IN THE SUPREME COURT OF THE STATE OF WASHINGTON

CERTIFICATION FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT
IN
CHAD MINNICK, LINDA STEPHENSON, DONALD SCHULTZ, STEPHEN REIMERS, COREY JELINSKI, VICTORIA BARTLEY, CHRISTOPHER CUHEL, KAREN GREFSRUD, RITA MCVICKER, JOSH KELLER, GLENN REYNOLDS, and EVA GIROD, on behalf of themselves and all those similarly situated,

Plaintiffs-Appellants,

v.

CLEARWIRE US LLC, and DOES 1 through 10,

Defendants-Appellees.

No. 85810-1

En Banc

Filed May 3, 2012

OWENS, J. -- The United States Court of Appeals for the Ninth Circuit certified the following question:

> Does Washington law treat the [early termination fee] at issue in this case as an alternative performance provision, or as a liquidated damages clause?

Minnick v. Clearwire US LLC, 636 F.3d 534, 538 (9th Cir. 2011) (hereinafter Order). This question is important because a liquidated damages provision is subject to a penalty analysis that an alternative performance provision avoids. The early termination fee (ETF) is a provision in a fixed-term telecommunications contract that charges customers a fee for terminating their contracts prematurely. Because the ETF, at the time of contracting, provided customers with a "real option" and was of relatively equal value with the alternative option of fulfilling the contract, we hold that it is an alternative performance provision and not a liquidated damages clause.

facts and procedural history

Clearwire provided wireless Internet and telephone services to the 12 subscribers (Appellants) who brought this case. Clearwire allows its users to access the Internet at broadband speeds from anywhere in the Clearwire coverage area simply by plugging in a wireless modem.

When signing up for this service, Clearwire's customers can choose between a month-to-month contract with no obligations beyond the monthly subscription charge and a fixed-term contract that has a discounted monthly subscription charge. Appellants all chose the fixed-term contract, for either one or two years. Those contracts allowed Appellants to cancel their subscription early by paying an ETF. The amount of the ETF varied depending on when the customer signed up and on whether

the customer selected a one- or two-year contract. For customers who signed up before March 7, 2007, Clearwire charged a flat ETF of $180. For customers who signed up on or after March 7, 2007, Clearwire charged a diminishing ETF. The ETF started at $220 and was reduced by $5 for each month thereafter under a two-year contract or $10 for each month under a one-year contract. As for customers under the "'Clear'" brand (as opposed to the "'Clearwire'" brand), the ETF was $120 less $4 for each month thereafter. *Id.*

Consequently, depending on how much time is left on the contract, canceling early may cost more or less than the sum of the remaining monthly payments. Under the $120 ETF, the customer always saves more money by canceling early because the ETF is always less than the sum of the remaining monthly payments. For the $220 ETF that decreases by $5 a month, the ETF is greater than the remaining payments only in the last three months. The $180 flat ETF is greater than the remaining payments only during the last four months.

Appellants are all customers who either incurred this ETF for canceling early or were threatened with this ETF for attempting to cancel early. For example, Chad Minnick incurred the ETF after informing Clearwire that he was canceling his subscription early. Similarly, Donald Schultz initially tried to cancel his service but refrained upon learning he would be responsible for the ETF. Eventually, Schultz

canceled anyway and paid the ETF when he moved outside of Clearwire's coverage area. In any event, all Appellants were dissatisfied with Clearwire's service, alleging that instead of the fast and reliable service promised, they received inconsistent and painstakingly slow speeds.

Minnick sued Clearwire in King County Superior Court in April 2009, claiming that Clearwire was committing false advertising and was imposing ETFs unlawfully. He then filed the first amended complaint in May, which added the other 11 plaintiffs through class certification. In July, Clearwire removed the case to the United States District Court for the Western District of Washington where it filed a motion to dismiss all of Appellants' claims. The district court granted Clearwire's motion.

Appellants then appealed to the United States Court of Appeals for the Ninth Circuit, arguing that the ETF was a liquidated damages provision and not an alternative performance provision as the trial court found. The Ninth Circuit believed the case involved an unsettled area of state law and certified the following question to this court: "Does Washington law treat the ETF at issue in this case as an alternative performance provision, or as a liquidated damages clause?" Order at 538.[1]

We accepted the certified question pursuant to the Federal Court Local Law Certificate Procedure Act, chapter 2.60 RCW, and RAP 16.16.

---

[1] It is worth noting that while Appellants spend a portion of their brief alleging fraudulent business practices by Clearwire that issue is not before this court.

Issue Presented

Is Clearwire's ETF an alternative performance provision or a liquidated damages provision subject to a penalty analysis?

Analysis

A. Standard of Review

"The decision whether to answer a certified question pursuant to chapter 2.60 RCW is within the discretion of the court." *Broad v. Mannesmann Anlagenbau, A.G.*, 141 Wn.2d 670, 676, 10 P.3d 371 (2000). This court treats the certified question as a pure question of law and reviews it de novo. *See, e.g.*, *Parents Involved in Cmty. Schs. v. Seattle Sch. Dist. No. 1*, 149 Wn.2d 660, 670, 72 P.3d 151 (2003).

B. The ETF Is an Alternative Performance Provision

To determine whether the ETF is an alternative performance provision or a liquidated damages provision, we first analyze the issue under Washington law. However, because Washington case law has not specifically addressed ETFs in this context, s*ee Chandler v. Doran Co.*, 44 Wn.2d 396, 267 P.2d 907 (1954); *Bellevue Sch. Dist. No. 405 v. Bentley*, 38 Wn. App. 152, 684 P.2d 793 (1984), we compare our analysis with that of other jurisdictions that have. Finally, we briefly address Appellants' argument that an alternative performance provision allows the promisee to recover only the option that results in the smallest recovery.

i. The ETF Is an Alternative Performance Provision under Washington Law

An alternative contract allows a promisor to render "'one of two or more alternative performances either one of which is mutually agreed upon as the bargained-for . . . exchange for the [other party's] return performance.'" *Chandler*, 44 Wn.2d at 401 (quoting 5 Arthur Linton Corbin, Corbin on Contracts § 1079, at 379 (1951)). By comparison, a liquidated damages provision is a sum of money agreed upon in advance that is a reasonable forecast of just compensation for the harm caused by breach. *Walter Implement, Inc. v. Focht*, 107 Wn.2d 553, 559, 730 P.2d 1340 (1987). If the liquidated damages provision is either not a reasonable forecast or if the harm is easy to ascertain, then the provision is an unlawful penalty. *Id.* Whether a contract provides for alternative performance or for liquidated damages is a question of factual interpretation that does not rely upon the form of words used by the parties. *Bentley*, 38 Wn. App. at 155. The distinguishing factor between the provisions is that the parties intended the options to give the promisor a real choice between reasonably equivalent choices. *Chandler*, 44 Wn.2d at 401.

This means that at the time fixed for performance either alternative might prove more desirable and that the parties did not intend the "device to assure the performance of the [other] option." *Id.* at 401, 403. Additional factors to consider are "whether the money payment is equivalent to performance of the option, and the

relative values of the performances." *Bentley*, 38 Wn. App. at 156. The value of the options is determined at the time of contracting and not at the time the option is exercised. *Id*. In other words, whether a contract provides for an alternative performance or for a liquidated damages provision depends on whether (a) the contract gives the promisor a "real option," and (b) there is a reasonable equivalence between the two choices.

Appellants reject this analytical framework, claiming that a true alternative performance contract would allow Appellants to choose between paying (1) the monthly payments and receiving Clearwire's services for the life of the fixed term or (2) the ETF and receiving Clearwire's services for the life of the fixed term. This is incorrect and is not supported by case law. So long as the ETF is a "'specified payment'" that either nullifies the contract or allows Appellants to "'regain the legal privilege of not'" performing, then an alternative contract can exist. *Chandler*, 44 Wn.2d at 402 (quoting 5 Corbin, *supra*, § 1213, at 883, 884); *Bentley*, 38 Wn. App. at 155-56 (same). Thus, despite Appellants' claims otherwise, the framework established in *Chandler* and *Bentley* applies here.

Under the Washington framework, the ETF at issue is an alternative performance provision and not a liquidated damages provision because the ETF provides a real option to Appellants and there is a reasonable equivalence between the

two choices.

Here, a "real option" exists because at the time of contracting, Appellants did not know whether they would want to honor the contract for the fixed term or cancel early. A real option exists if either option might prove more desirable and the promisor is free to choose either one. *Chandler*, 44 Wn.2d at 401; *Bentley*, 38 Wn. App. at 155. At issue in *Bentley* was a collective bargaining agreement between a teacher and her school. *Id*. at 154. Under the agreement, Bentley received paid sabbatical leave but had to repay the sabbatical funds if she chose not to return to work afterward. *Id*. The parties disputed whether this requirement was a liquidated damages provision or an alternative performance provision. *Id*. at 154-55. The court held a real option existed because the teacher did not, at the time of contracting, know whether she would need or desire to return to her position. *Id*. at 156. More importantly, the school could not compel Bentley to choose either option. *Id*. Thus, rather than coerce Bentley into returning to her job, the agreement gave her control over her future plans by not requiring her to return. *Id*. Similarly in *Chandler*, a real option existed because the defendant had the power to choose between the two choices. 44 Wn.2d at 403. The defendant corporation had agreed to either sell plaintiff property or to pay plaintiff additional salary. *Id*. at 398. The defendant argued that the option of an increased salary was merely a device to enforce the

property sale. *Id.* at 403. However, the court held that the agreement gave a real option because the defendant reserved for itself the ability to choose between paying the increased salary or selling the property depending on which one it preferred. *Id.*

Here, Appellants contracted with Clearwire to pay monthly fees for a fixed term in exchange for Clearwire's services at a discounted monthly price. Appellants had the option of canceling their contracts early if they paid the ETF. Similar to the teacher's position in *Bentley*, Appellants did not know whether they would want to continue the service in six months or in one year. As such, Appellants occupied a position similar to the defendant in *Chandler* and the teacher in *Bentley* who could choose between options. Appellants had a real option of exiting the contract early by paying the ETF if they so chose. Perhaps most importantly, Clearwire, like the school in *Bentley*, could not compel Appellants to choose either option.

Appellants counter that, unlike the school in *Bentley*, Clearwire can impose the ETF on the promisor in some situations. Clearwire, in fact, can force a customer to pay the ETF if the customer breaches the contract. However, Appellants' contention argues a scenario not before this court because Clearwire did not impose the ETF on any plaintiff for breach of contract. Rather, the only ETFs charged were for canceling the contract early, a contingency provided for in the contract allowing a customer to regain their freedom from performance. Thus, the question before us is not whether

the ETF is a liquidated damage if unilaterally imposed upon Appellants, but whether the ETF is a liquidated damage when charged for canceling the contract.

Another issue the Appellants raise is the apparent lack of negotiations between the parties. In *Chandler*, 44 Wn.2d at 403, the parties had conducted extensive negotiations while, here, Appellants signed a form contract on line. Regardless, Appellants had an initial option between a month-to-month contract and a fixed-term contract. Further, negotiations are not always significant to the analysis as illustrated by *Bentley*, which did not consider them. 38 Wn. App. at 154-56. Thus, even though extensive negotiations did not occur, Appellants still chose the fixed-term contract with the ETF over an alternative month-to-month contract. The lack of negotiations does not detract from the real option that existed between the two options.

Moreover, it is conceivable that even if these contracts were negotiated one at a time, customers would still negotiate for an ETF. A customer signing up for a year-long (or two-year-long) commitment might be hesitant without having an escape from performance. The ETF provides that escape. It allows customers to enjoy a discounted monthly premium• due to signing up for a long-term plan• while retaining some of the flexibility that existed with the month-to-month plan.

Next, this court must determine if there exists a reasonable equivalence between the two options: paying the ETF or continuing the contract. The court must look to the

relative value of the options at the time of contracting to determine if a reasonable equivalence exists. *Id*. at 155-56; *Chandler*, 44 Wn.2d at 403-04; Restatement (Second) of Contracts § 356 cmt. c (1981) ("In determining whether a contract is one for alternative performances, the relative value of the alternatives may be decisive."). If the values are "so disproportionate as to be unequal" then one option is a penalty and not an alternative performance. *Chandler*, 44 Wn.2d at 404. Both *Bentley* and *Chandler* analyze the relative value of options using a fairly deferential lens. In *Bentley*, the court held that a reasonable equivalence existed between the teacher returning to work or returning the sabbatical pay instead. 38 Wn. App. at 156. Bentley claimed the values were unequal because no reasonable person would choose unemployment. *Id*. However, at the time of contracting, a teacher may want to retain control over her future plans and not return to work. *Id*. Similarly, in *Chandler*, the court was unwilling to declare the option between the property and additional salary unequal because there was no vast disproportionality between them. 44 Wn.2d at 404. In other words, because there was a lack of obvious inequality between the two options, the relative values of the two options supported finding an alternative performance provision. *See id*. at 403-04.

We must determine the relative value of the ETF's three different values compared to the value of fulfilling the contract. Following the reasoning of *Bentley*,

where the court looked to the relative value between the options at the time of contracting, the options here are relatively equal. As stated above, the value of the ETF compared to the sum of the remaining monthly payments generally depended upon the time left under the contract. Under the two-year contract, most disfavorable to the customer, the ETF is greater than the remaining payments only during the last four months.

The ETF benefited Appellants by allowing them to retain control over their future decision making while enjoying Clearwire's services at a discount, much like the teacher's option to not return to work gave her flexibility. As for the few months where the ETF is greater than the remaining payments, the court's reasoning in *Chandler*• that so long as obvious inequality does not exist the relative values are equal• is instructive. The ETF is significantly less than the remaining payments for the majority of the life of the contract. Put differently, a customer at the time of contracting could see value in canceling early and paying the ETF rather than paying the remaining monthly payments.

Even when the ETF is greater, it is not so vastly unequal to the remaining payments as to render it a liquidated damages provision. Under the most disadvantageous circumstances, a customer would have to pay a $180 ETF even though a single monthly payment of either $36.99 or $29.99 remained. Br. of

Def./Appellee Clearwire US, LLC, App. A. This disparity between the ETF and the remaining payment may seem great, but taken in context of the entire two-year contract, the disparity lessens. Specifically, for the first 20 months of that contract the $180 ETF is less than the remaining payments. *Id*. In sum, the relative equivalence between the two options is such that a customer, at the time of contracting, could foresee utilizing the ETF to escape his or her obligation of monthly payments. Therefore, the ETF is an alternative performance provision and not a liquidated damages provision.

ii. Holding That the ETF is an Alternative Performance Provision Is Supported by Other Jurisdictions

The ETF is an alternative performance provision because it provides a real option to Appellants and is of relatively equal value to the alternative option of fulfilling the contract. This result is consistent with two other federal cases from California, which have specifically addressed whether ETFs are liquidated damage provisions or alternative performance provisions. On the other hand, this result is contrary to a few cases, including a California Court of Appeals case, which was decided after the two federal cases. We address the cases that favor ETFs as alternative performance provisions first.

The two federal cases from California support our holding that the ETF is an alternative performance provision because the cases involve similar facts and reasoning. The most closely related case is *Hutchison v. AT&T Internet Services, Inc.*, No. CV07-3674 SVW (JCX), 2009 WL 1726344 (C.D. Cal. May 5, 2009) (unpublished), *aff'd sub nom. Hutchison v. Yahoo! Inc.*, 396 F. App'x 331, 2010 WL 3706571 (9th Cir. Sept. 20, 2010) (unpublished), because it also involved an ETF that eventually became more expensive than fulfilling the contract. The ETF there was less than the remaining payments for the first seven months at which point fulfilling the contract was cheaper than paying the ETF. *Hutchinson*, 2009 WL 1726344, at *6.

Because the court examined whether the ETF was a rational choice at the time of contracting, the fact that the ETF was more expensive after seven months was irrelevant. *Id.* The other federal court case from California reached a similar result. *Schneider v. Verizon Internet Servs., Inc.*, 400 F. App'x 136, 2010 WL 3825502 (9th Cir. Sept. 27, 2010) (unpublished) (holding the ETF was an alternative performance provision under similar reasoning).

In contrast, other cases cited by Appellants reach a different result. Appellants mainly rely upon a California State Court of Appeals case, *In re Cellphone Termination Fee Cases*, 193 Cal. App. 4th 298, 122 Cal. Rptr. 3d 726, *cert. denied*, 132 S. Ct. 555 (2011), and a federal district court case from Illinois, *Mau v. L.A. Fitness Int'l, LLC*, 749 F. Supp. 2d 845 (N.D. Ill. 2010). Appellants incorrectly claim both *Hutchison* and *Schneider* are no longer good law because they were decided before *Cellphone Termination Fee Cases*, which held an ETF was a liquidated damages provision and not an alternative performance provision. 193 Cal. App. 4th at 329. Appellants mischaracterize that court's holding and wish to expand it so that all ETFs are liquidated damages. That court did not declare *Hutchison* bad law or that all ETFs are liquidated damages. *Id.* ("While [*Hutchison*] is not binding on this court . . ., it is self-evident that in contrast we deal here with contrary factual findings made after trial on a full evidentiary record.").

Instead, the court held that the ETF at issue was a liquidated damages provision on facts distinguishable from this case. Primarily, the defendant, Sprint, involuntarily imposed an ETF on some customers thereby depriving them of a rational choice between options. *Id*. at 328. The court found that of the customers charged an ETF, 80 percent were terminated by Sprint before being charged. *Id*. In comparison, Clearwire never declared a contract in breach before imposing the ETF. This is an important factual distinction because it demonstrates that Clearwire was not treating the ETF like a liquidated damages provision, which is only imposed upon breach. *See, e.g.*, *Walter Implement*, 107 Wn.2d at 559 ("[T]he [sum of money] must be a reasonable forecast of just compensation for the harm that is caused by the breach.").

The second case, *Mau*, is also unpersuasive because it adopts a test that excludes a whole category of alternative performance provisions: those that provide for payment to "'regain the legal privilege of not rendering the promised performance.'" *Chandler*, 44 Wn.2d at 402 (quoting 5 Corbin, *supra*, § 1213, at 883, 884). *Mau* ignores this type of provision and applies the penalty analysis to any provision that terminates the contract. 749 F. Supp. 2d at 847-48. In *Mau*, a plaintiff wished to cancel his gym membership but would have had to pay 50 percent of the remaining balance on his contract if he voluntarily terminated the contract. *Id*. at 847. The court applied a penalty analysis because the provision terminated the contractual

relationship. *Id*. at 848 ("[T]here was and is no expectation of a continuing relationship between [the parties] . . . . [The plaintiff] simply wanted to end his contract."). However, *Mau*'s reasoning is not persuasive because it did not apply an alternative performance analysis ("real option" and "reasonably related options") to reach its holding, and its proposed rule would exclude an entire class of potential alternative performance provisions.

Because *Cellphone Termination Fee Cases* relies on distinguishable facts and *Mau* applies a different legal standard, neither is persuasive. Accordingly, neither case impacts our conclusion that the ETF provision is an alternative performance provision and not a liquidated damages provision. This is not to say that if faced with similar facts as those in *Cellphone Termination Fee Cases* we might not hold otherwise.

iii. Clearwire May Still Charge Customers the ETF even if It Is More Expensive than the Remaining Monthly Payments

Finally, Appellants argue that even if the ETF is a form of alternative performance, Clearwire is unable to enforce it. The crux of their argument is that the promisee of an alternative performance contract may recover only "damages flowing from the alternative 'resulting in the smallest recovery.' Restatement (First) of Contracts § 344." Opening Br. of Appellant at 34. This is incorrect.

As the United States Court of Appeals for the Second Circuit stated, "Even if this is currently the rule• and its absence from the Second Restatement of Contracts

suggests that it is not• it does not appear to apply in a case such as this one." *Schwan-Stabilo Cosmetics GmbH & Co. v. Pacificlink Int'l Corp.*, 401 F.3d 28, 34 (2d Cir. 2005). In an alternative contract where one of the alternatives is a sum of money, the promisee is entitled to the sum of money even though the other alternative may be less onerous to the promisor. *Id*. (quoting 25 Richard A. Lord, Williston on Contracts § 66:106, at 120-21 (4th ed. 2002)). Therefore, Clearwire can charge the ETF even though it might be more expensive than the amount remaining under the contract.[2]

Conclusion

Under Washington law, an alternative performance provision is distinguishable from a liquidated damages provision because it provides a "real option" to the promisor and the alternatives are reasonably equal to each other. Here, the ETF provided a "real option" at the time of contracting because Appellants wanted to retain the control and flexibility that the early cancellation allowed them. Further, the ETF was less expensive than the remaining payments for the majority of the contract's life, thereby indicating the options were reasonably related. The ETF also allowed Appellants to benefit from reduced monthly premiums under the fixed-term contract but also enjoy some of the flexibility of the month-to-month subscription. Therefore, the ETF is an alternative performance provision that is not subject to a penalty

[2] Appellants request that we apply a penalty analysis even if the ETF is an alternative performance provision. We decline.

analysis.

AUTHOR:

Justice Susan Owens

WE CONCUR:

Chief Justice Barbara A. Madsen

Justice James M. Johnson

Gerry L. Alexander, Justice Pro Tem.

Justice Mary E. Fairhurst