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THE TUG OF WAR OVER MANDATORY EMPLOYMENT ARBITRATION AGREEMENTS

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AGENDA

1. Recent Developments in Arbitration of Claims under the Private Attorneys General Act (PAGA)

2. Essential Elements of an Enforceable Arbitration Agreement

3. Basics of PAGA Claims

4. Drafting and Identifying Enforceable Arbitration Agreements in Light of Recent Developments

5. Potential Impact of Recent Developments on Employment Litigation

The Tug of War Over
Mandatory Employment Arbitration Agreements

By Margaret J. Grover[1]

For decades, employers have been trying to force employment disputes into arbitration. State and federal courts, and the California legislature have regularly re-shaped the requirements and scope of agreements under which employment claims can be compelled to arbitration. The two most recent decisions, *Viking River Cruises, Inc. v. Moriana*, 596 U.S. ___, 142 S.Ct. 1906 (2022) and *Adolph v. Uber Technologies, Inc.*, 14 Cal. 5th 1104, 532 P.3d 682 (2023) addressed the enforcement of arbitration provisions limiting an employee's right to bring claims under the Private Attorneys General Act of 2004, California Labor Code Sections 2698 through 2699.5 (PAGA).

Basic Standards for Arbitration of Employment Claims

In 2000, the California Supreme Court recognized that arbitration of claims under the California Fair Employment and Housing Act can be compelled if the arbitration permits an employee to vindicate his or her statutory rights. *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal. 4th 83, 90-91, 6 P.3d 669, 674, 99 Cal. Rptr. 2d 745, 750 (Cal. 2000). An agreement allows for vindication to occur if it "(1) provides for neutral arbitrators, (2) provides for more than minimal discovery, (3) requires a written award, (4) provides for all of the types of relief that would otherwise be available in court, and (5) does not require employees to pay either unreasonable costs or any arbitrators' fees or expenses as a condition of access to the arbitration forum." *Id*. at 102, 6 P.3d at 682, 99 Cal. Rptr. 2d at 759.

Courts also evaluate whether the arbitration agreement is unconscionable. "One common formulation of unconscionability is that it refers to 'an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.' [Citation.] As that formulation implicitly recognizes, the doctrine of unconscionability has both a procedural and a substantive element, the former focusing on oppression or surprise due to unequal bargaining power, the latter on overly harsh or one-sided results. 'The procedural element of an unconscionable contract generally takes the form of a contract of adhesion, 'which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it.' " *Sonic-Calabasas A, Inc. v. Moreno*, 57 Cal. 4th 1109, 1133, 311 P.3d 184, 194, 163 Cal. Rptr. 3d 269, 281 (2013).

"Procedural and substantive unconscionability must both be present in order for a court to exercise its discretion to refuse to enforce a contract or clause under the doctrine of unconscionability. But they need not be present in the same degree. Essentially a sliding scale is invoked that disregards the regularity of the procedural process of the contract formation, that creates the terms, in proportion to the greater harshness or unreasonableness of the substantive terms themselves. In other words, the more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is

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unenforceable, and vice versa." *Armendariz*, 24 Cal. 4th at 88, 6 P.3d at 690, 99 Cal. Rptr. 2d at 767.

A number of factors contribute to the determination of whether an arbitration agreement is unconscionable. The following list provides some examples, but is not intended to be exhaustive:

- Mutuality of Agreement, including whether claims the employee is likely to bring are given the same treatment as claims the employer is likely to bring. *Nyulassy v. Lockheed Martin Corp.*, 120 Cal. App. 4th 1267, 1287, 16 Cal. Rptr. 3d 296, 311 (2004); *Mercuro v. Superior Court*, 96 Cal. App. 4th 167, 175-76, 116 Cal. Rptr. 2d 671, 611 (2002).
- Neutrality of Arbitrator Selection Process. *Chavarria v. Ralphs Grocery Co.*, 733 F.3d 916, 923-24 (9th Cir. 2013).
- Limitations on Available Discovery. *Fitz v. NCR Corp.*, 118 Cal. App. 4th 702, 717-18, 13 Cal. Rptr. 3d 88, 97-98 (2004).
- Limitations on Recoverable Damages: *Armendariz*, 24 Cal. 4th at 121, 6 P.3d at 694, 99 Cal. Rptr. 2d at 772.
- Terms Affecting Recovery of Attorney's Fees and Costs. *Serafin v. Balco Properties Ltd.*, 235 Cal. App. 4th 165, 184-85, 185 Cal. Rptr. 151, 165 (2015).
- Lack of Meaningful Opportunity to Negotiate or Opt Out. *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165, 1171-72 (9th Cir. 2003).
- Employer's Ability to Modify Unilaterally. *Ingle*, 328 F.3d 1165, 1179 (9th Cir. 2003).
- Oppression. *Baxter v. Genworth North America Corp.*, 16 Cal. App. 5th 713, 722, 224 Cal. Rptr. 3d 556, 564 (2017),
- Unfair Surprise, which may cover "a variety of deceptive practices and tactics, including hiding a clause in a mass of fine print or phrasing a clause in language that is incomprehensible to a layperson." *Penilla v. Westmont Corp.*, 3 Cal. App. 5th 205, 216, 207 Cal. Rptr. 3d 473, 482 (2016).

PAGA Essentials

PAGA was enacted in 2004, providing "aggrieved" employees a private right of action against a California employer in order to collect penalties on behalf of the state's Labor and Workforce Development Agency (LWDA). It is technically a type of *qui tam* claim. PAGA requires that 75 percent of any penalties collected be paid to the LWDA, with the remaining 25 percent distributed to the aggrieved employees. If successful, the plaintiff in a PAGA action is entitled to recover attorneys' fees and costs.

PAGA groups violations into three categories and provides for slightly different procedures for each category:

- *Violations of Labor Code Provisions Specifically Listed in Labor Code section 2699.5*. There are over 150 different violations listed, including Section 203 (waiting time penalties), Section 226.7 (meal and rest break premiums), Section 1198 (which includes any "conditions prohibited by the wage order")4, and certain violations of Section 226 (wage statement penalties).

  Before commencing a category one claim, an employee must give written notice describing the "specific provisions … alleged to have been violated, including the facts

and theories to support the alleged violation" to the LWDA via its website (along with a $75 filing fee) and on the employer via certified mail. A PAGA lawsuit can be dismissed outright if the notice is deficient.

If the LWDA declines to investigate, or otherwise fails to respond to the employee, within 65 days of the postmark date of the notice, then the employee can proceed to file a civil lawsuit seeking PAGA penalties.

- *Health and Safety Violations (Labor Code 6300 et seq.).* The second category is for health and safety violations predicated on any section of Labor Code sections 6300 et seq. (other than those listed in Section 2699.5).

  In addition to sending notice to LWDA and employer, an employee bringing a health and safety based PAGA claim must also send notice to the Division of Occupational Safety and Health, which is then required to investigate the claim. If the Division issues a citation, the employee is precluded from commencing a civil action under PAGA. In the alternative, if the Division does not issue a citation, then the aggrieved employee may appeal to the Superior Court for an order directing the Division to issue a citation.

- *All Other Labor Code* Violations. The third category is for Labor Code violations other than those covered by the first two categories. Some common violations include wage statements that fail to provide inclusive dates of a pay period or the legal employer's name and address, as required by Labor Code Section 226.

  The notice requirement is the same as category one claims but an employer can "cure" the violation within 33 days of the PAGA notice. An employer sends notice to LWDA and the employee describing the actions taken to cure the violation. The employee can respond to the LWDA, as to why those actions did not actually cure the violation, and the LWDA has 17 days to review the actions taken and determine whether the employer did in fact cure the violations. There are limitations on the number of times an employer can avail itself of the cure provision.

  If the LWDA determines that the employer did not cure the violations, or otherwise fails to provide a timely response, then the employee can proceed with the civil lawsuit. If the LWDA instead determines the violations have been cured, then an employee can appeal the agency's determination by filing an action with the Superior Court.

PAGA claims are subject to the one-year statute of limitations. The limitations period is tolled by serving a PAGA notice until the employee fully exhausts his or her administrative remedies. Even though PAGA is a representative action, it does not need to be certified as a class action. *See Arias v. Superior Court*, 46 Cal. 4th 969 (2009). If the underlying Labor Code provision already provides for a civil penalty, then an employee can seek to collect that penalty on behalf of other aggrieved employees.

Where the underlying Labor Code section does not already provide a civil penalty, the PAGA penalty is equal to $100 per employee per pay period for the initial violation and $200 for each employee per pay period for each subsequent violation. These claims can mount quickly. A trial court must review and approve any proposed settlement that releases PAGA claims. A copy of the proposed settlement must also be submitted to the LWDA online at the same time as the court.

Decisions Regarding Arbitration of PAGA Claims

The California Supreme Court first weighed in on the arbitrability of PAGA claims in *Iskanian v. CLS Transp. Los Angeles, LLC*, 59 Cal. 4th 348, 382, 327 P. 3d 129, 148, 173 Cal. Rptr. 3d 289 (2014). In that matter, Plaintiff Iskanian had signed an agreement with his employer providing for binding arbitration of any and all claims arising out of his employment. *Id.* at 360, 327 P. 3d at 133, 173 Cal. Rptr. 3d at 294. The agreement stated that "each will not assert class action *or representative action claims* against the other in arbitration or otherwise. . .." *Id*. at 360-61, 327 P. 3d at 133, 173 Cal. Rptr. 3d at 294. Plaintiff Iskanian alleged Labor Code violations as an individual, a putative class representative, and in a representative capacity under PAGA. *Id*. at 361, 327 P. 3d at 294, 173 Cal. Rptr. 3d at 133. T

The California Supreme Court discussed whether a state court could refuse to enforce an arbitration agreement waiving the right to pursue class action proceedings and waiving the right to pursue representative claims under PAGA. This article discusses only the PAGA waiver issues. The court held an employee's right to bring a PAGA claim was "unwaivable." *Id*. at 383, 327 P. 3d at 148-49, 173 Cal. Rptr. 3d at 312. By enacting PAGA, the Legislature determined that it was "in the public interest to allow aggrieved employees, acting as private attorneys general, to recover civil penalties for Labor Code violations, with the understanding that labor law enforcement agencies were to retain primacy over private enforcement efforts." An aggrieved employee's PAGA action for civil penalties is a substitute for an action brought by the government itself, the government is always the real party in interest, and a judgment thus binds all those, including nonparty aggrieved employees, who would be bound by a judgment in an action brought by the government. *Id*. at 381-82, 327 P. 3d at 147, 173 Cal. Rptr. 3d at 310-11.

In *Viking River Cruises, Inc. v. Moriana*, 596 U.S. ___, 142 S.Ct. 1906 (2022), the United States Supreme Court considered a predispute employment contract with an arbitration provision specifying that "in any arbitral proceeding, the parties could not bring any dispute as a class, collective, or representative PAGA action. It also contained a severability clause specifying that if the waiver was found invalid, any class, collective, representative, or PAGA action would presumptively be litigated in court. But under that severability clause, if any 'portion' of the waiver remained valid, it would be 'enforced in arbitration.'" *Id.*, 142 S.Ct. at 1915-16.

The United States Supreme Court held that the Federal Arbitration Act, 9 U.S.C. sec. 1 *et seq.*, (FAA) compelled enforcement of an arbitration agreement that waived an employee's right to bring *individual* claims through PAGA and declared that the FAA "preempted" a separate state law rule that "PAGA actions cannot be divided into individual and non-individual claims" where the parties have agreed to arbitrate individual claims; and that, once those individual claims are sent to arbitration, the employee lacked standing to bring representative claims for violations of the California Labor Code on behalf of other aggrieved employees. *Id.*, 142 S.Ct. at 1917.

The California Supreme Court' decision in *Adolph v. Uber Technologies, Inc.*, 14 Cal. 5th 1104, 532 P.3d 682 (2023) 2023) opened the door for an employee to pursue PAGA claims in court, even when the employee had agreed to arbitrate the employee's personal alleged Labor Code violations.

Plaintiff Adolph was bound by a technology services agreement that included an arbitration provision requiring him to arbitrate, on an individual basis only, almost all work-related claims he might have against Defendant Uber. With regard to PAGA actions, the agreement stated: "To the extent permitted by law, you and Company agree not to bring a representative

action on behalf of others under the [PAGA] in any court or in arbitration. This waiver shall be referred to as the `PAGA Waiver.'" The agreement also includes a severability clause: "If the PAGA Waiver is found to be unenforceable or unlawful for any reason, (1) the unenforceable provision shall be severed from this Arbitration Provision; (2) severance of the unenforceable provision shall have no impact whatsoever on the Arbitration Provision or the Parties' attempts to arbitrate any remaining claims on an individual basis pursuant to the Arbitration Provision; and (3) any representative actions brought under the PAGA must be litigated in a civil court of competent jurisdiction ...."

In *Adolph*, the court explained that "[t]To have PAGA standing, a plaintiff must be an 'aggrieved employee'—that is, (1) 'someone `who was employed by the alleged violator'' and (2) ''against whom one or more of the alleged violations was committed.'' *Id*. at 1114, 532 P.3d at 686 (citations omitted). Relying on this analysis, the Court held: **"Where a plaintiff has brought a PAGA action comprising individual and non-individual claims, an order compelling arbitration of the individual claims does not strip the plaintiff of standing as an aggrieved employee to litigate claims on behalf of other employees under PAGA.**" *Id*.

The decision in *Adolph* also addressed some logistical issues arising when the plaintiff has brought a PAGA action comprising individual and representative claims, explaining that the "PAGA action could proceed in the following manner if [the plaintiff] were ordered to arbitrate [their] individual PAGA claim: First, the trial court may exercise its discretion to stay the [representative] pending the outcome of the arbitration pursuant to section 1281.4 of the Code of Civil Procedure. Following the arbitrator's decision, any party may petition the court to confirm or vacate the arbitration award under section 1285 of the Code of Civil Procedure. If the arbitrator determines that [the plaintiff] is an aggrieved employee in the process of adjudicating his individual PAGA claim, that determination, if confirmed and reduced to a final judgment (Code Civ. Proc., § 1287.4), would be binding on the court, and [the plaintiff] would continue to have standing to litigate [their] non-individual claims. If the arbitrator determines that [the plaintiff] is not an aggrieved employee and the court confirms that determination and reduces it to a final judgment, the court would give effect to that finding, and [the plaintiff] could no longer prosecute [representative] claims due to lack of standing." *Id*. at 1123-24, 532 P.3d at 692-93.

Practical Actions

In light of *Adolph v. Uber Technologies, Inc.*, *Adolph v. Uber Technologies, Inc.*, 14 Cal. 5th 1104, 532 P.3d 682 (2023), both employers and employees may have strategic decisions to make.

For employers, these include:

1. Whether to require arbitration of PAGA claims, with the possible result of having to litigate the claims in two forums. This may well depend on the size of the workforce and whether the employer believes that an arbitrator is more likely than a judge to concluded that an individual plaintiff is an "aggrieved employee."
2. Whether to include a severance provision in any arbitration agreement, so that any finding that a provision of that agreement would not invalidate the entire agreement.

3. Whether to compel arbitration of PAGA claims, with the result of having to litigate the claims twice. This may depend upon the types of claims raised by the employee and the potential for defending any or all of them.

For employees, these include:

1. Determining whether any arbitration agreement contains the essential requirements set forth in *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal. 4th 83, 90-91, 6 P.3d 669, 674, 99 Cal. Rptr. 2d 745, 750 (Cal. 2000).
2. Evaluating whether any arbitration agreement is either procedurally or substantively unconscionable.
3. Determining whether the arbitration agreement includes a severance provision.
4. Evaluating whether the potential recovery on PAGA claims warrants the expense of litigation in multiple fora.
5. Determining whether to bring any PAGA claims in a separate action, to enhance the likelihood of the PAGA claims being pursued as a single action.