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UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

ELENA DEL CAMPO on behalf of herself and all others similarly situated, *Plaintiffs*, v. GEORGE KENNEDY, AMERICAN CORRECTIVE COUNSELING SERVICES, INC., BRUCE RAYE, DONALD R. MEALING, LYNN R. HASNEY and DOES 1 through 20. *Defendants*.	Civ. No. 01-21151 JW CLASS ACTION **PLAINTIFFS' OPPOSITION TO DEFENDANTS' MOTION TO DISMISS** Date: July 10, 2006 Time: 9:00 a.m. Courtroom 8
AND CONSOLIDATED ACTION	Civ. No. 03-02691 JM

TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

INTRODUCTION 1

STATEMENT 2

A. Criminal Prohibitions on Fraudulent Check Writing Present Serious Dangers of Abuse. 2

B. California Law Permits Counties to Establish "Check Diversion" Programs, But Only Within Strict Limits. 4

C. Allegations In the Complaint. 5

ARGUMENT 9

I. PLAINTIFFS HAVE STATED CLAIMS UNDER THE UNITED STATES AND CALIFORNIA CONSTITUTION UPON WHICH RELIEF MAY BE GRANTED. 9

A. The Plaintiffs Were Deprived of Property Interests Protected by the Due Process Clause. 9

B. The Plaintiffs' Property Was Extracted Through Misrepresentation, Duress, and Coercion. 12

II. THE RES JUDICATA DOCTRINE DOES NOT BAR THE PLAINTIFFS' CONSTITUTIONAL CHALLENGES. 19

CONCLUSION 24

TABLE OF AUTHORITIES

CASES

AVX Corp. v. Cabot Corp.,
424 F.3d 28 (1st Cir. 2005) 20, 21

Aerojet-General Corp. v. Askew,
511 F.2d 710 (5th Cir. 1975) 22

Aguilera v. Pirelli Armstrong Tire Corp.,
223 F.3d 1010 (9th Cir. 2000) 21

Allen v. Leis,
213 F. Supp. 2d 819 (S.D. Ohio 2002) 10

Angarita v. St. Louis County,
981 F.2d 1537 (8th Cir. 1992) 17

Burnham v. Commonwealth,
15 S.W.2d 256 (Ky. 1929) 2

In re Byrd,
256 B.R. 246 (Bankr. E.D.N.C. 2000) 14

Cardwell v. Lewis,
417 U.S. 583 (1974) 11

Clausen Co. v. Dynatron/Bondo Corp.,
889 F.2d 459 (2d Cir. 1989) 21

Connecticut v. Doehr,
501 U.S. 1 (1991) 10, 12

Donovan v. Mazzola,
761 F.2d 1411 (9th Cir. 1985) 20

Ethnic Employees of the Library of Congress v. Boorstin,
751 F.2d 1405 (D.C. Cir. 1985) 22

Favish v. Office of Independent Counsel,
217 F.3d 1168 (9th Cir. 2000) 22

Federated Department Stores, Inc. v. Moitie,
452 U.S. 394 (1981) 20

Fuentes v. Shevin,
407 U.S. 67 (1972) 10, 12

Goldyn v. Hayes,
444 F.3d 1062 (9th Cir. 2006) 4

Hargray v. City of Hallandale,
57 F.2d 1560 (11th Cir. 1995) 17, 18

Harris v. State,
378 So. 2d 257 (Ala. Crim. App. Ct. 1979) 2

Headwaters, Inc. v. U.S. Forest Services, Inc.,
399 F.3d 1047 (9th Cir. 2005) 22, 23

Homer v. Ferron,
362 F.2d 224 (9th Cir. 1966) 21

Irwin v. Mascott,
370 F.3d 924 (9th Cir. 2004) 23

Jackson v. Hayakawa,
605 F.2d 1121 (9th Cir. 1979) 21, 22

In re Jenson,
980 F.2d 1254 (9th Cir. 1992) 20

Johnson v. General Motors Corp.,
598 F.2d 432 (5th Cir. 1979) 22

Keyes v. District of Columbia,
372 F.3d 434 (D.C. Cir. 2004) 16

Leheny v. City of Pittsburgh,
183 F.3d 220 (3d Cir. 1999) 17

Los Angeles Branch NAACP v. Los Angeles Unified School District,
750 F.2d 731 (1985) 22

Malone v. United States Postal Service,
526 F.2d 1099 (6th Cir. 1975) 16, 17

Norton v. City of Chicago,
690 N.E.2d 119 (Ill. Ct. App. 1997) 13

In re Marino,
181 F.3d 1142 (9th Cir. 1999) 20

Marshall County Board of Education v. Marshall County Gas District,
992 F.2d 1171 (11th Cir. 1993) 9

Montana v. United States,
440 U.S. 147 (1979) 22

Moody v. Mississippi,
716 So. 2d 562 (Miss. 1998) 3

North Georgia Finishing, Inc. v. Di-Chemical, Inc.,
419 U.S. 601 (1975) 12

Parker v. Board of Regents of Tulsa Jr. College,
981 F.2d 1159 (10th Cir. 1992) 17

Parratt v. Taylor,
451 U.S. 527 (1981) 10

People v. Becker,
30 P.2d 562 (Cal. Ct. App. 1934) 2

People v. North,
182 Cal. Rptr. 126 (Cal. Ct. App. 1982) 2

People v. Vinnola,
494 P.2d 826 (Colo. 1972) 2, 3

Pollard v. Cockrell,
578 F.2d 1002 (5th Cir. 1978) 22

Richards v. Jefferson County, Alabama,
517 U.S. 793 (1996) 23

Senza-Gel Corp. v. Seiffhart,
803 F.2d 661 (Fed. Cir. 1986) 21

In re Reisen,
2004 WL 764628 (Bankr. N.D. Iowa 2004) 14, 15

In re Simonini,
282 B.R. 604 (Bankr. W.D.N.C. 2002) 14, 15

Sniadach v. Family Finance Corporation of Bay View,
395 U.S. 337 (1969).....11, 12, 16

South Central Bell Telephone Co. v. Alabama,
526 U.S. 160 (1999).....23

Spreen v. Brey,
961 F.2d 109 (7th Cir. 1992) 17, 19

State v. Orth,
359 S.E.2d 136 (W.Va. 1987).....3

Stewart v. U.S. Bancorp,
297 F.3d 953 (9th Cir. 2002) 20

Stone v. University of Maryland Medical System Corp.,
855 F.2d 167 (4th Cir. 1988) 13, 17, 19

Tice v. American Airlines,
162 F.3d 966 (7th Cir. 1999) 22

Tolbert v. State,
321 So. 2d 227 (Ala. 1975).....3

United States v. Farhad,
190 F.3d 1097 (9th Cir. 1999) 19

United States v. Griffin,
530 F.2d 739 (7th Cir. 1976) 13

United States v. Jacobsen,
466 U.S. 109 (1984).....11

Wolford v. Angelone,
38 F. Supp. 2d 452 (W.D.Va. 1999) 19

Wright v. Schock,
742 F.2d 541 (9th Cir. 1984) 21

STATUTES AND RULES

28 U.S.C. § 1291 20

Cal. Penal Code § 476a 2, 4, 6, 7

Cal. Penal Code § 1001 4

Cal. Penal Code § 1001.60 4

Fed. R. Civ. P. 54(b)....20, 21

ARTICLES

Geoffrey C. Hazard, Jr. et al., An Historical Analysis of the Binding Effect of Class Suits, 146 U. Pa. L. Rev. 1849 (1998) 22

Josephine R. Potuto, *A Review of the Bad Check Offense and the Law Enforcement Debt Collector*, 65 Neb. L. Rev. 242 (1986). 4

Comment, *Imprisonment for Debt and the Constitution* 1970 L. & Soc. Order 659 (1970). 2

Note, *Pretrial Diversion from the Criminal Process,* 83 Yale L.J. 827 (1981) 4

INTRODUCTION

This lawsuit challenges the constitutionality of a debt collection operation run by American Corrective Counseling Services, Inc., and its affiliates (collectively "ACCS") under contract with local district attorneys. Under ACCS's business model, a district attorney's office rents its name and authority to ACCS, which then holds itself out as the district attorney and uses false threats of prosecution to coerce consumers who have written dishonored checks into paying not only the check amount, but also unlawful collection fees. ACCS then splits the profits with the district attorney.

The case raises four constitutional challenges to the ACCS program: (1) that the program violates due process because the defendants have a substantial financial interest in maintaining a high rate of collections; (2) that the program violates both equal protection and due process because it extracts fees from people, under the threat of criminal prosecution, without regard for their ability to pay; (3) that the program violates the most basic command of the due process clause: the state or entities cloaked in its authority may not take plaintiffs' property without providing some meaningful opportunity to contest the deprivation; and (4) that the defendants violate due process by making baseless threats of prosecution solely to extract the payment of fees, knowing that the fees are unlawful and that no probable cause determination has been made by a prosecutor.

In their motion to dismiss, the defendants do not address the merits of each of these constitutional challenges. Instead, with virtually no supporting legal authority, they ask the Court to dismiss *all* of the claims on the theory that plaintiffs' payments in response to ACCS's collection demands do not implicate a property interest and were purely voluntary. Neither contention has merit. It is well-settled that a deprivation of money, even money that is allegedly

owed to someone else, implicates a protected interest in property and that misrepresentation and coercion render an ostensibly voluntary deprivation involuntary. Plaintiffs allegations are more than sufficient to withstand defendants' motion to dismiss.

STATEMENT

A. Criminal Prohibitions on Fraudulent Check Writing Present Serious Dangers of Abuse.

In California, writing a check that is returned for insufficient funds, without more, is not a crime. Under Section 476a of the California Penal Code, it is a crime only if the check writer *intends to defraud* the recipient. The California courts have long described "intent to defraud the person to whom the check was delivered" as "the gist of the offense," *People v. North*, 182 Cal. Rptr. 126, 128 (Cal. Ct. App. 1982), for which "no presumption of law will suffice." *People v. Becker*, 30 P.2d 562, 563 (Cal. Ct. App. 1934). "The rationale is that the statute punishes the crime of intent to defraud rather than the inability to pay the debt." *Harris v. State*, 378 So.2d 257, 260-61 (Ala. Crim. App. Ct. 1979).

A statute that prohibits the writing of dishonored checks without an element of fraudulent intent becomes "no more than a device to force payment of debt." *People v. Vinnola*, 494 P.2d 826, 831 (Colo. 1972). "Such a result strikes at the very foundation of our system of criminal justice" and has repeatedly been held to violate due process, equal protection, and constitutional prohibitions on punishment for debt. *Vinnola*, 494 P.2d at 831 (striking down bad check statute on due process and equal protection grounds). Judicial scrutiny of these statutes is not new. *See*, *e.g.*, *Burnham v. Commonwealth*, 15 S.W.2d 256, 258 (Ky. 1929) (striking down bad check statute that was "palpably designed merely to enforce the collection of debts" and lacked a constitutionally-required indigency defense); *see generally Comment, Imprisonment for Debt and the Constitution*, 1970 L. & Soc. Order 659 (1970).

Given these dangers, courts have long warned that the use of bad check laws "should be closely scrutinized," *Vinnola*, 494 P.2d at 828, and that even facially constitutional statutes, like California's, "lend themselves to use by the unscrupulous who seek only payment of debts and have no interest in criminal prosecution other than as a means of collecting money allegedly due them," which is "an unconstitutional application of such statutes." *Tolbert v. State*, 321 So.2d 227, 232 (Ala. 1975) ("This court has repeatedly condemned the use of threat of prosecution as a means of collection of worthless checks.").

Some courts have also taken note of the abuses that can occur when financially interested parties are permitted to have a hand in enforcement and when the normally salutary practice of "pretrial diversion"—which ordinarily occurs only after the filing of criminal charges—is twisted into a tool for debt collection. "Allowing the District Attorney, the county's chief law enforcement officer, to process civil debt as a criminal proceeding, flies in the face of our constitution . . . . [W]hen the District Attorney's bread and butter depends upon, or is enriched by, the fees collected in bad check cases, the special interests arising therefrom cannot be ignored." *Moody v. Mississippi*, 716 So.2d 562, 567 (Miss. 1998). In *Moody*, the Mississippi Supreme Court held that "a standard practice of extracting a set fine from persons accused of writing bad checks on the pain of suffering full criminal prosecution for failure do so," in the context of a pretrial diversion program, violates the Equal Protection Clause. *Id.* at 563. In another bad check case, the West Virginia Supreme Court declared that "[t]he prosecutorial services of the state are not for private use in civil debt collection" and held that prosecutors "are not authorized to divert cases prior to bringing formal charges where there is probable cause to believe the accused is guilty." *State v. Orth*, 359 S.E.2d 136, 141 (W.Va. 1987) (observing that the "threat of prosecution for the failure to make the required payments smacks of the generally discredited practice of imprisonment for

debts"); *see generally* Josephine R. Potuto, *A Review of the Bad Check Offense and the Law Enforcement Debt Collector*, 65 Neb. L. Rev. 242 (1986).

The types of abuses raised in this lawsuit, therefore, are not new and have not escaped the attention of courts. What makes the ACCS operation unique is that it has standardized these abuses and transformed them into a profitable business model that it can sell to local prosecutors. The Constitution does not permit such abuses to go unchecked. As the Ninth Circuit recently observed in a bad check case, while a creditor may always "try to collect its money . . . using the debt collection procedures it would employ for any other" debt, the mere failure to pay an obligation "is not a crime; the days of imprisoning insolvent debtors are long gone." *Goldyn v. Hayes*, 444 F.3d 1062, 1069 (9th Cir. 2006). "Perhaps some would say that [the check writer's] innocence is a mere technicality, but that would miss the point. In a society devoted to the rule of law, the difference between violating or not violating a criminal statute cannot be shrugged aside as a minor detail." *Id.* at 1070.

B. California Law Permits Counties to Establish "Check Diversion" Programs, But Only Within Strict Limits.

In 1985, Califiornia's Legislature enacted legislation to permit county district attorneys, with the approval of their county board of supervisors, to create pretrial "bad check diversion programs." Cal. Penal Code § 1001.60, *et seq*. [1]

District Attorney Must Find Probable Cause. The statute limited these programs to cases in which "there is *probable cause* to believe that there has been a violation of Section 476a." *Id.* § 1001.60. Although a county may choose a private contractor to administer the program, only

[1] Ordinarily, "[p]retrial diversion refers to the procedure of postponing prosecution of an offense filed as a misdemeanor either temporarily or permanently at any point in the judicial process from the point at which the accused is charged until adjudication." Cal. Penal Code § 1001; *see generally* Note, *Pretrial Diversion from the Criminal Process*, 83 Yale L.J. 827 (1981).

"[t]he *district attorney* may refer a bad check case to the diversion program." *Id.* § 1001.61; *id.* § 1001.62. ("*[T]he district attorney* shall determine if the case is one which is appropriate to be referred to the bad check diversion program."). Under the ACCS business model, however, the district attorney makes no probable cause determination before collection begins.

Limits on Fees. The statute also places strict limits on the fees that may be charged. The statute provides that "[a] district attorney may collect a fee if his or her office collects and processes a bad check," but that "[t]he amount of the fee shall not exceed thirty-five dollars ($35) for each bad check in addition to the actual amount of any bank charges incurred by the victim as a result of the offense." *Id.* § 1001.65. "If the district attorney elects to collect any fee for bank charges . . . that fee shall be paid to the victim," but "[i]n no event shall" that charge "exceed ten dollars ($10) per check." *Id*. ACCS routinely demands fees of $170 or more per check.

Only A Court, After Determining Ability to Pay, May Assess Class Fees. The statute permits a charge for a diversion class *only* after a criminal complaint is filed following a check writer's failure to comply with the terms of the diversion program. In that event, "the court, after conviction . . . shall make inquiry into the financial condition of the defendant and, upon a finding that the defendant is able in whole or part to pay the expense of the education class, the court may order him or her to pay for all or part of that expense." *Id.* § 1001.65. Nevertheless, ACCS routinely charges a "class fee" of up to $150, without regard for an individual's ability to pay.

C. Allegations In The Complaint

1. ACCS and Its Affiliates Threaten Prosecution Without Probable Cause.

Merchants that participate in the ACCS program refer dishonored checks directly to ACCS for collection. Complaint ¶ 71. They do not provide ACCS with any information not on the face of the check, *id.*, and they do not allege that the check writers intended to defraud or knew of

insufficiency of funds—the requirements for a violation of Cal. Penal Code § 476a. *Id.* ¶ 81(d). Upon receiving only the check information—and without any review by a prosecutor—ACCS sends official-looking notices on district attorney letterhead threatening check writers with criminal prosecution if they do not immediately enroll in its "Bad Check Restitution Program." *Id.* ¶¶ 41, 45, 50, 56, 66, 81(e).

The notices inform check writers that the District Attorney has received an "INCIDENT REPORT alleging you violated Penal Code 476a." *Id.* Ex. 1, 6, 9, 11. The notice states: "YOU MAY AVOID A COURT APPEARANCE if you agree to enroll in the Santa Clara District Attorney's Bad Check Restitution Program." *Id.* If plaintiffs do not respond to the initial notice, ACCS sends a second demand. *Id.* ¶¶ 41, 46, 51, 57, 59, 67, with more forceful and threatening language:

> "Your failure to respond NOW may result in the referral of this crime report for CRIMINAL PROSECUTION!"
>
> "IF YOU WISH TO AVOID POTENTIAL ARREST AND PROSECUTION, YOU NEED TO CALL THIS OFFICE IMMEDIATELY!"

Id. Ex. 5, 10, 13. If plaintiffs do not respond to the second letter, ACCS sends a third letter, *id.* ¶¶ 42, 54, 68:

> "PLEASE CONTACT THIS OFFICE TO AVOID CRIMINAL PROSECUTION"
>
> "Criminal charges . . . are being prepared for review by a deputy prosecutor."

Id. Ex. 8, 14. ACCS thus commences its collection procedures and repeatedly threatens criminal prosecution without any indicia of probable cause to conclude that plaintiffs have the requisite criminal intent. *Id.* ¶¶ 74, 110(a). Even plaintiffs who inform ACCS that their dishonored check was the result of a bona fide mistake are told that they are nonetheless liable and must enroll in the

program to avoid criminal prosecution—despite ACCS's actual knowledge that the requirements of § 476a cannot be satisfied. *Id.* ¶ 75.

2. ACCS and Its Affiliates Use Misrepresentation And Coercion To Extract Fees.

ACCS extracts fees from plaintiffs through numerous coercive and misleading techniques. ACCS informs plaintiffs that the district attorney has received an "Incident Report" alleging that plaintiffs violated Cal. Penal Code § 476a. *Id.* ¶ 80(d). The truth is that merchants do not generally allege that dishonored check writers have violated Cal. Penal Code § 476a. *Id.* ¶ 81(d). ACCS informs plaintiffs that they have committed a crime by writing a dishonored check. *Id.* ¶ 80(e). The truth is that no evidence has crossed a prosecutor's desk; the district attorney has not determined that there is probable cause to believe that the plaintiff committed a crime. *Id.* ¶ 80(e). ACCS threatens plaintiffs with criminal prosecution unless they participate in the diversion program. *Id.* ¶¶ 80(e), (g). The truth is that the district attorney rarely, if ever, initiates criminal prosecution against dishonored check writers who do not enroll in the diversion program. *Id.* ¶¶ 81(f)-(g). ACCS informs plaintiffs that the district attorney operates the Bad Check Restitution Program and that all communications regarding the diversion program are sent and received by the district attorney's office. *Id.* ¶¶ 80(a)-(c). The truth is that ACCS operates all facets of the diversion program, with little or no supervision by the district attorney. *Id.* ¶¶ 81(a)-(c).

3. The Named Plaintiffs Were Deprived Of Protected Interests In Property Based on Misrepresentation and Coercion.

***Elena del Campo*.** In July 2002, in connection with returned checks of $81.99 and $240.00, ACCS demanded that Ms. del Campo pay $536.99 (the amount of the checks + $35 administrative fee per check + $10 bank charges per check + a class fee of $125). *Id.* ¶¶ 43-45. Ms. Del Campo paid $411.99, in payment of the check amounts, the bank charges, and the administrative fees. *Id.* ¶ 47. ACCS, rather than paying the merchant the check amounts and

keeping only the $90.00 in fees, kept half of del Campo's payment, without notifying her or the merchant of its actions, thus leaving the merchant and Ms. del Campo with an outstanding debt between them. *Id.* ¶ 48. In October 2001, in connection with a returned check of $95.02, ACCS demanded that Ms. del Campo pay the amount of the check plus $170.00 in various illegal fees (totaling $265.02). *Id.* ¶ 36. She mailed ACCS only the check amount of $95.02. *Id.* ¶ 37. Because this payment covered only the check amount and not any of the $170.00 in fees, ACCS—without the merchant or plaintiff's knowledge or consent—converted 50% of this amount ($47.51) for its own use, and sent the remaining $47.51 to the merchant along with a notice that plaintiff had only paid half her balance to the merchant. *Id.* ¶¶ 38-40.

Ashorina Medina. Ms. Medina sent ACCS $210.00 as payment for a returned check in the amount of $250.00. *Id.* ¶¶ 49, 52. ACCS, which had demanded payment of $250 plus $170.00 in fees, converted 50% of Medina's payment ($105.00) to its own use, and reported to the merchant that she had paid only $105.00 of her $250.00 debt, thus leaving the merchant and Ms. Medina with a $145 outstanding debt between them. *Id.* ¶ 53.

Lisa Johnston. Ms. Johnston, after receiving demands from ACCS, made a series of payments totaling $110.58. *Id.* ¶¶ 60, 62-63. ACCS, without Ms. Johnston's knowledge or consent, deducted its own fees from the amounts paid to cover only the amount of the returned check, leaving the merchant and Ms. Johnston with an outstanding debt between them. *Id.* ¶¶ 64, 66.

4. The ACCS Program Injects An Impermissible Profit Motive Into The Enforcement Process.

As with any run-of-the-mill collection agency, ACCS—and its commission-earning employees—receives a share of what it collects. *Id.* ¶ 29. Defendant George Kennedy also receives a portion of the fees that ACCS collects *Id.* ¶ 30. All of the defendants receive some

share of the money ACCS collects in operating its Bad Check Restitution Programs in California. *Id.* ¶ 33. The defendants thus operate the Bad Check Restitution Program for profit, *id.* ¶ 81(a), and have a direct and substantial financial interest in assessing and collecting the maximum possible fees. *Id.* ¶ 111.

5. ACCS Provides Consumers No Opportunity To Contest the Fees Assessed Or The Accusations Against Them.

ACCS does not offer plaintiffs the opportunity to contest the accusations against them or the fees assessed before a neutral decision-maker and does not determine individuals' ability to pay before making demands for payment. *Id.* ¶ 110. ACCS provides a telephone number for plaintiffs to contact if plaintiffs received the notice in error, were not properly notified, or already paid the merchant, *id.* Ex. 1, 6, 9, 11, but that telephone line is staffed by ACCS employees, *id.* ¶ 81(c), who have a personal financial interest in collections and are not neutral decision-makers. *Id.* ¶ 29.

ARGUMENT

I. PLAINTIFFS HAVE STATED CLAIMS UNDER THE UNITED STATES AND CALIFORNIA CONSTITUTION UPON WHICH RELIEF MAY BE GRANTED.

A. The Plaintiffs Were Deprived of Property Interests Protected by the Due Process Clause.

Although they concede that the plaintiffs have "paid various amounts of money" to them as part of the challenged program, the defendants nevertheless contend that "one thing is clear from the Consolidated Complaint: plaintiffs have not been deprived of any liberty or property interest that is more than de minimus [sic] by virtue of defendants' conduct." Def's Br. at 13. This argument is meritless.

To begin with, "[t]he plaintiffs clearly have a property interest in the money they own." *Marshall County Bd. of Educ. v. Marshall County Gas Dist.*, 992 F.2d 1171, 1176 (11th Cir.

1993); *see Allen v. Leis*, 213 F.Supp.2d 819 (S.D. Ohio 2002) (holding that a county jail's policy of charging a "booking fee," which averaged $9.35 and did not exceed $30 per person, violated the Due Process Clause). Ms. Campo paid the defendants a total of at least $507.01 (Complaint ¶ 34-48); Ms. Medina paid a total of at least $210.00 (*id.* ¶¶ 49-54); and Ms. Johnston paid a total of at least $110.58 (*id.* ¶¶ 60-68).[2] Those allegations are all that is necessary to show that a cognizable property interest is at stake.

Defendants cannot seriously contend that the deprivation of plaintiffs' money is a *de minimis* deprivation. "[T]he Court has never held that only . . . extreme deprivations trigger due process concern." *Connecticut v. Doehr*, 501 U.S. 1, 12 (1991). On the contrary, in *Parratt v. Taylor*, 451 U.S. 527, 536 (1981), for example, the Court held that even a $23.50 hobby kit that had been mail-ordered, but not received, by a prisoner was "property" within the meaning of the Due Process Clause. And in *Fuentes v. Shevin*, 407 U.S. 67, 89-90 (1972), the Court explained that the deprivation of even ordinary household items triggers due process protections. "No doubt, there may be many gradations in the 'importance' or 'necessity' of various consumer goods . . . But if the root principle of procedural due process is to be applied with objectivity, it cannot rest on such distinctions. The Fourteenth Amendment speaks of 'property' generally" and "[i]t is not

[2] Plaintiff Miriam Campos has been deprived of neither property nor liberty. *See* Complaint ¶¶ 55-59. She therefore does not assert claims under the first or second counts of the complaint and will not be named as a representative for the relevant subclass, *id*. ¶ 101 ("All members of the umbrella class from whom ACCS collected money in the name of the Santa Clara District Attorney on, or after, December 12, 1999").

the business of a court adjudicating due process rights to make its own critical evaluation of [consumers'] choices and protect only the ones that, by its own lights, are 'necessary.'"[3]

Far from being insignificant, the case for due process protections with respect to plaintiffs' deprivations is particularly compelling—not necessarily because of the size of the amounts (which are not insignificant for people of limited means), but because of the manner in which they are extracted. The Supreme Court has recognized that where, as here, payment on a debt is sought upon pain of some coercive action, such as the garnishment of wages, there is a special need for constitutional safeguards. *See Sniadach v. Family Fin. Corp. of Bay View*, 395 U.S. 337, 341 (1969). In such situations, the "leverage of the creditor . . . is enormous," particularly where the demand includes "not only the original debt but 'collection fees.'" *Id.* The debtor often "is in no position to resist demands for collection fees. If the debt is small, the debtor will be under considerable pressure to pay the debt and collection charges" to become free of the garnishment *Id*. When demands for payment are accompanied by an apparently real threat of criminal prosecution from a prosecutor's office, there can be little doubt that the pressure exerted is similarly "enormous."

Without any supporting authority, defendants' brief argues that the plaintiffs have not suffered a deprivation unless they have paid the full "case balance" demanded by ACCS—*i.e.* the amount of the check and *all* of the various collection fees demanded—and that "[t]o the extent plaintiffs mailed in payments up to the total amount of their respective bad check(s), they have not been deprived of anything that was rightfully theirs to keep in the first place." Defs.' Br. 13.

[3] Those few property interests that the Court has deemed *de minimis* have generally been truly insignificant—the sort of thing that nobody at all would value. *See*, *e.g.*, *United States v. Jacobsen*, 466 U.S. 109 (1984) (holding that a "trace amount" of cocaine used for testing, "the loss of which appears to have gone unnoticed" by the owner and which "had already been lawfully detained," was a *de minimis* property interest); *Cardwell v. Lewis*, 417 U.S. 583, 591-92 (1974) (owner had a *de minimis* interest in paint scrapings from an automobile).

Nothing in due process jurisprudence supports these distinctions. Under *Sniadach* and its progeny, it is well-settled that even the deprivation of *property that one allegedly owes to someone else* is a deprivation of property cognizable under the Due Process Clause. *See, e.g., Doehr*, 501 U.S. 1; *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601 (1975). As the Supreme Court stated when it rejected a similar argument in *Fuentes*, "[t]he Fourteenth Amendment's protection of 'property' . . . has never been interpreted to safeguard only the rights of undisputed ownership." *Id.* at 86. The Court further explained that, "even assuming that the [plaintiffs] had fallen behind in their installment payments, and that they had no other valid defenses, that is immaterial here. . . . To one who protests against the taking of his property without due process of law, it is no answer to say that in his particular case due process of law would have led to the same result because he had no adequate defense upon the merits. It is enough to invoke the procedural safeguards of the Fourteenth Amendment that a significant property interest is at stake." *Id.* at 87.

B. The Plaintiffs' Property Was Extracted Through Misrepresentation, Duress, and Coercion.

Defendants next contend that the plaintiffs have failed to state a due process claim because the challenged program is "voluntary and optional," and therefore does not implicate due process. Defs' Br. 13. They ask the Court to turn a blind eye to their use of misrepresentations and coercion to extract fees from consumers and instead focus on only one fact—that the defendants have included a line in their collection demands describing their program as "optional." The Constitution is not so easily fooled.

1. It is an elementary principle of American constitutional law—across a broad range of contexts, including procedural due process—that even an ostensibly voluntary act is rendered involuntary when misrepresentation or coercion prevent a person's choice from being truly "free

and informed." *Stone v. University of Md. Med. Sys. Corp.*, 855 F.2d 167, 174 (4th Cir. 1988); *see also United States v. Griffin*, 530 F.2d 739, 742-43 (7th Cir. 1976) ("A consent obtained through the use of coercion, whether actual or implicit, is inherently involuntary," and "[t]rickery, fraud, or misrepresentation . . . naturally undermine the voluntariness of any consent."). "Subtle coercion, in the form of an assertion of authority or color of office by the law enforcement officers may make what appears to be a voluntary act an involuntary one." *Id.; cf. Norton v. City of Chicago,* 690 N.E.2d 119, 125 (Ill. Ct. App. 1997) (concluding that notices of parking violations sent by a private contractor on behalf of local government, which "urged recipients to pay the fines in lieu of steeper penalties or court action," were "coercive enough to render plaintiffs' payment involuntary").

The facts alleged in the complaint are more than enough to show that the defendants extract their unlawful fees in a manner that renders plaintiffs' decisions to "enroll" in the collection program involuntary. Despite a lack of good cause to threaten people with criminal prosecution for fraudulent check-writing, ACCS's threats send an unmistakable signal:

> IF YOU WISH TO AVOID POTENTIAL ARREST AND PROSECUTION, YOU NEED TO CALL THIS OFFICE IMMEDIATELY!
>
> PLEASE CONTACT THIS OFFICE TO AVOID CRIMINAL PROSECUTION.
>
> Due to your failure to complete the requirements of the District Attorneys' Bad Check Restitution Program . . . we are now initiating formal prosecution proceedings against you. Criminal charges of PC 476(a) . . . are being prepared[.]

Complaint ¶¶ 38, 39, 48, 43, 51, 64, 65. At the time these threats are made, no prosecutor has made a determination of probable cause and no evidence of fraudulent intent has been gathered. Complaint ¶ 74. This problem is compounded by the fact that when consumers call ACCS—believing they are speaking with neutral employees of the District Attorney's Office rather than collection agency employees who work on commission—and "explain that the check was returned

because of a mistake made by the check writer or by the bank," they are told they are "nonetheless liable, and must pay the money being demanded to avoid the possibility of prosecution." Consolidated Compl. ¶ 75. At the appropriate stage in the litigation, the plaintiffs will present evidence obtained in discovery—including an ACCS employee handbook and telephone scripts—indicating that ACCS operators, who receive commissions on the amounts they collect, may be engaging in even more coercive and deceitful conduct over the telephone.[4]

This court can also draw upon the experience of a handful of courts that have examined the collection notices sent by District Attorney Bad Check Diversion programs, including ACCS, and have found that the notices are coercive and render the programs involuntary. *See In re Byrd*, 256 B.R. 246 (Bankr. E.D.N.C. 2000); *In re Simonini*, 282 B.R. 604 (Bankr. W.D.N.C. 2002), *vacated on other grounds*, 2003 WL 21500197 (4th Cir. 2003); *In re Reisen*, 2004 WL 764628 (Bankr. N.D. Iowa 2004). As these courts have recognized, defendants' characterization of their scheme strains credulity.

In *In re Byrd*, for example, the court reviewed the Clark County, Nevada District Attorney's Bad Check Diversion Unit's eligibility criteria, procedures, and notices and, based on this review, gave "no credence to Clark County's argument that 'Byrd *voluntarily* chose to enter the deferred prosecution program.'" 256 B.R. at 253 (emphasis in original). Instead, the court found that "Byrd was prompted *under pressure* to pay an amount equivalent to the debt . . . plus fines, without having the benefit of judicial overview or discretion." *Id.* at 254 (emphasis added). The court observed that the County's "characterization of the program [was] wholly untenable"

[4] In addition, plaintiffs' counsel have recently learned that ACCS may be making recordings of its telephone calls with consumers. These recordings would provide a more complete picture of the nature and scope of ACCS's deceptive practices. On June 16, 2006, Magistrate Judge Trumbull issued an order requiring ACCS to refrain from destroying these recordings pending a hearing on the matter on August 16, 2006.

and that "the County's actions are troubling, and its lack of candor regarding the purposes" of the program warranted special mention. *Id.* at 253.

Similarly, in *In re Simonini*, the court concluded that the bad check diversion program's "prosecution" was merely "debt collection in sheep's clothing." 282 B.R. at 614. Even though check writers were theoretically given a "choice" between paying and facing criminal prosecution, the program was nothing more than a "*mandatory* restitution program" that was "a blatant attempt to collect debt for private persons." *Id.* (emphasis added). These conclusions were based on a thorough examination of the collection notices, which were admitted into evidence along with an affidavit submitted by the program's counsel. The court observed that "[s]ome passages suggest, with little ambiguity," that imminent prosecution would be "dropped" upon payment by the check writer. *Id.* at 617. The court made clear that participation in the program could not be considered voluntary:

> *The message is transparent: pay . . . or go to jail.* Taken in sum, the documents place the Debtor in a virtual debtor's gaol by holding the threat of prosecution over his head until he pays in full, at which time the prosecution threat subsides.

Id. The court went so far as to describe the predicament in which the bad check diversion program placed consumers as "a legal box—if not a literal jail—they can place debtors in until payment. Although this might otherwise be said to have the general benefit of protecting the people of [the state] from bad checks, the fact that the threat of prosecution disappears upon payment raises serious questions about who exactly this scheme helps." *Id.*

Finally, in *In re Reisen*, the court concluded that an ACCS-run check diversion program was "not an instrumentality of the Dubuque County Attorney" but a "collection agency" that "exists to facilitate the payment of bad checks" and "operates under typical debt collection rules." 2004 WL 764628, at *3. The court heard testimony from the County Attorney concerning the

program's operations, considered an affidavit filed by ACCS's Regional Manager, and carefully reviewed the demand letters (virtually identical to those at issue here), cataloguing their increasingly ominous references to criminal prosecution. It noted that the first notice "warns [the recipient] that failure to contact the Restitution Program could result in criminal prosecution," that the second notice "threatened [the recipient] with 'potential arrest and prosecution' if she did not contact the Restitution Program immediately," and that the third notice suggested that criminal prosecution was imminent if she did not pay. *Id.* at *3 (quoting notice language, including the statement: "we are now initiating steps toward formal prosecution proceedings against you"). The court concluded that ACCS's notices "were strongly worded and promise the imposition of substantial sanctions including criminal charges unless certain conduct occurs." *Id.* at *7.

In short, ACCS's program is designed to create a situation in which a check writer "is in no position to resist demands for collection fees." *Sniadach*, 395 U.S. at 341. The defendants cannot evade the requirements of due process merely by labeling such deprivations "voluntary and optional."

2. The only authority the defendants cite in support of their voluntariness argument is a case concerning a public employee, a mail carrier named Malone, who sought to challenge his discharge for insubordination. *See Malone v. United States Postal Serv.*, 526 F.2d 1099, 1105 (6th Cir. 1975). Although he was offered an evidentiary hearing, Malone "nevertheless chose to file a grievance" under an alternative administrative procedure. *Id.* He then sued and complained that the grievance procedure violated due process. The court rejected the claim because Malone was offered a *choice* between the two schemes. "A difficult question would be presented if Malone had been given no opportunity to have an evidentiary hearing," but because he was offered and

waived the right to a hearing, there was no due process violation. *Id.* Nobody disputed that Malone's choice was in fact voluntary.

To the extent it is relevant here, then, *Malone* stands for the unremarkable proposition that a person may voluntarily waive his or her constitutional rights. As the court put it, "[a] litigant may voluntarily forego his right to a jury trial, or to present witnesses, or even to be present at his trial, without offending due process." *Id.*

But the question here is *whether* the plaintiffs knowingly, intelligently, and voluntarily waived their due process rights by submitting to ACCS's demands. That is not a question to which *Malone* provides an answer. However, in the very same context to which defendants point—due process protections for public employment—the federal courts, borrowing from non-constitutional federal public employment law, have created an analytical framework that does help to answer these kinds of question. *See Stone*, 855 F.2d at 173-74 (noting that the employment cases "are perfectly apposite analytical sources" because "the dispositive factual inquiry—whether an apparent 'resignation' was in fact involuntary—is essentially the same in both situations"). Every circuit to have addressed the issue has concluded that an employee's "resignation," and thus his or her deprivation of a protected property interest in employment, may be shown to be involuntary by reason of misrepresentation, coercion, or duress. *See, e.g., Spreen v. Brey*, 961 F.2d 109 (7th Cir. 1992); *Angarita v. St. Louis County*, 981 F.2d 1537 (8th Cir. 1992); *Hargray v. City of Hallandale*, 57 F.2d 1560 (11th Cir. 1995); *Stone*, 855 F.2d 167; *Leheny v. City of Pittsburgh*, 183 F.3d 220, 227-28 (3d Cir. 1999); *Parker v. Bd. of Regents of Tulsa Jr. Coll.*, 981 F.2d 1159, 1162 (10th Cir. 1992); *Keyes v. District of Columbia*, 372 F.3d 434 (D.C. Cir. 2004).

These cases permit a showing of involuntary deprivation under a "misrepresentation theory" or a "duress/coercion theory." In *Spreen*, 961 F.2d at 111, for example, the Seventh

Circuit affirmed the denial of the defendant's summary judgment motion because there was a genuine issue of material fact concerning whether the defendant told the plaintiff she would lose her retirement benefits if she did not resign, a fact that would obviously have been material to her decision. The court also explained that "the misleading information can be negligently or even innocently provided"; a showing of intentional misrepresentation is not required. *Id.* at 113. And in *Hargray*, 57 F.3d at 1565, the court confronted a situation in which an employee resigned in response to his employer's threats of criminal prosecution. Although the court ultimately determined that the employee's resignation was voluntary because the employer had gathered ample evidence of probable cause, *id.* at 1569-71, the court made clear that baseless threats of prosecution are sufficient to show involuntariness. Under the misrepresentation theory, a deprivation would be involuntary where the defendant "knew, or reasonably should have known, that the threatened criminal prosecution could not be substantiated." *Id.* at 1571-72. Under the coercion/duress theory, a resignation would be involuntary where the defendant "lacked good cause for the threatened criminal proceedings at the time the alternatives were offered." *Id.* at 1568.

These cases, moreover, hold that deception or coercion can be shown to render a resignation involuntary despite the fact that resignations, based on the rules of ordinary employment law, are *presumed to be voluntary*—a presumption that does not operate here. Here, the presumption runs in the opposite direction because "[w]aivers of constitutional rights are disfavored, and the courts indulge in every reasonable presumption against them. In cases where the validity of a waiver of a constitutional right is at issue, the government has the burden to prove 'an intentional relinquishment or abandonment of a known right or privilege.'" *United States v.*

Farhad, 190 F.3d 1097, 1108 (9th Cir. 1999) (internal citation omitted). Defendants have not satisfied that burden.

Finally, the question of whether the loss of a property interest is the product of misrepresentation, coercion, or duress such that it is an involuntary deprivation for due process purposes is one that can rarely be resolved on the basis of the pleadings alone. Instead, the court must conduct a "factual inquiry into voluntariness" based on an examination of the totality of the circumstances surrounding the deprivation, *Stone*, 855 F.2d at 172-73—an inquiry that often cannot be resolved even on summary judgment. *See*, ***e.g.,*** *Spreen*, 961 F.2d at 111 (holding defendants had "not come forth with evidence showing the *absence* of a genuine issue of material fact as to whether Defendants misled Plaintiff into resigning her employment") (emphasis in original); *Wolford v. Angelone*, 38 F.Supp.2d 452, 459 (W.D.Va. 1999) (finding "genuine issue of material fact as to whether the plaintiff's resignation was involuntary and obtained by coercion or duress"). "The answer to that factual inquiry is dispositive of the constitutional 'deprivation' issue." *Stone*, 855 F.2d at 73.

II. THE RES JUDICATA DOCTRINE DOES NOT BAR THE PLAINTIFFS' CONSTITUTIONAL CHALLENGES.

In another attempt to prevent the Court from considering the constitutional claims on the merits, the defendants argue that the Court's May 2002 dismissal of Elena del Campo's due process claim bars all of the plaintiffs' due process and equal protection claims under the doctrine of res judicata. Defendants' position is meritless. In their March 2, 2006 motion for leave to file the consolidated complaint (Docket #170)—which defendants did not oppose—plaintiffs explained in detail why the 2002 order does not bar even Ms. del Campo from going forward with her constitutional claims, let alone the other named plaintiffs who were not a party to the order.

Plaintiffs incorporate by reference the arguments in that motion and offer the following response to the specific points raised by defendants.

1. Defendants' argument fails to satisfy the first element of res judicata or claim preclusion: that there be a final judgment in the prior case. In a nutshell, the problem with defendants' position is that there was never a final judgment in the *del Campo* action. The order is interlocutory and, under Federal Rule of Civil Procedure 54(b), remains subject to revision by this Court at any time.

"[O]nly a final judgment is res judicata.'" *Donovan v. Mazzola*, 761 F.2d 1411, 1416 (9th Cir. 1985). "To determine the finality of the order," courts "consider the criteria used to determine finality for the purposes of 28 U.S.C. § 1291, on finality as a prerequisite for appealability." *Id.* at 1416. "The fact that a judgment is unappealed ordinarily does not deprive it of preclusive effect. However, the fact that a party was *unable to appeal* from the prior decision militates against giving the decision preclusive effect." *In re Jenson*, 980 F.2d 1254, 1257 n.2 (9th Cir. 1992).

As defendants correctly point out, "[o]rdinarily a dismissal for failure to state a claim is treated as a dismissal on the merits, and there is abundant case law to this effect." *AVX Corp. v. Cabot Corp.*, 424 F.3d 28 (1st Cir. 2005); *see* Def's Br. at 9 (*citing Federated Dep't Stores, Inc. v. Moitie*, 452 U.S. 394 (1981)). What they fail to appreciate, however, is that "Rule 12(b)(6) dismissals have claim-preclusive effect" only where "the dismissal disposed of an entire complaint, not just some subset of the plaintiff's claims." *AVX*, 424 F.3d at 31. The dismissal in *Moitie*, for example, was a dismissal of "all of the actions 'in their entirety.'" *Id.* at 396; *see also Stewart v. U.S. Bancorp*, 297 F.3d 953, 956 (9th Cir. 2002) ("[T]he district court's judgment . . . stated that *the action* was dismissed.") (emphasis added); *In re Marino*, 181 F.3d 1142, 1144 (9th Cir. 1999) ("The bankruptcy court . . . dismissed *the complaint*.") (emphasis added).

Here, however, the order at issue was a ruling that "adjudicates fewer than all the claims or the rights and liabilities of fewer than all the parties" and was therefore (unless certified for interlocutory appeal) "subject to revision at any time before the entry of judgment adjudicating all the claims and the rights and liabilities of all the parties." Fed. R. Civ. P. 54(b). The order, therefore, was both unappealable under Rule 54(b) and non-final for res judicata purposes. This rule has long been settled law in the Ninth Circuit. *See Homer v. Ferron*, 362 F.2d 224, 230 (9th Cir. 1966) (denial of a motion in an action "which is still pending, was not a final and appealable order. Since the denial of that motion might yet be overturned in a future appeal in [the first action,] that unreviewed order of denial could hardly serve as res judicata or work a collateral estoppel in this case."); *accord Clausen Co. v. Dynatron/Bondo Corp.*, 889 F.2d 459, 466 (2d Cir. 1989); *Senza-Gel Cor. v. Seiffhart*, 803 F.2d 661, 667 (Fed. Cir. 1986). Under these circumstances, the order at issue "patently did not constitute a final judgment." *AVX*, 424 F.3d at 31, and "[r]es judicata is simply inapplicable." *Senza-Gel Corp. v. Seiffhart*, 803 F.2d 661, 667 (Fed. Cir. 1986).

2. Because finality is lacking, the Court need go no further in assessing defendants' res judicata argument. That argument, however, also fails the second res judicata requirement: privity between the parties. The privity rule must be applied with great care in class actions: "[W]hen a motion is maintained against an uncertified class, only the named plaintiffs are affected by the ruling. There is no res judicata effect as to unnamed members of the purported class." *Aguilera v. Pirelli Armstrong Tire Corp.*, 223 F.3d 1010, 1013 n.1 (9th Cir. 2000); *accord Wright v. Schock*, 742 F.2d 541, 544 (9th Cir. 1984).

The defendants acknowledge this rule, but state that there are "exceptions" to it. That is not so. Defendants cite *Jackson v. Hayakawa*, 605 F.2d 1121 (9th Cir. 1979), which held that a

decision in an earlier case that, although not formally certified as a class action under Rule 23, "was brought as a class action and *treated by the court as a class action*" was therefore entitled to preclusive effect. *Id.* at 1126 (emphasis added). But just last year, in *Headwaters, Inc. v. U.S. Forest Services, Inc.,* 399 F.3d 1047, 1056 n.8 (9th Cir. 2005), the Ninth Circuit held that *Jackson* does not apply where, as here, the first action was not "treated as a class action" and thus did not create a "de facto class."[5] *Headwaters* also explicitly questioned whether *Jackson* was still good law in light of intervening Supreme Court authority and instead cited the Seventh Circuit's contrary holding that "[u]nless there is a *properly certified* class action . . . normal privity analysis must govern whether nonparties to an earlier case can be bound to the result." *Id.* (citing *Tice v. American Airlines*, 162 F.3d 966, 972-73 (7th Cir. 1999) (emphasis in *Headwaters*). *Headwaters* thus doubly dooms defendants' argument.[6]

Defendants' "virtual representation" argument—which conspicuously relies only on cases from the 1970's—cannot be reconciled with the Supreme Court's more recent decisions in

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[5] *Jackson* thus falls into a small, historical category of decisions according preclusive effect to judgments in "de facto" class actions litigated during the infancy of Rule 23, when courts often did not employ formal class certification procedures. *See*, *e.g.*, *Los Angeles Branch NAACP v. Los Angeles Unified Sch. Dist.*, 750 F.2d 731, 741 (1985) (although a prior action "was never formally certified," "[n]o procedure for such certification existed in California prior to 1973" and the "California courts treated [the suit] as a class action throughout"); *Johnson v. General Motors Corp.*, 598 F.2d 432, 434-45 (5th Cir. 1979); *see also* Geoffrey C. Hazard, Jr. et al., *An Historical Analysis of the Binding Effect of Class Suits*, 146 U. Pa. L. Rev. 1849 (1998) (analyzing the evolving and often inconsistent treatment of preclusion in early class action litigation).

[6] The only other cases defendants cite are plainly inapposite. *Montana v. United States*, 440 U.S. 147 (1979), extended the traditional scope of privity only modestly, to nonparties who "assume control over litigation in which they have a direct financial or proprietary interest. *Id.* at 154-55. Defendants' reliance on *Aerojet-General Corp. v. Askew*, 511 F.2d 710 (5th Cir. 1975), is similarly misplaced. To be sure, *Aerojet* offers "[p]erhaps the broadest statement of the doctrine" of virtual representation, *Ethnic Employees of the Library of Congress v. Boorstin*, 751 F.2d 1405, 1411 n.8 (D.C. Cir. 1985), but that statement was qualified by the Fifth Circuit just three years later in *Pollard v. Cockrell*, 578 F.2d 1002, 1008 (5th Cir. 1978), which held that "[v]irtual representation demands the existence of an express or implied legal relationship in which parties to the first suit are accountable to non-parties who file a subsequent suit raising identical issues."

Richards v. Jefferson County, Alabama, 517 U.S. 793 (1996), and *South Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999); and the Ninth Circuit's decisions in *Headwaters*, 399 F.3d 1047, and *Favish v. Office of Indep. Counsel*, 217 F.3d 1168 (9th Cir. 2000). In *Richards*, and again in *South Central Bell*, the Supreme Court rejected the notion that preclusion could operate against persons who were not parties to the earlier litigation simply because they advanced the same legal claims. And in *Favish* and *Headwaters*, the Ninth Circuit held that parties that shared the same lawyers as litigants in previous suits, raised the same issues, and shared the same abstract interests, were nevertheless not in privity. *See Favish*, 217 F.3d at 1171 (plaintiff, who was lawyer for plaintiff in previous action raising issue, was not barred from bringing subsequent suit); *Headwaters*, 399 F.3d 1047 (environmental groups, which shared same lawyer and raised same issue as previous suit, were not barred from bringing subsequent suit).

Finally, defendants fail even to mention, let alone attempt to meet, the rigorous five-factor test for "virtual representation" analysis in the Ninth Circuit. *See Irwin v. Mascott*, 370 F.3d 924 (9th Cir. 2004) (factors include close relationship between party and non-party, substantial participation or control by non-party, tactical maneuvering, identity of relevant interests, and adequate representation). In any event, the Ninth Circuit has made clear that "the pertinent 'virtual representation' privity factors, outlined in *Irwin*, require factual development beyond the bare record." *Headwaters*, 399 F.3d at 1055; *id.* at 1054 ("the requisites for finding nontraditional forms of privity, outlined in *Irwin*, are not readily determined from the pleadings.").

CONCLUSION

Defendants' motion to dismiss should be denied.

Respectfully submitted,

/s/

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[7] Counsel acknowledge the valuable assistance of David Becker, a third-year student at George Washington University Law School, and Miriam Achtenberg, a second-year student at Harvard Law School, in the preparation of this brief.