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California Court Refuses To Enforce Texas Forum Selection Clause Without Guarantee Texas Court Would Apply California Law

Contractual forum selection clauses have historically been favored in California so long as they are entered into "freely and voluntarily, and their enforcement would not be unreasonable."[1] This analysis, however, changes when the claims involve unwaivable California statutory rights like those granted to California franchisees as part of the Franchise Investment Law and Franchise Relations Act.[2]

In these instances, California courts have found it "counterintuitive" to accept that California's laws will be applied by an out-of-state forum resolving a dispute that involves a resident of that forum and a choice-of-law provision compelling the application of that forum's laws.[3]

To avoid the contractual circumvention of California's unwaivable statutes, California courts are making it increasingly more difficult for parties to enforce forum selection clauses. This is evident in the California Appellate Court's recent decision in the employment law case *Verdugo v. Alliantgroup, L.P.*, 2015 Cal. App. LEXIS 466 (May 28, 2015).

In *Verdugo*, as discussed below, the California Appellate Court refused to enforce a Texas forum selection clause in an employment agreement because the employer would not guarantee – *by stipulation* – that the Texas court would apply unwaivable California wage and hour laws to the dispute.

Relevant Factual Background

Defendant Alliantgroup, L.P. ("Alliantgroup") is a Texas company that provides specialty tax consulting services to businesses throughout the United States. From 2007 to 2013, plaintiff Rachel Verdugo ("Verdugo") worked as the Associate Director at Alliantgroup's Irvine, California office.

As a condition of employment, Verdugo entered into an employment agreement that contained a Texas choice-of-law provision and a forum selection clause that designated Harris County, Texas as the exclusive forum for any dispute arising out of her employment with Alliantgroup.

In April 2013, Verdugo brought a class action lawsuit in California Superior Court asserting numerous claims for wage and hour violations under California's Labor Code. Alliantgroup immediately moved to dismiss or stay the action in reliance upon the Texas forum selection clause in the employment agreement. The trial court granted the motion and stayed the action finding that the forum selection clause was valid and enforceable.

Verdugo timely appealed, arguing that the trial court erred because enforcing the Texas forum selection clause (and related choice-of-law clause) violated California's unwaivable law on employee compensation.

Burden Is On Party Seeking Enforcement Of Forum Selection Clause

A party opposing enforcement of a forum selection clause typically bears the burden of showing that the clause is unfair or unreasonable. California courts, however, have reversed the burden – placing it on the party attempting to enforce the forum selection clause – when the underlying claims are predicated upon statutory rights the California Legislature has declared to be unwaivable.[4]

The California Appellate court in the franchise case of *Wimsatt v. Beverly Hills Weight etc*., 32 Cal.App.4th 1511 (1995), is credited with being the first to address which party bears the burden of proof on a motion to enforce a forum selection clause when confronted with unwaivable statutory rights.

In *Wimsatt*, the franchisee plaintiff sued the franchisor defendant for violation of California's Franchise Investment Law ("CFIL"). The franchisor moved to dismiss the action pursuant to the out-of-state forum selection clause in the franchise agreement. The trial court granted the motion and the franchisee appealed.

The Appellate Court reversed, holding that the party attempting to enforce a forum selection clause bears the burden to show enforcement of the clause is not unreasonable or unjust "when unwaivable statutory rights are involved because a forum selection clause otherwise could be used to circumvent those unwaivable rights."[5] In reaching this conclusion, the Appellate Court explained that a forum selection clause carries the potential to contravene unwaivable franchisee protections in the CFIL by placing litigation in a forum in which there is no guaranty that California's franchise laws will be applied.

Since *Wimsatt*, California courts have applied the same reversed-burden rational when confronted with forum selection clauses and other California unwaivable statutory rights.[6]

Relying upon *Wimsatt* and its progeny, the *Verdugo* court held that – because California Labor Code rights cannot "in any way be contravened or set aside by a private agreement" – the burden of proof shifted to Alliantgroup.[7]

Alliantgroup Cannot Show Texas Court Would Apply California Law

To meet this burden, Alliantgroup was required to show that the enforcement of the Texas forum selection and choice-of-law clauses would "*not in any way diminish*

Verdugo's unwaivable Labor Code rights."[8] According to the *Verdugo* court, Alliantgroup could have easily satisfied this substantial burden by stipulating to the application of California law – something that Alliantgroup would not do.[9]

Instead, Alliantgroup loosely argued that "[u]nder Texas' choice of law doctrine, a Texas court would ***most likely*** apply California law to Verdugo's claims notwithstanding the [employment agreement's] choice of law provision."[10] The *Verdugo* court found this "conclusory speculation" to be insufficient to satisfy Alliantgroup's burden.[11]

In the alternative, Alliantgroup argued that the trial court's ruling should be affirmed because it had stayed rather than dismissed the action. By issuing a stay, Alliantgroup argued that the trial court had retained jurisdiction and could "lift the stay" and proceed with the action if the Texas court later refused to apply California law. Again, the *Verdugo* court rejected Alliantgroup's argument.

According to *Verdugo* court, the Texas court's application of Texas law would not make Texas an unsuitable forum, and would not "necessarily" allow the California court to lift the stay and resume proceedings on Verdugo's claims.[12] "If the trial court sought to resume proceedings every time the foreign jurisdiction made an adverse ruling, the unseemly conflicts among jurisdictions that the forum non conveniens doctrine is designed to eliminate would be commonplace."

Ultimately, Alliantgroup's failure to stipulate – coupled with its continued downplay of the California labor laws – suggested that Alliantgroup was intending to seek to enforce the Texas choice-of-law provision once the case was moved to Texas. Because of this, the *Verdugo* court reversed the trial court's decision and allowed Verdugo's claims to go forward in California.

Although *Verdugo* is an employment law matter, the same rationale and analysis should apply to any dispute involving a non-waivable California statute – including those confronting franchise counsel and arising out of the CFIL and California Franchise Relations Act.

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This case report was prepared by Kevin A. Adams (kadams@mulcahyllp.com) of the Irvine law firm of Mulcahy LLP. Mulcahy LLP is a boutique litigation firm that provides legal services to franchisors, manufacturers and other companies in the areas of franchise, trademark, trade secret, unfair competition, and distribution laws.

[1] *Smith, Valentino & Smith, Inc. v. Superior Court of Los Angeles County*, 17 Cal. 3d 491, 495-96 (Cal. 1976); *America Online, Inc. v. Superior Court*, 90 Cal. App. 4th 1, 11 (Cal. App. 1st Dist. 2001); *Verdugo v. Alliantgroup, L.P.*, 2015 Cal. App. LEXIS 466, *5-6 (Cal. App. 4th Dist. May 28, 2015)(To be reasonable, the clause must simply have "a logical connection with at least one of the parties or their transaction.").

[2] Corp. Code § 31512 ("Any condition, stipulation or provision purporting to bind any person acquiring any franchise to waive compliance with any provision of this law or any rule or order hereunder is void."); Bus. & Prof. Code § 20010 ("Any condition, stipulation or provision purporting to

bind any person to waive compliance with any provision of this law is contrary to public policy and void.").

[3] *Verdugo v. Alliantgroup, L.P.*, 2015 Cal. App. LEXIS 466 at *24 (citing *America Online, Inc.*, *supra,* 90 Cal. App. 4th at 14).

[4] *Verdugo v. Alliantgroup, L.P.*, 2015 Cal. App. LEXIS 466 at *2.

[5] *Id.* at 10.

[6] *See, e.g.*, *America Online, Inc. v. Superior Court*, 90 Cal.App.4th at 14 (reversing burden of proof to claims under the California Consumer Legal Remedies Act).

[7] *Verdugo v. Alliantgroup, L.P.*, 2015 Cal. App. LEXIS 466 at *13.

[8] *Id.* at *29.

[9] *Id.* at *31.

[10] *Id.* at *29.

[11] *Id.* (emphasis added); *see also*, *id.* at *30 (Noting that, although Alliantgroup "postulate[d]" about what a Texas court was "likely" to do, Alliantgroup carefully avoided making any specific and definitive argument that Texas courts either have applied or will apply California wage and hour laws despite a choice-of-law clause designating Texas law.).

[12] *Id.* at *38.

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