Background on Class Action Waivers in Arbitration

Lise Gelernter, NAA Member
Lise.Gelernter@gmail.com
University at Buffalo Law School
O'Brian Hall
Amherst, New York 14260
716-645-5540

Much of the case law concerning class actions in arbitration has necessarily arisen within the context of individual employment contracts, or non-employment contracts, primarily between consumers and businesses. Because the Federal Arbitration Act (FAA) applies to these agreements, 9 U.S.C. §§2 *et seq.* (2017), the law and doctrine of the FAA has governed courts' decisions. Section 301 of the Labor Management Relations Act (LMRA), 29 U.S.C. §185 (2017), applies specifically to collective bargaining agreements between unions and private sector employers and has its own arbitration jurisprudence. Nonetheless, because the Supreme Court as well as the lower federal courts and many state courts appear to consider arbitration doctrine developed under the FAA to be interwoven with arbitration doctrine developed under the LMRA, both FAA and LMRA precedents have informed the courts' understanding of how and whether to enforce arbitration agreements that permit or waive class actions. The following discussion examines the recent history and trends in the FAA case law, which can have an effect on LMRA cases.

I. Contractual Silence or Ambiguity Regarding Class Actions in Arbitration

A. FAA – No class actions where no agreement on issue was reached – *Stolt-Nielsen S. A.* v. *AnimalFeeds Int'l Corp.*

In *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662, 671, 130 S. Ct. 1758 (2010), the Supreme Court held that arbitrators interpreting an arbitration agreement governed by the FAA cannot infer that class actions are permissible if the arbitration agreement is silent on the issue and the parties stipulated that they never made any agreement on class arbitration.

B. However, arbitrators interpreting a vague contract can still find that it permits class actions – *Oxford Health Plans v. Sutter*.

In *Oxford Health Plans v. Sutter*, the Supreme Court refused to vacate an arbitrator's interpretation of a contract to arbitrate that permitted class actions even though the contract was not explicit about it. 133 S. Ct. 2064, 2068-2069 (2013). The contract provided:

> No civil action concerning any dispute arising under this Agreement shall be instituted before any court, and all such disputes shall be submitted to final and binding arbitration in New Jersey, pursuant to the rules of the American Arbitration Association with one arbitrator.

133 S. Ct at 2067. The Supreme Court described the arbitrator's decision-making process as follows:

> Noting that the question turned on "construction of the parties' agreement," the arbitrator focused on the text of the arbitration clause quoted above. He reasoned that the clause

> sent to arbitration "the same universal class of disputes" that it barred the parties from bringing "as civil actions" in court: The "intent of the clause" was "to vest in the arbitration process everything that is prohibited from the court process." And a class action, the arbitrator continued, "is plainly one of the possible forms of civil action that could be brought in a court" absent the agreement. Accordingly, he concluded that "on its face, the arbitration clause ... expresses the parties' intent that class arbitration can be maintained."

Id. (internal citations omitted).

The Court invoked the LMRA cases limiting judicial review of arbitration awards in delineating the narrow reach of its review power. The majority upheld the arbitrator's interpretation of the contract and distinguished the case from *Stolt-Nielsen*.

> Because the parties "bargained for the arbitrator's construction of their agreement," an arbitral decision "even arguably construing or applying the contract" must stand, regardless of a court's view of its (de)merits.
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> Oxford misreads *Stolt–Nielsen* : We overturned the arbitral decision there because it lacked any contractual basis for ordering class procedures, not because it lacked, in Oxford's terminology, a "sufficient" one. The parties in *Stolt–Nielsen* had entered into an unusual stipulation that they had never reached an agreement on class arbitration. See 559 U.S., at 668–669, 673, 130 S.Ct. 1758. In that circumstance, we noted, the panel's decision was not—indeed, could not have been—"based on a determination regarding the parties' intent." Id., at 673, n. 4, 130 S.Ct. 1758; *see id*., at 676, 130 S.Ct. 1758 ("Th[e] stipulation left no room for an inquiry regarding the parties' intent"). Nor, we continued, did the panel attempt to ascertain whether federal or state law established a "default rule" to take effect absent an agreement. *Id*., at 673, 130 S.Ct. 1758. Instead, "the panel simply imposed its own conception of sound policy" when it ordered class proceedings. *Id*., at 675, 130 S.Ct. 1758. But "the task of an arbitrator," we stated, "is to interpret and enforce a contract, not to make public policy." *Id*., at 672, 130 S.Ct. 1758. In "impos[ing] its own policy choice," the panel "thus exceeded its powers." *Id*., at 677, 130 S.Ct. 1758.

133 S. Ct at 2068-2069. *See NCR Corporation v. Goh*, Civ. No. C16-127 (W.D. Wash. 5/30/17) (https://scholar.google.com/scholar_case?case=2564011903774253828&hl=en&lr=lang_en&as_sdt=20003&as_vis=1&oi=scholaralrt) (court applies *Oxford Health* and upholds an arbitrator's award interpreting a contract to allow class action arbitration, even though the arbitration agreement did not explicitly mention class actions).

II. FAA preemption of state law bans on class action waivers in arbitration

A. *AT&T Mobility v. Concepción*. In *AT&T Mobility v. Concepción*, __ U.S. __, 131 S. Ct. 1740 (2011), the Supreme Court held that the FAA preempted California legal doctrine that barred consumer contracts from prohibiting class action arbitrations. Vincent and Lisa

Concepción bought cellular service and were supposed to receive a "free" phone from Cingular (later bought by AT&T Mobility). When they were billed $30.22 in sales tax, they first tried to commence a class action in federal district court alleging false advertising and fraud, among other claims, but AT&T moved to compel arbitration under the consumer contract the Concepcións had signed that required that all disputes with Cingular/AT&T be arbitrated. 131 S. Ct at 1744-45. The agreement required all arbitration claims to "be brought in the parties' 'individual capacity, and not as a plaintiff or class member in any purported class or representative proceeding,'" and also prohibited an arbitrator from consolidating " 'more than one person's claims, and . . . [presiding] over any form of a representative or class proceeding.' " *Id.* at 1744) (quoting the agreement).

The Concepcións opposed the motion to compel arbitration by claiming that under California legal doctrine announced in *Discover Bank v. Superior Court*, 36 Cal. 4th 148 (2005), the arbitration agreement was unconscionable because it banned class actions. The District Court for the Southern District of California and the Ninth Circuit Court of Appeals found that the arbitration agreement was unconscionable under the "*Discover Bank* rule" and therefore held it to be invalid, as permitted by FAA § 2, but the Supreme Court overturned that judgment in a 5-4 decision.

The Supreme Court majority found that although the *Discover Bank* rule appeared to apply to any type of contract, it had a heightened, and therefore impermissible, impact on arbitration agreements. The Court stated that "our cases place it beyond dispute that the FAA was designed to promote arbitration," and that "California's *Discover Bank* rule . . . interferes with arbitration." *Id*. at 1749, 1750. The Court found that this special interference was due to the fact that " 'changes brought about by the shift from bilateral arbitration to class-action arbitration' are 'fundamental.' " *Id*. at 1750, *quoting Stolt-Nielsen S. A.* v. *AnimalFeeds Int'l Corp.*, 559 U.S. ___, 130 S. Ct. 1758, 1776 (2010). The Court described the "fundamental changes" as follows:

> Classwide arbitration includes absent parties, necessitating additional and different procedures and involving higher stakes. Confidentiality becomes more difficult. And while it is theoretically possible to select an arbitrator with some expertise relevant to the class-certification question, arbitrators are not generally knowledgeable in the often-dominant procedural aspects of certification, such as the protection of absent parties. The conclusion follows that class arbitration, to the extent it is manufactured by *Discover Bank* rather than consensual, is inconsistent with the FAA.

AT&T, 131 S. Ct. at 1750-51.

The Court went on to list three major inconsistencies. First, the majority found that switching from "bilateral" to class arbitration would result in a much more formal, slower, and expensive process. Second, the Court stated that, unlike bilateral arbitration, class arbitration required much more procedural formality due to the need to keep absent class members protected and bound by any arbitration award. Third, class arbitration is much more risky for defendants than bilateral arbitration. The risks the Court listed included an "absence of multilayered

review" that would result in more uncorrected errors on a classwide, rather than an individual scale. The potential for a huge, potentially unfair monetary loss would unfairly pressure defendants to settle "questionable claims," the majority reasoned. *Id*. at 1751-52.

Finally, the Court brushed away the dissent's concerns about the impossibility of small claims being pursued without the benefit of a class action process.

> The dissent claims that class proceedings are necessary to prosecute small-dollar claims that might otherwise slip through the legal system. . . . But States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons. Moreover, the claim here was most unlikely to go unresolved. As noted earlier, the arbitration agreement provides that AT&T will pay claimants a minimum of $7,500 and twice their attorney's fees if they obtain an arbitration award greater than AT&T's last settlement offer. The District Court found this scheme sufficient to provide incentive for the individual prosecution of meritorious claims that are not immediately settled, and the Ninth Circuit admitted that aggrieved customers who filed claims would be "essentially guarantee[d]" to be made whole, 584 F.3d, at 856, n. 9. Indeed, the District Court concluded that the Concepcións were *better off* under their arbitration agreement with AT&T than they would have been as participants in a class action, which "could take months, if not years, and which may merely yield an opportunity to submit a claim for recovery of a small percentage of a few dollars." *Laster*, 2008 U.S. Dist. LEXIS 103712, [WL] at *12.
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> Because it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Hines* v. *Davidowitz*, 312 U.S. 52, 67, 61 S. Ct. 399, 85 L. Ed. 581 (1941), California's *Discover Bank* rule is preempted by the FAA.

Id. at 1753.

B. Impossibility of pursuing a statutory claim does not bar waiver of class action arbitration – *American Express v. Italian Colors Restaurant.*

In *American Express v. Italian Colors Restaurant, et al.* __ U.S. __, 133 S. Ct. 2304 (2013), a class of merchants sought to bring a class action in court against American Express. They claimed that American Express was violating federal antitrust laws by using "its monopoly power in the market for charge cards to force merchants to accept credit cards at rates approximately 30% higher than the fees for competing credit cards." *Id*. at 2308. However, the contract they had signed with American Express required the arbitration of all disputes and stated that "[t]here shall be no right or authority for any Claims to be arbitrated on a class action basis." *Id*. American Express argued that the merchants should be required to arbitrate their claims individually. The merchants argued that it would cost more to pursue an individual claim than an individual merchant could ever recover and therefore the waiver of class actions "bars effective vindication [of their rights] . . . because they have no economic incentive to pursue their antitrust claims individually in arbitration." *Id*. at 2309.

The majority (5-3) (Justice Sotomayor took no part in the decision) rejected the merchants' claims and noted that Section 2 of the FAA "reflects the overarching principle that arbitration is a matter of contract," and that the antitrust laws did not preclude waiver of a class action. *Id*. at 2309. The Court rejected the "effective vindication" argument, reasoning, "the fact that it is not worth the expense involved in *proving* a statutory remedy does not constitute the elimination of the *right to pursue* that remedy. . . .The class-action waiver merely limits arbitration to the two contracting parties. It no more eliminates those parties' right to pursue their statutory remedy than did federal law before its adoption of the class action for legal relief in 1938." 131 S.Ct. at 2311. In other words, the availability of a class remedy was not considered essential to the vindication of the plaintiff's rights, even if the absence of such a remedy would render the claim impractical.

Justice Kagan's dissent, in which Justices Breyer and Ginsberg joined, lamented the results flowing from the majority's decision:

> Here is the nutshell version of this case, unfortunately obscured in the Court's decision. The owner of a small restaurant (Italian Colors) thinks that American Express (Amex) has used its monopoly power to force merchants to accept a form contract violating the antitrust laws. The restaurateur wants to challenge the allegedly unlawful provision (imposing a tying arrangement), but the same contract's arbitration clause prevents him from doing so. That term imposes a variety of procedural bars that would make pursuit of the antitrust claim a fool's errand. So if the arbitration clause is enforceable, Amex has insulated itself from antitrust liability—even if it has in fact violated the law. The monopolist gets to use its monopoly power to insist on a contract effectively depriving its victims of all legal recourse.
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> And here is the nutshell version of today's opinion, admirably flaunted rather than camouflaged: Too darn bad.

Id. at 2313. Justice Kagan explained the practical and legal results flowing from the majority decision. Even though all parties agreed that the antitrust laws gave Italian Colors a cause of action, the restaurant would not be able to prove that Amex acted illegally without a complex "economic analysis" by an expert that would cost up to $1 million. The cost of the necessary analysis could amount to ten times or more of the value of Italian Colors' maximum recovery of $39,549. Therefore, it would be irrational to pursue the individual claim without the possibility of multiple recoveries for a class of business owners. This would deprive Italian Colors of "any effective opportunity" to challenge Amex's allegedly monopolistic practices. *Id.* at 2313-2320.

C. But complete waiver of statutory protection through an arbitration agreement is not enforceable, per the Fourth Circuit. A 2016 Fourth Circuit consumer arbitration decision has an interesting discussion on arbitration agreement enforceability that has implications for the employment and labor arbitration arenas. *Hayes v. Delbert Services*, 811 F.3d 666 (4th Cir. 2016). The case involved Delbert, a payday lender's servicing agent, and a loan agreement with an arbitration clause that stated:

> This Loan Agreement is subject solely to the exclusive laws and jurisdiction of the Cheyenne River Sioux Tribe, Cheyenne River Indian Reservation. By executing this Loan Agreement, you, the borrower, hereby acknowledge and consent to be bound to the terms of this Loan Agreement, consent to the sole subject matter and personal jurisdiction of the Cheyenne River Sioux Tribal Court, and that no other state or federal law or regulation shall apply to this Loan Agreement, its enforcement or interpretation.

811 F.3d at 669 (emphasis in the original). The loan agreement also stated: "Neither this Agreement nor Lender is subject to the laws of any state of the United States of America." *Id.* at 669-670.

The loan agreement's arbitration agreement required the arbitration of any disputes related to the loan or its servicing and stated that the arbitration proceedings shall be "conducted by the Cheyenne River Sioux Tribal Nation by an authorized representative in accordance with its consumer dispute rules and the terms of this Agreement." The version of the agreement at issue in the case also provided that a party "shall have the right to select" the AAA or JAMS, or another group to "administer the arbitration." The arbitration clauses also provided that the agreement

> IS MADE PURSUANT TO A TRANSACTION INVOLVING THE INDIAN COMMERCE CLAUSE OF THE CONSTITUTION OF THE UNITED STATES OF AMERICA, AND SHALL BE GOVERNED BY THE LAW OF THE CHEYENNE RIVER SIOUX TRIBE. The arbitrator will apply the laws of the Cheyenne River Sioux Tribal Nation and the terms of this Agreement.

Id. at 670. The agreement also prohibited the arbitrator from applying "any law other than the law of the Cheyenne River Sioux Tribe of Indians to this Agreement." *Id.*

After finding that Delbert was not a tribal entity, the Fourth Circuit ruled that the arbitration agreement was unenforceable because it "fails for the fundamental reason that it purports to renounce wholesale the application of any federal law to the plaintiffs' federal claims." The court recognized that the Supreme Court has found choice of law provisions and waivers of certain rights, such as class actions, to be enforceable, but distinguished the *Delbert* case because it violated the Supreme Court's ruling that arbitration waivers that blocked "a party's right to pursue statutory remedies" were not enforceable. The court stated: "a party may not underhandedly convert a choice of law clause into a choice of no law clause -- it may not flatly and categorically renounce the authority of the federal statutes to which it is and must remain subject."

This appears to be a pretty extreme case of a waiver. In the employment and labor arena, the Fourth Circuit's reasoning might have some play if there is an arbitration clause that appears to effectively waive all the rights of a party under an otherwise applicable law, such as Title VII or the Fair Labor Standards Act. But the Fourth Circuit made it clear that it considers the Supreme Court's decisions in *AT&T v. Concepcion* and *Italian Colors* to limit that inquiry by embracing the enforceability only of waivers of certain procedural or attendant rights, such as class actions, that merely make it more difficult or costly to pursue a federal remedy.

III. Circuit split on whether the NLRB was correct in holding that the NLRA prohibits bans on class actions in employment arbitration agreements.

A. Fifth Circuit – reverses NLRB in *D.R. Horton*; followed by Eighth and Second Circuits. In a case that the Fifth Circuit Court of Appeals reversed in part, the National Labor Relations Board (NLRB) issued a decision on January 3, 2012 that prohibited employment arbitration agreements from banning class actions. The Board found that barring class actions interfered with the NLRA's protection of employees' Section 7 rights to "engage in concerted action for mutual aid or protection" *D.R. Horton, Inc. and Michael Cuda*, 357 NLRB No. 184, 12-CA-25764 at 1 (2012), *rev'd in part, aff'd in part D.R. Horton v. NLRB*, 737 F.3d 344 (5th Cir. 2013). Therefore, an employer's requirement for employees to "sign an agreement that precludes them from filing joint, class, or collective claims addressing their wages, hours or other working conditions . . . in any forum, arbitral or judicial," violated Section 8(a)(1) of the NLRA, 29 U.S.C. § 158(a)(1), which makes it an unfair labor practice for an employer to "interfere with, restrain, or coerce employees in the exercise of the rights guaranteed in section 7 [29 U.S.C. § 157]." *Id*.

In reviewing the NLRB's decision, the Fifth Circuit Court of Appeals held that the NLRA does not trump the FAA's protection of the arbitration agreement and rejected the Board's other arguments defending the invalidation of the agreement's exclusion of class actions.[1] *D.R. Horton v. NLRB*, 737 F.3d 344 (5th Cir. 2013). The Fifth Circuit found a similar class action waiver in an arbitration agreement did not violate the NLRA in *Murphy Oil v. NLRB*, 808 F.3d 1013, 1019-1020 (5th Cir. 2015*).* The Eighth and Second Circuits have also rejected the NLRB's position on class action waivers. *Cellular Sales of Missouri v. NLRB*, 824 F.3d 772 (8th Cir. 2016); *Patterson v. Raymours Furniture*, 659 Fed. Appx. 40, 43 (2d Cir. 2016) ; *Sutherland v. Ernst & Young LLP*, 726 F.3d 290, 295 n. 8 (2d Cir. 2013).

B. Seventh and Ninth Circuits uphold the NLRB's position. In *Lewis v. Epic Systems Corp.* 823 F.3d 1147 (7th Cir. 2016), the Seventh Circuit sided with the NLRB, setting up a circuit split. Soon after, the Ninth Circuit agreed with the Seventh Circuit in *Morris v. Ernst & Young LLP*, 834 F.3d 975, 983 (9th Cir. 2016). In the *Lewis v. Epic Systems* case, the Seventh Circuit noted that "both courts and the Board have held that filing a collective or class action suit constitutes 'concerted activit[y]' under Section 7." 823 F.3d at 1152. It rejected an argument that "concerted activity" could not include class actions because they did not exist, in their current form, when the NLRA was enacted. The Court said: "Congress was aware of class, representative, and collective legal proceedings when it enacted the NLRA. The plain language of Section 7 encompasses them, and there is no evidence that Congress intended them to be excluded." *Id*. at 1154.

[1] In *D.R. Horton,* however, the Fifth Circuit did find that the NLRB was correct in finding that the language of the agreement could be read to bar employees from protecting their collective rights under §7 of the NLRA, and upheld the Board's order insofar as it required D.R. Horton to revise the language. 737 F3e at 356-362, 363.

The Seventh Circuit found that "Epic's [arbitration] clause runs straight into the teeth of Section 7." *Id.* at 1156. Because it interfered with an employee right to engage in "concerted activity," it violated Section 8 of the NLRA, which prohibits employers from limiting or interfering with that right. The court held that there was no conflict between the NLRA and the FAA because the FAA explicitly states that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. If an arbitration clause is illegal because it violates the NLRA, it meets the FAA conditions for the "revocation of any contract," the court held. *Id.* at 1155-57. Further, the court stated, "finding the NLRA in conflict with the FAA would render the FAA's saving clause a nullity. . . Illegality is a standard contract defense contemplated by the FAA's saving clause. If the NLRA does not render an arbitration provision sufficiently illegal to trigger the saving clause, the saving clause does not mean what it says." *Id*. at 1158.

C. Circuit split to be decided by the Supreme Court.

The Supreme Court granted petitions for certiorari in *Lewis v. Epic Systems*, *Murphy Oil v. NLRB*, and the Ninth Circuit's *Ernst & Young* case. 137 S.Ct. 809 (2017). The three cases have been consolidated under *National Labor Relations Board v. Murphy Oil USA* (Docket No. 16-307), with briefing completed by July 27, 2017. The arguments were held on October 2, 2017 and the case could be decided at any time. In an unusual twist, the United States Solicitor General changed sides in the case on June 16, 2017 and filed a "friend of the court" brief supporting the employers. The Justice Department, which had filed a petition for review on behalf of the NLRB in 2016, gave the NLRB permission to represent itself in the Supreme Court. http://www.scotusblog.com/2017/06/murphy-oils-law-solicitor-generals-office-reverses-course-arbitration-cases-supports-employers/#more-257105 .

IV. Post-Concepción class action strategies.

A. Challenges under the FAA. Although *Concepción*, *Italian Colors,* and the Fifth Circuit's ruling in *D.R. Horton* limited the options for plaintiffs who want to bring class actions despite the existence of a class action waiver, challenges to the waivers have continued under Section 2 of the FAA, which provides:

> A written provision in any . . . contract . . . to settle by arbitration a controversy thereafter arising out of such contract or transaction . . . or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. §2 (2017) (emphasis added).

Where a plaintiff can show that he or she did not actually agree to the terms of a contract or that the contract was not binding on him or her due to non-party status under state contract law, a plaintiff can have success. *See e.g. James v. Global Tellink*, 852 F.3d 262, 267-268 (3rd Cir. 2017) (parties using a telephone service did not agree to an arbitration clause containing a class action waiver where the parties were advised by an "interactive telephone voice response

system" that the terms of service, which contained the arbitration agreement, appeared on the service company's website); *Meyer v. Kalanick*, 200 F.Supp.3d 408, 420 (S.D.N.Y. 2016) (Uber customer deemed not to have agreed to arbitration clause in an electronic contract because the plaintiff did not have "reasonably conspicuous notice" of the electronic agreement reached through an obscure on-line hyperlink); *Preferred Care, Inc. v. Howell*, 187 F.Supp.3d 796, 808-809 (E.D. Ky. 2016) (when a nursing home resident's guardian signed an agreement to arbitrate any of the resident's claims against the nursing home, he did not bind the resident's wrongful death beneficiaries who sued the nursing home in court after the death of the resident).

But it is much more difficult for a plaintiff to prove that an arbitration agreement is unconscionable enough to violate state law and is therefore voidable under the FAA §2. First, some arbitration clauses delegate the question of arbitrability, including enforceability, to the arbitrator, precluding a court from even deciding a question of unconscionability. For example, in one of the many cases involving Uber's arbitration clauses, the Ninth Circuit held that Uber's arbitration agreements with its drivers "clearly and unmistakably" delegated all questions of arbitrability to an arbitrator. *Mohammed v. Uber Technologies*, 836 F.3d 1102, 1110 (9th Cir. 2016).

Second, meeting the standards for proof of unconscionability can be very difficult, especially if a plaintiff arguably consented to arbitrate his or her claims and was not forced to enter into the contractual relationship. In addition, many arbitration clauses are carefully worded enough to avoid a finding of unconscionability. In the *Mohammed v. Uber* case, the Ninth Circuit ruled that the delegation clause was not unconscionable because drivers had the opportunity to opt out of arbitrating their claims. *Id*. at 1111-1112. The alleged difficulties involved in opting out did not make a difference to the court.

B. Alternative causes of action that are similar to class actions – California's PAGA actions. In California, the state's Private Attorney General Act (PAGA) allows individuals to bring representative actions on behalf of the state concerning violations of the state's Labor Code that harm the individual and his or her co-workers. The private attorney general may seek civil penalties that are paid, in large part, to the state. Ca. Lab.Code, § 2698 et seq (2017); *Iskanian v. CLS Transportation Los Angeles*, 59 Cal.4th 348, 360, 327 P.3d 129, 133 (2014). This constitutes an alternative to a class action that is not affected by a class action waiver, according to the state's Supreme Court and the federal Ninth Circuit Court of Appeals. As discussed below, the reasoning in the California and Ninth Circuit cases might be successfully applied to other types of representative actions.

In *Iskanian*, the plaintiff, Arashavir Iskanian, tried to bring a class action on behalf of himself and co-workers concerning the employer's alleged failure to provide the appropriate compensation for overtime and meal and rest periods. However, because the employee had signed a class action waiver in an arbitration agreement, the California Supreme Court held that "due to recent United States Supreme Court precedent," the FAA preempted any state law or decisions that would have found the waiver to be unconscionable. 59 Cal. 4th at 359. In addition, the majority agreed with the Fifth Circuit's holding in *D.R. Horton*, and rejected

Iskanian's argument that the waiver violated the NLRA. [2]

But the Court found that the FAA did not preempt the plaintiff from proceeding with a representative action under the California Labor Code's Private Attorneys General Act of 2004 (PAGA). Ca. Lab. Code §2698 et seq. The waiver specifically prohibited "representative actions," but the Court held that the waiver could not abrogate Iskanian's rights under PAGA. The Court explained that an employee's PAGA action "functions as a substitute for an action brought by the government itself." *Id.* at 381, *quoting Arias v. Superior Court,* 46 Cal.4th 969, 986, 209 P.3d 923 (2009) (internal quotations omitted). A PAGA suit seeks civil penalties for violations of the state's Labor Code, with 75% of any penalties awarded going to a state agency, and 25% going to the "aggrieved employees." *Id.* at 380; Ca. Lab. Code §2699(i). The Court concluded that "an employee's right to bring a PAGA action is unwaivable" because it violates the state's public policy, as embodied in two state laws: sections 1668 and 3513 of the California Civil Code.

Section 1668 prohibits the enforcement of contracts that exempt anyone from responsibility for: 1) a willful injury to a person or property; or 2) any violation of law. Ca. Civ. Code §1668 (2017); *Iskanian*, 59 Cal. 4th at 382-383. The Court explained that the "the Legislature's purpose in enacting the PAGA was to augment the limited enforcement capability of the Labor and Workforce Development Agency by empowering employees to enforce the Labor Code as representatives of the Agency." *Iskanian*, 59 Cal. 4th at 383. A class action waiver violates §1668 because it "serves to disable one of the primary mechanisms for enforcing the Labor Code. Because such an agreement has as its 'object, ... indirectly, to exempt [the employer] from responsibility for [its] own ... violation of law' it is against public policy and may not be enforced." *Id.* at 382.

Section 3513 of the Civil Code provides that "a law established for a public reason cannot be contravened by a private agreement." Ca. Civ. Code §3513 (2017). A class action waiver violates this section of the Civil Code, the Court reasoned, because "[t]he PAGA was clearly established for a public reason, and agreements requiring the waiver of PAGA rights would harm the state's interests in enforcing the Labor Code and in receiving the proceeds of civil penalties used to deter violations." 59 Cal.4th at 383. Therefore, the Court concluded, an arbitration agreement, even with a class action waiver, cannot waive a person's authority to bring a PAGA action because it violates California's clearly enunciated public policy. *Id*. at 384.

The Court also found that the FAA does not preempt this particular state law rule (as opposed to the *Discover Bank* rule preempted in the *AT&T v. Concepión* case), finding: "that the rule against PAGA waivers does not frustrate the FAA's objectives because . . . the FAA aims to ensure an efficient forum for the resolution of *private* disputes, whereas a PAGA action is a dispute between an employer and the state Labor and Workforce Development Agency." *Id.* at 384. In addition, the legislative history of the FAA shows that its"primary object was the settlement of ordinary commercial disputes . . . There is no indication that the FAA was intended to govern disputes between the government in its law enforcement capacity and private

[2] *Iskanian* was decided in 2014, two years before the Ninth Circuit's 2016 decision in *Morris v. Ernst & Young*, which found that class waivers could violate the NLRA. 834 F.3d at 983.

individuals.," the Court noted. *Id*.

The United States Supreme Court's decision in *EEOC v. Waffle House* lends further support to the conclusion that the FAA does not affect governmental enforcement of the law, the California Court found. *Id*. at 386. In *Waffle House*, the Court held that the Equal Employment Opportunity Commission was not bound by an individual employee's arbitration agreement to resolve disputes through arbitration only and could therefore exercise its statutory authority in bringing a lawsuit in court against the Waffle House on behalf of the employee. 534 U.S. 279, 288-289; 122 S.Ct. 754 (2002). Although Iskanian had signed the arbitration agreement in his individual capacity, the arbitration agreement did not affect his ability to bring a PAGA action because he was acting as an arm of the California state government, not as an individual. The Court held:

> Simply put, a PAGA claim lies outside the FAA's coverage because it is not a dispute between an employer and an employee arising out of their contractual relationship. It is a dispute between an employer and the *state,* which alleges directly or through its agents—either the Labor and Workforce Development Agency or aggrieved employees—that the employer has violated the Labor Code.

Id. at 386-387.

In 2015, the federal Ninth Circuit Court of Appeals agreed with the California Supreme Court on both issues *Iskanian* had addressed: 1) PAGA actions cannot be waived by agreement; and 2) the FAA does not preempt PAGA. *Sakkab v. Luxottica Retail North America, Inc.*, 803 F.3d 425, 437-439 (9th Cir. 2015). *See also Mohammed v. Uber Technologies,* 836 F.3d 1102, 1113 (9th Cir. 2016) (although Uber drivers could be compelled to arbitrate their wage and hour claims individually, their PAGA claims cannot be waived).

C. An arbitration agreement can, nonetheless, require PAGA claims to be arbitrated rather than litigated in court. In *Valdez v. Terminix International Company Limited Partnership*, __Fed.Appx. ___ 2017 WL 836085 (9th Cir. 2017) (note that the court deemed the case "not appropriate for publication and is not precedent"), the federal Ninth Circuit Court of Appeals held that although the Ninth Circuit had ruled previously that a plaintiff's PAGA claims could not be waived by an arbitration agreement, *Iskanian* had not barred PAGA claims from being heard by an arbitrator rather than by a court. *Id*., *also citing Sakkab v. Luxottica Retail N. Am., Inc.*, 803 F.3d 425, 429 (9th Cir. 2015). Further, a magistrate judge in the Northern District of California had held previously that where an arbitration agreement clearly and unmistakably delegates questions of arbitrability to an arbitrator, an arbitrator, not the court, has the authority to decide whether the PAGA claims are arbitrable under the agreement. *Lewis v. Caviar*, __ F.Supp.3d ___2016 WL 270619 (N.D. Ca. 2016) (Docket No.3:15-cv-01285-EDL).

D. Industry-specific regulatory attempted solutions. During the Obama administration, two agencies finalized rules addressing arbitration agreements in the financial services and nursing home industries. However, after the 2016 election, either Congress or the agency involved rescinded the rules.

1. Financial services. The Consumer Protection Financial Board (CFPB) had issued a final rule on July 19, 2017 that would have prohibited federally-regulated financial services providers "from using a pre-dispute arbitration agreement to block consumer class actions in court." https://www.federalregister.gov/documents/2017/07/19/2017-14225/arbitration-agreements , 82 Fed. Reg. 33210 (7/19/17). However, Congress voted to rescind the rule on October 25, 2017. https://www.npr.org/sections/thetwo-way/2017/10/25/559950275/senate-kills-rule-on-class-action-suits-against-financial-companies .

2. Nursing homes. In 2016, the Centers for Medicare and Medicaid Services (CMS) had issued a rule that would have prohibited federally-funded nursing homes from entering into any type of pre-dispute arbitration agreements (including class action waivers) with their residents. 42 C.F.R. § 483.70 (2016). The agency had found the agreements to be "fundamentally unfair because, among other things, it is almost impossible for residents or their decision-makers to give fully informed and voluntary consent to arbitration before a dispute has arisen." 81 Fed. Reg. 68792 (10/4/16), https://www.federalregister.gov/documents/2016/10/04/2016-23503/medicare-and-medicaid-programs-reform-of-requirements-for-long-term-care-facilities . However, the American Health Care Association won a preliminary injunction against enforcement of the rule on November 7, 2016. *American Health Care Association v. Burwell*, Civil Action No. 3:16-CV-00233 (N.D. Miss. 2016). On June 8, 2017, CMS proposed a rule that would revise the rule to no longer ban pre-dispute arbitration agreements. 82 Fed. Reg. 26649 (6/8/17), https://www.federalregister.gov/documents/2017/06/08/2017-11883/medicare-and-medicaid-programs-revision-of-requirements-for-long-term-care-facilities-arbitration . Instead, the revised rule would retain the portions of the rule that required any proposed arbitration agreements to be explained to residents and would impose a new requirement for "plain language" in all arbitration agreements. The agency has not yet taken further action on the rule, but it has instructed its staff and related agencies to honor the preliminary injunction against the 2016 Obama-era rule.

E. Proposed legislation concerning sexual harassment claims. The recent focus on sexual harassment has spurred some lawmakers to try to outlaw mandatory arbitration of sexual discrimination claims as a condition of employment.

1. Federal. On December 6, 2017, Senators Kirsten Gillibrand (D-N.Y.) and Lindsey Graham (R-S.C.) joined with four other senators to introduce S. 2203, the "Ending Forced Arbitration of Sexual Harassment Act of 2017." https://www.congress.gov/bill/115th-congress/senate-bill/2203/text?format=txt . The bill would amend the Federal Arbitration Act to render predispute arbitration agreements unenforceable in sex discrimination disputes, which are defined as employment disputes arising from cognizable sex discrimination claims under Title VII. This would, of course, cover class action waivers. Because it is a direct amendment of the FAA, there would be no potential for a *Concepción*-based or other type of FAA challenge if the bill became law.

Although the bill exempts collective bargaining agreements (CBAs) from its provisions, it makes an exception to that exception by providing that "no . . . arbitration provision [in a

CBA] shall have the effect of waiving the right of an employee to seek judicial enforcement of a right arising under a provision of the Constitution of the United States, a State constitution, or a Federal or State statute, or public policy arising therefrom." S. 2203, § 402(b)(2). This appears to disturb the holding in *14 Penn Plaza v. Pyett*, 556 U.S. 247 (2009). In that case, the Supreme Court had held that if the arbitration clause of a CBA covered statutory discrimination claims and if it "clearly and unmistakably" waived a bargaining unit member's opportunity to pursue those claims in court, then the waiver was enforceable.

2. New York. In New York, Governor Andrew Cuomo proposed a bill that would prohibit an employer from forcing an employee to enter into any "written contract" that "would restrict or limit such employee's ability to bring or adjudicate claims relating to unlawful discriminatory practices based on sexual harassment in any forum." N.Y. Executive Budget Title VII "Women's Agenda" Bill, Part I, Subpart B (p. 49), https://www.budget.ny.gov/pubs/archive/fy19/exec/fy19bills.html . Although this bill was crafted to apply to any "written contract," it is obviously aimed at predispute arbitration clauses, including those that waive a party's right to participate in a class action. If the bill became law, employers would likely bring a *Concepción*-based challenge, arguing that the law violates the FAA because it disfavors arbitration.