

# Client Alert

A report  
for clients  
and friends  
of the firm July 2006

## California Supreme Court Rules That All Parties Must Consent Before Out-of-State Companies Doing Business in California Record Telephone Conversations

The California Supreme Court has put *all* out-of-state companies doing business in California on notice that they must take heed of California's stringent privacy laws. A recent ruling makes out-of-state companies subject to California law requiring two-party consent for the recording of telephone conversations made to or received from California. *Kearney v. Salomon Smith Barney, Inc.*, No. S124739, 2006 Cal. LEXIS 8362 (Cal. Sup. Ct. July 13, 2006).

### The Facts

Kelly Kearney and Mark Levy were California residents employed in California by WorldCom. WorldCom granted their employees, including Kearney and Levy, stock options that could be exercised only through the Atlanta, Georgia offices of Salomon Smith Barney, Inc. ("SSB"). Kearney and Levy therefore opened accounts with SSB's Atlanta office. During their relationship with SSB, Kearney and Levy had numerous telephone conversations with SSB executives located in Atlanta.

Unbeknownst to Kearney and Levy at the time, SSB had recorded many of those conversations. When Kearney and Levy later filed an unrelated suit against SSB, the pair discovered that their phone conversations had been recorded. They then filed suit on behalf of themselves and similarly situated SSB clients residing in California, seeking an injunction prohibiting SSB from recording future California residents' phone calls, monetary damages, and restitution.

### The Law

Section 637.2 of the California Penal Code provides a statutory private right of action authorizing any person who has been injured by a violation of California's invasion of privacy legislation to bring a civil action for damages and injunctive relief. Section 632 prohibits a party to a telephone conversation from secretly or surreptitiously recording the conversation, but does not address the question of whether the statute was intended to apply when one party is in California and the other is outside the State. Eleven other states require two-party consent.<sup>1</sup> Georgia law, like the laws of thirty-six other states,<sup>2</sup> allows for recording such communications with only one party's consent.

### Choice of Law Issue

SSB filed a demurrer to the complaint, which the Superior Court sustained on the grounds that the conduct was permissible under Georgia law; on appeal, the Court of Appeal affirmed. The California Supreme Court granted review to consider the novel choice-of-law issue. After rejecting SSB's arguments regarding personal jurisdiction, preemption, and the constitutionality of applying California's laws, the

<sup>1</sup> Connecticut, Florida, Illinois, Maryland, Massachusetts, Michigan, Montana, Nevada (by court decision, *State v. Reyes*, 808 P.2d 544 (Nev. 1991)), New Hampshire, Pennsylvania, and Washington.

<sup>2</sup> Alabama, Alaska, Arizona, Arkansas, Colorado, Delaware, District of Columbia, Hawaii, Idaho, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Virginia, West Virginia, Wisconsin, and Wyoming.

Court addressed the choice of law issue, applying the governmental interest analysis adopted in California.<sup>3</sup>

The Court concluded that a true conflict exists between California and Georgia law and that, “as a general matter, the failure to apply California law in this context would impair California’s interest in protecting the degree of privacy afforded to California residents by California law more severely than the application of California law would impair any interest of the State of Georgia.” The Court concluded there was no question that the principal purpose of section 632 is to protect the privacy of confidential communications of California residents while they are in California, and therefore must apply even where one party is outside the State. Further, “in light of the substantial number of businesses operating in California that maintain out-of-state offices or telephone operators, a resolution of this conflict permitting all such businesses to regularly and routinely record telephone conversations made to or from California clients or consumers without the clients’ or consumers’ knowledge or consent would significantly impair the privacy policy guaranteed by California law, and potentially would place local California businesses (that would continue to be subject to California’s protective privacy law) at an unfair competitive disadvantage vis-à-vis their out-of-state counterparts.”

Conversely, the Court found that application of California law to Georgia would not have a significant detrimental impact because it would not adversely affect any privacy interest, would affect only business telephone calls that are made to or received from California clients, and would not prevent a practice of recording all such calls, but merely require that the business inform the clients or customers of the company’s policy at the outset of the conversation.

However, in finding that SSB reasonably relied on Georgia law and that Georgia had a significant interest in protecting its citizens from monetary liability for adhering to their own law, the Court held that Georgia’s interest would be more severely impaired were monetary liability for past conduct to be imposed. Therefore, while finding that plaintiffs were entitled to pursue their claims for injunctive relief, the Court rejected plaintiffs’ claims for damages for SSB’s past violations of California law.

## **Kearney’s Implications**

The implications of *Kearney* for any and all out-of-state companies doing business in California are immediate and significant. The Court placed tremendous significance on California’s interest in protecting the privacy of its citizens and explicitly stated that “out-of-state companies that do business in California now are on notice that, with regard to future conduct, they are subject to California law with regard to the recording of telephone conversations made to or received from California, and that the full range of civil sanctions afforded by California law may be imposed for future violations.” Out-of-state companies doing business in California should familiarize themselves and comply with all of California’s privacy statutes, which generally provide much more stringent protection for consumers than other state laws.

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<sup>3</sup> The governmental interest analysis involves three steps. The court must first determine whether the relevant law of each of the potentially affected jurisdictions with regard to the particular issue in question is the same or different. If there is a true conflict, i.e., each jurisdiction has an interest in the application of its own law under the circumstances of the particular case, the court must evaluate and compare the nature and strength of the interest of each jurisdiction in the application of its own law “to determine which state’s interest would be more impaired if its policy were subordinated to the policy of the other state.” The court ultimately applies “the law of the state whose interest would be the more impaired if its law were not applied.”

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