the law under which the enforceability of a class action waiver is to be determined.

Under the foregoing principles, if section 9 of DIRECTV's 2007 customer agreement had said that the enforceability of the class action waiver "shall be determined under the law of your state to the extent that it is not preempted by the FAA," then that provision would have been enforceable. Likewise, if section 9 had said that the enforceability of the class action waiver "shall be determined under the law of your state without considering the preemptive effect, if any, of the FAA," then that provision would have been enforceable as well. No party argues to the contrary.

Section 9 of the 2007 customer agreement is not, however, as explicit as either of those hypothetical examples. The question before us, then, is how to interpret section 9's choice of law concerning enforceability of the class action waiver. Where section 9 requires us to consider whether "the law of your state would find this agreement to dispense with class arbitration procedures unenforceable," does it mean "the law of your state to the extent it is not preempted by the FAA," or "the law of your state without considering the preemptive effect, if any, of the FAA"? Plaintiffs argue that it means the latter, and we agree.

Plaintiffs' principal argument in favor of their interpretation is that "under well established principles of contract interpretation, when a general and a particular provision are inconsistent, the particular and specific provision is para[]mount to the general provision." On that basis, plaintiffs contend that the reference to "the law of your state" in section 9 of the 2007 customer agreement operates as "a specific *exception* to the arbitration agreement's *general* adoption of the FAA" in section 10. That is, although the agreement provides that in general section 9 is governed by the FAA, section 9 itself provides that the specific issue of the enforceability of the class action waiver shall be governed by "the law of your state."

DIRECTV's sole response to that argument is that "the contract interpretation principle [p]laintiffs invoke applies only where 'the provisions in question are truly inconsistent,'" but "there is no inconsistency" here because "both federal *and* state law have a role." We are not persuaded. If we apply state law alone (for example, the antiwaiver provision of the CLRA) to the class action waiver, then the waiver is unenforceable. If we apply federal law, then the class action waiver is enforceable and any state law to the contrary is preempted. That is a sufficient inconsistency to make plaintiffs' principle of contract interpretation applicable. Indeed, the entire preemption analysis of *Concepcion* is based on a conflict or inconsistency between the *Discover Bank* rule and the FAA.

Our interpretation of the contract finds further support in "the common-law rule of contract interpretation that a court should construe ambiguous language against the interest of the party that drafted it." DIRECTV "drafted an ambiguous document, and [it] cannot now claim the benefit of the doubt. The reason for this rule is to protect the party who did not choose the language from an unintended or unfair result."

Moreover, "[t]hat rationale is well suited to the facts of this case" because "[a]s a practical matter, it seems unlikely that" plaintiffs anticipated in 2007 that the Supreme Court would hold in 2011 that the FAA preempts the *Discover Bank* rule concerning the enforceability of class action waivers in arbitration agreements. "In the face of such doubt, we are unwilling to impute this intent to [plaintiffs]."

Finally, DIRECTV cites three cases as having "rejected" plaintiffs' argument. Two of the cases are readily distinguishable because, unlike the instant case, neither of them involves an arbitration agreement that specifically provides that the enforceability of the class action waiver is to be decided under state law.

The third case, however, is a decision in the federal multidistrict litigation that parallels the instant state court actions. In an "[i]ndicative [r]uling" under rule 62.1 of the Federal Rules of Civil Procedure, the federal district court stated that the reference to "the law of your state" in section 9 of the customer agreement could not mean that enforceability of the class action waiver should be determined exclusively under state law, because that would render "meaningless" section 10's general statement that the arbitration agreement is governed by the FAA. We disagree. The specific reference to state law concerning the enforceability of the class action waiver creates a narrow and specific exception to the general provision that the arbitration agreement will be governed by the FAA. It does not render that general provision meaningless. In addition, the district court's analysis does not address the principles that a specific provision controls over a general one and that ambiguous language is construed against the interest of the drafter. For all of these reasons, we decline to follow the district court's decision.

After briefing in this appeal was completed, the United States Court of Appeals for the Ninth Circuit decided a similar case concerning the enforceability of the arbitration provision and class action waiver in DIRECTV's customer agreement under *Concepcion*. The court held that "the arbitration agreement is enforceable under *Concepcion*," which preempts any state law to the contrary. The court reasoned that "the parties' various contract interpretation arguments"—which included both the argument that the specific reference to state law controlled over the general reference to the FAA and the argument that ambiguities should be construed against the drafter—"are largely irrelevant to our analysis," because under the Supremacy Clause of the United States Constitution, and the related doctrine of federal preemption, federal law is the law of every state.

We find the analysis in *Murphy* unpersuasive. On the one hand, insofar as the court's reasoning is a matter of contract interpretation, it means that when the parties used the phrase "the law of your state," they meant "federal law plus (nonfederal) state law." *Murphy* provides no basis for concluding that the parties intended to use the phrase "the law of your state" in such a way, and we are aware of none. On the contrary, a reasonable reader of the customer agreement would naturally interpret the phrase "the law of your state" as referring to (nonfederal) state law, and any ambiguity should be construed against the drafter. On the other hand, insofar as the court reasoned that contract interpretation is irrelevant because the parties are powerless to opt out of the FAA by contract, we are aware of no authority for the court's position. Rather, as we have already observed, if the customer agreement expressly provided that the enforceability of the class action waiver "shall be determined under the (nonfederal) law of your state without considering the preemptive effect, if any, of the FAA," then that choice of law would be enforceable; *Murphy* cites no authority to the contrary. Consequently, the dispositive issue is whether the parties intended to make that choice. As a result, "the parties' various contract interpretation arguments" are not "largely irrelevant."

To summarize: Section 9 of the 2007 customer agreement provides that "if . . . the law of your state would find this agreement to dispense with class arbitration procedures unenforceable, then this entire Section 9 is unenforceable." The class action waiver is unenforceable under California law, so the entire arbitration agreement is unenforceable. The superior court therefore properly denied the motion to compel arbitration.

DISPOSITION

The order is affirmed. Respondents shall recover their costs of appeal.

"U.S. Supreme Court Agrees to Hear DirecTV Arbitration Case"

Reuters
Lawrence Hurley
March 23, 2015

The U.S. Supreme Court on Monday agreed to hear an appeal filed by DirecTV Inc concerning the satellite television provider's efforts to enforce arbitration agreements its customers in California have signed.

The high court agreed to review a decision by a state appeals court in California that found that consumers were not bound by a provision in the company's customer agreement preventing disputes being resolved on a class-wide basis.

The company says that disagreements must be resolved individually via private arbitration.

Consumer advocates have criticized the increased use of arbitration agreements that they say deny customers the opportunity to vindicate their rights in court.

The litigation dates back to 2008 when Amy Imburgia and Kathy Grenier filed class action lawsuits saying that DirecTV had violated state law by imposing cancellation fees.

DirecTV says the April 2014 ruling by the California Court of Appeal, Second District in favor of the consumers conflicts with a 2013 decision the company won on the same matter that was issued by the San Francisco-based 9th U.S. Circuit Court of Appeals.

The high court will hear the case during its next term, which starts in October and ends in June 2016.

"Direct to Arbitration: Enforcing Arbitration in Consumer Contracts"

JLPP: Cornell Journal of Law and Public Policy

Wayne Yu

April 12, 2015

The Supreme Court has agreed to review a class action lawsuit brought by consumers challenging DirecTV's early termination fees. At issue is whether DirecTV's customer agreements, which require consumer disputes to be settled through private arbitration as opposed to litigation, are enforceable.

Most recently, the Second District California Court of Appeals ruled against DirecTV, finding that consumers were "not bound" by DirecTV's contract provision forcing disputes to be settled through private arbitration rather than litigation. In upholding the decision, the California Supreme Court denied review, stating that "California law forbids arbitration agreements that include a class action waiver." DirecTV petitioned for a writ of certiorari, arguing that the Federal Arbitration Act ("FAA") preempts state law, and therefore company contracts barring class action lawsuits are enforceable.

DirecTV, and many businesses, favor arbitration because the process generally lowers litigation costs, and more efficiently resolves customer disputes. Unlike litigation, the arbitration process is much quicker, permitting companies to spend "less time fighting, and more time actually running their businesses."

Arbitration is also less adversarial than litigation. This assists in resolving disputes while preserving ongoing customer and business relationships. One of the most compelling advantages of arbitration is the ability to keep both disputes and resolutions private. Arbitration proceedings are usually private, and parties generally agree to keep both the proceedings and terms of the resolution confidential. Accordingly, companies attain invaluable benefits through arbitration if a dispute concerns commercially sensitive and/or embarrassing matters.

Consumers claim that the increased use of arbitration denies individuals their rightful opportunity to vindicate their claims in court. Plaintiffs' attorneys assert that because arbitration occurs "behind closed doors," arbitration is stacked in favor of the companies. Unlike a judge in the courtroom, an arbiter's final decision is neither constrained nor guided by law, statutes, or precedent. As a result, both the lack of transparency and public accessibility of arbitration proceedings and resolutions may undermine the credibility and integrity of the process, and any final decisions of a presumed "objective" arbiter. Furthermore, unlike arbitration, litigation encourages and permits extensive discovery and full disclosure of evidence to all parties involved in a dispute.

Perhaps, the most important difference between litigation and arbitration is the right to appeal. In arbitration, the arbitrator's decision is generally not subject to review. Accordingly, consumers disapprove of arbitration because they believe that "mistakes are made frequently," and that the right to request a "second look" is both vital and important. The process of litigation preserves such rights through the appeals process.

Given the pros and cons of either arbitration or litigation, it is unclear which process is better for settling disputes and reaching resolutions. However, the Supreme Court will determine whether arbitration clauses barring class action lawsuits are enforceable, when it hears *DirecTV Inc. v. Amy Imburgia, et al.* this fall. This determination should hopefully settle the dispute once and for all.

"Recent California Appellate Opinion Raises Issue of *Concepcion*'s Scope"

National Law Review
May 2, 2014

On April 27, 2011, the Supreme Court in *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011), cleared the way for consumer products companies and other businesses to incorporate class action waivers into their arbitration agreements with customers. On April 7, 2014, the Second District Court of Appeal in California affirmed the denial of a motion to compel arbitration despite *Concepcion*, relying on language in the arbitration clause that rendered the clause invalid if state law would find the class action waiver unenforceable. The decision appears to contradict a recent Ninth Circuit decision, calling into question *Concepcion*'s scope and ensuring further litigation of the issue.

In *Imburgia v. DirecTV, Inc.*, 170 Cal. Rptr. 3d 190 (2014), Plaintiffs accused DirecTV of improperly charging early termination fees and brought a class action against the company for false advertising, violation of California's Consumer Legal Remedies Act (CLRA) and related claims. After the trial court granted in part Plaintiffs' motion for class certification, *Concepcion* came down and DirecTV moved to decertify the class and compel arbitration. DirecTV's arbitration clause included a class action waiver and provided generally that the Federal Arbitration Act (FAA) applied, but also provided: "If, however, the law of your state would find this agreement to dispense with class arbitration procedures unenforceable, then this entire Section … is unenforceable."

The trial court denied the motion based on this language, and the Court of Appeal affirmed, finding that "the law of California would find the class action waiver unenforceable because, for example, the CLRA expressly precludes waiver of the right to bring a class action under the CLRA."

DirecTV argued that the decision was contrary to *Concepcion* and its broad interpretation of the FAA. However, the Court stated, "[t]he FAA's broad policy of enforcement of arbitration agreements according to their terms applies even to 'agreements to arbitrate under different rules than those set forth in the [FAA] itself.'" Id. (citation omitted). Accordingly, based on the California rule of contract interpretation that a specific provision controls over a general one, "the reference to 'the law of your state' in [the arbitration agreement] operates as 'a specific exception to the arbitration agreement's general adoption of the FAA'" found elsewhere in the agreement. In addition, the Court held, Plaintiffs' "interpretation of the contract finds further support in 'the common-law rule of contract interpretation that a court should construe ambiguous language against the interest of the party that drafted it.'"

DirecTV relied on the recent Ninth Circuit case of *Murphy v. DirecTV, Inc*., 724 F.3d 1218 (9th Cir. 2013), which was decided after briefing in the *Imburgia* appeal was completed. There, the Ninth Circuit held that the class action waiver in DirecTV's customer agreement was enforceable under *Concepcion*, which preempts contrary state law. The Court of Appeals reasoned that "'the parties' various contract interpretation arguments'—which included both the argument that the specific reference to state law controlled over the general reference to the FAA and the argument that ambiguities should be construed against the drafter — 'are largely irrelevant to our analysis,' because under the Supremacy Clause of the United States Constitution, and the related doctrine of federal preemption, federal law is the law of every state."

The California Court of Appeal was unpersuaded: "a reasonable reader of the customer agreement would naturally interpret the phrase 'the law of your state' as referring to (nonfederal) state law, and any ambiguity should be construed against the drafter. On the other hand, insofar as the court reasoned that contract interpretation is irrelevant because the parties are powerless to opt out of the FAA by contract, we are aware of no authority for the court's position."

DirecTV's counsel has stated that the company intends to appeal. Thus, the extent to which parties are indeed powerless to opt out of the FAA because "federal law is the law of every state," or whether state law contract principles may allow them to do so, remains undecided. Based on the broad scope of the FAA as interpreted by *Concepcion* and *Murphy*, it is far from clear that the *Imburgia* decision will survive.