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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION THREE

JOHN EDWARDS,

Plaintiff and Respondent,

v.

FIRST REPUBLIC BANK,

Defendant and Appellant.

A135505

(San Francisco County
Super. Ct. No. CGC-11-516928)

Defendant First Republic Bank (the Bank) appeals from an order denying its motion to compel arbitration of an employment dispute with plaintiff John Edwards. An arbitration agreement may be unenforceable if it is both procedurally and substantively unconscionable. (*Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, 114 (*Armendariz*)). The trial court found that the agreement here is substantively unconscionable because the Bank can modify it at any time. As Division One of this Appellate District recently observed in a case presenting the same issues as those raised here (*Peng v. First Republic Bank* (2013) 219 Cal.App.4th 1462, 1473-1474 (*Peng*)), the trial court's finding of substantive unconscionability was contrary to our holding in *24 Hour Fitness, Inc. v. Superior Court* (1998) 66 Cal.App.4th 1199, 1214 (*24 Hour Fitness*). Like the court in *Peng*, we adhere to the reasoning expressed in *24 Hour Fitness* and the cases that have followed it, and conclude that the Bank's arbitration agreement is not substantively unconscionable. We therefore reverse the order denying the motion to compel arbitration.

I. BACKGROUND

Edwards signed a March 2010 offer of employment from the Bank, and an agreement attached to the offer that specified all claims relating to his employment would be resolved by arbitration. The Bank reserved the right under the arbitration agreement to modify it “at any time with or without notice.” Edwards sued the Bank for gender discrimination and other causes of action arising from termination of his employment. The court denied the Bank’s motion to compel arbitration on the grounds that the arbitration agreement is substantively unconscionable because of the modification provision, and procedurally unconscionable because it provides for arbitration “in accordance with the rules of the American Arbitration Association or such alternative dispute resolution service as agreed upon by the parties” and such rules “were not provided to [Edwards], much less identified with any clarity.” Before the trial court, the parties did not discuss the limitations the covenant of good faith and fair dealing places on an employer’s ability to modify an employment agreement as identified in *24 Hour Fitness*, or its possible application to the agreement offered by the Bank.

II. DISCUSSION

In *24 Hour Fitness*, this court rejected an argument that an arbitration agreement in a personnel handbook was “illusory” because the employer had the right to change the handbook “at any time for any reason without advance notice.” (*24 Hour Fitness, supra*, 66 Cal.App.4th at pp. 1213-1214.) We observed that “ “[w]here the contract specifies performance the fact that one party reserves the power to vary it is not fatal if the exercise of the power is subject to prescribed or implied limitations such as the duty to exercise it in good faith and in accordance with fair dealings.” ’ [Citations.]” (*Id.* at p. 1214.) We held that the employer’s “discretionary power to modify the terms of the personnel handbook . . . indisputably carries with it the duty to exercise that right fairly and in good faith. [Citation.] So construed, the modification provision does not render the contract illusory.” (*Ibid.*)

As the court in *Serpa v. California Surety Investigations, Inc.* (2013) 215 Cal.App.4th 695 (*Serpa*) recently noted, our analysis in *24 Hour Fitness* was followed in

Peleg v. Neiman Marcus Group, Inc. (2012) 204 Cal.App.4th 1425 (*Peleg*). “In *Peleg* the employee of a department store asserted the arbitration agreement he signed was illusory because the store retained the unilateral right to amend, modify or revoke the agreement on 30 days’ advance written notice with the change to apply to any unfiled claim. (*Id.* at p. 1437.) Citing *24 Hour Fitness*, the *Peleg* court observed had the agreement to arbitrate simply authorized the department store to make unilateral modifications, it would not be illusory under California law because the implied covenant of good faith and fair dealing would preclude any change that undermined the employee’s rights. (*Peleg*, at pp. 1465-1466.)” (*Serpa, supra*, 215 Cal.App.4th at p. 707.)

Serpa likewise followed *24 Hour Fitness*. The arbitration agreement in *Serpa* incorporated provisions in an employee handbook (*Serpa, supra*, 215 Cal.App.4th at p. 699), and the employer had the right to “revise, modify, or delete” the handbook’s provisions “except for the policy of at-will employment, at any time” (*id.* at p. 700). The employee’s argument that the modification provision made the obligation to arbitrate illusory and thus unconscionable “fail[ed] to recognize the fundamental limit on [the employer’s] ability to alter the arbitration agreement imposed by the covenant of good faith and fair dealing implied in every contract.” (*Id.* at p. 706.) “[U]nder the analyses of both *24 Hour Fitness* and *Peleg*, the implied covenant of good faith and fair dealing is properly applied in this case and saves this arbitration contract from being illusory.” (*Id.* at pp. 707-708.)

Like the *Peng* court, we conclude that *24 Hour Fitness*, *Peleg*, and *Serpa* govern here. (*Peng, supra*, 219 Cal.App.4th at pp. 1473-1474.) Because any modification of the arbitration agreement by the Bank is subject to a “covenant of good faith and fair dealing [that] would preclude any change that undermined the employee’s rights” (*Serpa, supra*, 215 Cal.App.4th at p. 707), the modification provision did not make the arbitration agreement substantively unconscionable.

Edwards argues for a different result based on *Sparks v. Vista Del Mar Child and Family Services* (2012) 207 Cal.App.4th 1511 (*Sparks*), and *Ingle v. Circuit City Stores*,

Inc. (9th Cir. 2003) 328 F.3d 1165 (*Ingle*). In both cases, the courts stated that arbitration agreements were substantively unconscionable because the employer had the ability to modify them at will. (*Sparks, supra*, 207 Cal.App.4th at pp. 1514, 1516, 1523; *Ingle, supra*, 328 F.3d at pp. 1172-1173, 1179, fn 23.) We agree with the *Serpa* court that *Sparks* is unpersuasive because it did not consider “*24 Hour Fitness* and its application of the implied covenant of good faith and fair dealing.” (*Serpa, supra*, 215 Cal.App.4th at p. 708, fn. 7.) *Ingle* is unpersuasive for the same reason.

In view of our conclusion that the arbitration agreement is not substantively unconscionable, we need not decide whether the agreement is procedurally unconscionable. (*Armendariz, supra*, 24 Cal.4th at p. 114.)

III. DISPOSITION

The order denying the motion to compel arbitration is reversed, with directions to grant the motion. Each party is to bear its own costs on appeal.

Siggins, J.

We concur:

Pollak, Acting P.J.

Jenkins, J.