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Posted at 7:07 AM on April 30, 2010 by Sheppard Mullin

California's Fourth Appellate District Holds That Named Plaintiffs In Putative Class Actions Alleging Misrepresentation And Deception Under The UCL'S "Unlawful" Prong Must Plead Actual Reliance

By Philip F. Atkins-Pattenson and Martin White

On April 19, 2010, California's Fourth Appellate District decided two companion cases – *Durell v. Sharp Healthcare*, --- Cal.Rptr.3d ----, 2010 WL 1529322, Cal.App. 4 Dist., April 19, 2010 (NO. D054261) and *Hale v. Sharp Healthcare*, --- Cal.Rptr.3d ----, 2010 WL 1529329, Cal.App. 4 Dist., April 19, 2010 (NO. D054637) – that mark a potentially significant development in pleading standards under California's Unfair Competition Law, California Business & Professions Code sections 17200, *et seq*. ("UCL"). Broadly speaking, both *Durell* and *Hale* stand for the proposition that named class plaintiffs alleging a UCL violation under the "unlawful" prong of the statute must now also plead "actual reliance" when the conduct challenged involves "misrepresentation and deception." Stated another way, plaintiffs alleging unlawful conduct stemming from misrepresentation and deception under the UCL now must actually have relied on the defendant's alleged misrepresentation; proximate cause or a mere "factual nexus" is insufficient. Both decisions extend the reasoning of the California Supreme Court's recent decision in *In re Tobacco II Cases* (2009) 46 Cal.4th 298 (*Tobacco II*), which addressed the requirements for pleading standing under the UCL's "fraud" prong, to UCL class actions brought under the "unlawful" prong, at least where the conduct challenged involves misrepresentation and deception.

The facts of *Durell* and *Hale* are virtually indistinguishable. In both cases, the named plaintiff in these putative class actions were uninsured, received medical treatment at defendant's hospital emergency room, and received large bills for their treatments, which they contend were excessive and greater than the amounts charged for the same services where the emergency room patient was covered by Medicare or private insurance. Despite similar underlying facts, the Fourth Appellate District reached different conclusions on defendant's pleading challenges. In *Durell*, the Court affirmed the trial court's Judgment, which sustained Sharp's demurrer without

leave to amend. In *Hale*, the same panel reversed the trial court's sustaining of Sharp's demurrer, finding that the named plaintiff had stated a cause of action for violation of the UCL's "unlawful" prong. These different results can be explained by one word: causation.

The UCL's "Unlawful" Prong

The *Durell* Court looked first to whether Durell's complaint had alleged a violation of the "unlawful" prong under the UCL. Generally speaking, the "unlawful" prong "borrows violations of other laws and treats them as unlawful practices that the UCL makes independently actionable. . . . Virtually any law – federal, state or local – can serve as a predicate for an action under Business and Professions Code section 17200."

Durell alleged that the predicate violation was Sharp's alleged violations of the Consumers Legal Remedies Act, Civ. Code sections 1750, *et seq*. ("CLRA"), which prohibits, *inter alia*, a person from "advertising goods or services with intent not to sell them as advertised." (Civil Code § 1750(a)(9)). Specifically, Durell alleged that Sharp's web site included "a number of misrepresentations," including statements that Sharp's goal was "to offer quality care and programs" in a "cost-effective and accessible manner." This, Durell alleged, was a "false" promise "intended to induce patients to seek treatment at Sharp facilities." Further, Durell alleged that Sharp's Agreement for Services stated that it would charge him "usual and customary charges for services, when it actually charged him substantially higher rates in applies only to uninsured parties."

The question before the Court was whether Durell had standing to allege this claim. Proposition 64, approved by California voters in 2004, the Court noted, amended the UCL so that plaintiffs under *any* prong must show that "he or she has suffered injury in fact and hast lost money or property as a result of the unfair competition." The Court turned to the question: what does the phrase "as a result of" mean?

To answer this question, the Court looked to the California Supreme Court's decision in *Tobacco II*. In *Tobacco II*, the California Supreme Court addressed this question with respect to the "fraud" prong of the UCL, but had expressly reserved judgment on the question of what the phrase "as a result of" meant with respect to the "unlawful" prong of the UCL – neither Durell nor Hale had alleged violations of the UCL's "fraud" prong, presumably in an effort to avoid the reliance requirement. *Tobacco II* holds that the "as a result of" language "imposes an actual reliance requirement on plaintiffs prosecuting a private enforcement action under the UCL's fraud prong."

The *Durell* Court extended this requirement to certain types of cases alleging violations of the "unlawful" prong. "[T]he reasoning of *Tobacco II* applies equally to the 'unlawful' prong of the UCL when, as here, the predicate unlawfulness is misrepresentation and deception." The court went on, stating, "[a] customer's burden of pleading causation in a UCL action should hinge on the nature of the alleged wrongdoing rather than the specific prong of the UCL the consumer invokes. This is a case in which the 'concept of reliance' unequivocally applies, and omitting an actual reliance requirement when the defendant's alleged misrepresentation has not deceived the plaintiff would blunt Proposition 64's intended reforms."

Having concluded that Durell had to show “actual reliance” under the UCL’s “unlawful” prong, the Court then examined the sufficiency of the allegations in Durell’s complaint, and concluded that it did not “allege Durell relied on either Sharp’s Web site representations or on the language in the Agreement for Services in going to Sharp[‘s Hospital] or in seeking or accepting services once he was transported there. Instead, the Court found that Durell had merely alleged that “as a proximate result of Sharp’s unlawful business practices” the class had “suffered economic damages.” This was insufficient and was “the type of ‘factual nexus’ causation” the Supreme Court had “rejected in *Tobacco II* in the context of claimed misrepresentation and deception.” The Court affirmed the Judgment sustaining Sharp’s demurrer without leave to amend.|

As noted, in the companion *Hale* case, the same appellate panel came to a different result in a case involving similar facts. In *Hale,* the named plaintiff also alleged that Sharp had violated the “unlawful” prong of the UCL by violating the same provisions of the CLRA. Unlike *Durell*,however, the named plaintiff satisfied the standing requirement because her complaint alleged that “the Admission Agreement obligates her to pay Sharp the balance on her account. Thus she faces at least an *imminent* invasion or injury to a legally protected interest.” This, the Court found, was “not the type of action Proposition 64 was intended to squelch.”

The Court also found the allegations of reliance to be sufficient, as Hale alleged that she had “signed the Admission Agreement, and at the time of signing the contract, she was *expecting* to be charged ‘regular rates,’ and certainly not the grossly excessive rates that she was subsequently billed.” This, the Court found, under *Tobacco II*, was sufficient to allege “actual reliance” because “the difference between ‘expecting’ to be charged regular rates and ‘relying’ on being charged regular rates is a distinction without a difference.” On that basis, the Court reversed the Judgment.

<u>Conclusions</u>

Durell and *Hale*’s holdings that a named plaintiff in a UCL class action claiming violations of the “unlawful” prong must plead and prove actual reliance, at least where the conduct challenged involves a defendant’s misrepresentation and deception, is a natural – and logical – extension of the Supreme Court’s reasoning in *Tobacco II*. At least in this category of cases, UCL plaintiffs cannot use the “unlawful” prong as end run around the pleading and proof requirements that the Supreme Court in *Tobacco II* required of plaintiffs alleging violations of the UCL’s “fraud” prong. Left unanswered by these two cases is the question of whether the holdings in *Durell* and Hale will have application to allegations of “unlawful” conduct not involving misrepresentation and deception.