



Iskanian v. CLS Transportation:
Class Action Waivers Are Enforceable In Employment Arbitration Agreements. Period.
Representative Action Waivers That Preclude All PAGA Claims Are Not.

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On June 23, 2015, the California Supreme Court in *Iskanian v. CLS Transportation Los Angeles, LLC*, No. S204032, answered two questions that have been excruciatingly litigated in California courts since the U.S. Supreme Court's landmark decision in *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011) (class actions cannot be ordered in arbitration absent agreement by the parties; class action waivers are valid; any rule to the contrary is preempted by the Federal Arbitration Act (FAA)) (*Concepcion*):

1. Despite *Concepcion*, are class action waivers in employment arbitration agreements subject to the limitations of *Gentry v. Superior Court*, 42 Cal. 4th 443 (2007) (if individual arbitration or litigation cannot be designed to approximate the advantages of a class proceeding, then a class waiver is invalid) (*Gentry*) and/or invalid under Section 7 of the National Labor Relations Act ("Employees shall have the right ... to engage in ... concerted activities for the purpose of ... mutual aid or protection") (NLRA)? **Answer: No.**

2. Are *representative action* waivers in employment arbitration agreements valid? **Answer: No, not if they preclude representative actions under the California Private Attorneys' General Act (PAGA) from being pursued in any forum.**

Will *Iskanian* survive U.S. Supreme Court scrutiny? Yes, and maybe no. Below, we address each of the California Court's momentous holdings in turn. We wrap up by identifying certain questions that remain unanswered, and making some predictions.

Background

Iskanian, a driver for CLS Transportation Los Angeles, LLC (CLS), signed an arbitration agreement with CLS providing, "[E]xcept as otherwise required under applicable law, (1) EMPLOYEE and COMPANY expressly intend and agree that class action and representative action procedures shall not be asserted, nor will they apply, in any arbitration pursuant to this Policy/Agreement; (2) EMPLOYEE and COMPANY agree that each will not assert class action or representative action claims against the other in arbitration or otherwise; and (3) each of EMPLOYEE and COMPANY shall only submit their own, individual claims in arbitration and will not seek to represent the interests of any other person."

After terminating his employment with CLS, Iskanian brought a putative class action against the company for, among other things, failure to pay overtime and failure to provide meal and rest periods. Plaintiff also sought to bring a representation action for penalties under PAGA. CLS

promptly filed a motion to compel individual arbitration under the parties' agreement, which the Superior Court granted. Plaintiff appealed. Before his appeal was decided, the California Supreme Court issued its decision in *Gentry* that class action waivers in employment arbitration agreements are invalid under California law in certain circumstances. CLS then voluntarily withdrew its motion to compel arbitration, and the parties proceeded to litigation. After three years of litigation in court, the Superior Court granted Iskanian's motion to certify the class action.

Then the U.S. Supreme Court issued *Concepcion*. CLS promptly renewed its motion to compel arbitration and to dismiss class claims, arguing that *Concepcion* invalidated *Gentry*. The Superior Court granted CLS's motion, ordered the case to arbitration, and dismissed Iskanian's claims with prejudice. Iskanian appealed. The Court of Appeal affirmed the Superior Court's decision. In so doing, the Court of Appeal rejected Iskanian's arguments that *Gentry* survived *Concepcion*, that class action waivers violated the NLRA, that CLS waived its right to compel arbitration, and that PAGA provides an unwaivable right to litigate in court.

The California Supreme Court granted review and holds as follows:

Class Action Waivers Are Enforceable In Employment Arbitration Agreements.

Gentry is Dead

Iskanian first holds that, "[u]nder the logic of *Concepcion*, the FAA preempts *Gentry's* rule against employment class waivers" (Sl. Op. at 8) – even though *Gentry* did not create a complete bar to class action waivers in the employment context, but rather allowed a plaintiff to establish that a class action waiver in a particular case should not be enforced after scrutinizing factors set forth in *Gentry*. Under *Concepcion*, the *Iskanian* Court recognizes that if the arbitration agreement is otherwise valid, then the included class-action waiver also is valid. Period. Any rule mandating special scrutiny of class action waivers in the employment context is preempted by the Federal Arbitration Act (FAA). *Gentry* is, thus, dead.

The NLRA Does Not Preclude Class Action Waivers

Iskanian next holds that Section 7 of the NLRA does "not represent 'a contrary congressional command' overriding the FAA's mandate." Sl. Op. at 21. In so holding, the California Supreme Court entirely follows the reasoning of the Fifth Circuit in *D.R. Horton, Inc. v. NLRB*, 737 F.3d 344 (5th Cir. 2013) – which rejected the position of the National Labor Relations Board (NLRB) in *D.R. Horton Inc. & Cuda*, 357 NLRB No. 184 (2012) (class action waivers improperly interfere with employees' rights to concerted action under Section 7). The FAA, *Iskanian* holds, preempts any NLRA-construed rule that cuts against arbitration. The FAA's Section 2 "savings clause" (that arbitration agreements are subject to challenge on grounds "for the revocation of any contract") does not assist the NLRB's position, because a rule that class waivers are invalid is not arbitration-neutral. Sl. Op. at 19. Further, "neither the NLRA's language nor its legislative history showed any indication of prohibiting a class action waiver in an arbitration agreement." Sl. Op.

at 19. Finally, there is no conflict between the FAA and the NLRA, which fact itself “favors arbitration.” Sl. Op. at 19-20.

After upholding class action waivers against Section 7 challenges in general, however, the Court cautions – in dicta – that a broad restriction against concerted activities could possibly still run afoul of Section 7. Sl. Op. at 20-21. Here, the Court did not have to consider such possibility, because the arbitration agreement at issue did not restrict employees from pooling resources, bringing group actions, using the same lawyer, discussing among each other their claims, or soliciting support from other employees.

CLS Did Not Waive Its Right To Move To Compel Arbitration

The Court next considered whether CLS waived its right to compel arbitration by withdrawing its motion after *Gentry* and then litigating the case in court for years until *Concepcion* came down. Iskanian argued that CLS waived its right by voluntarily dropping its motion after *Gentry*, that CLS took steps inconsistent with an intent to invoke arbitration, and that Iskanian was significantly prejudiced by the delayed motion. The Court rejects each of Iskanian’s arguments.

Faced With The Futility Of Pursuing Arbitration After Gentry, CLS Did Not Take Steps Inconsistent With Its Motion To Compel By Dropping Its Motion Until Concepcion Changed The Legal Landscape

“In light of the policy in favor of arbitration,” the Court preliminarily notes, “waivers are not to be lightly inferred and the party seeking to establish a waiver bears a heavy burden of proof.” Sl. Op. at 23-24 (Citation omitted.)

CLS pursued arbitration diligently from the outset, withdrew its motion only after *Gentry*, and then renewed its motion promptly after *Concepcion*. It acted reasonably at all steps. “[F]utility as grounds for delaying arbitration is implicit in the general waiver principles we have endorsed.” Sl. Op. at 23. “The fact that a party initially successfully moved to compel arbitration and abandoned that motion only after a change in the law made the motion highly unlikely to succeed weighs in favor of finding that the party has not waived its right to arbitrate.” Sl. Op. at 25. Since “neither party has ever disputed that the class action waiver at issue would not have survived *Gentry*,” futility here is undisputed. *Id.* This is not a case where a party dropped a motion to compel arbitration when it had a real chance of succeeding with the motion.

Financial Cost In Litigation Is Insufficient To Establish Prejudice Absent “Unreasonable” or “Unjustified” Behavior By The Proponent Of Arbitration

Iskanian’s contention that he spent a considerable amount of effort and money litigating class certification over the three years the case remained in court between *Gentry* and *Concepcion*, alone, does not establish sufficient prejudice to find waiver by CLS. “[C]ourts will not find prejudice where the party opposing arbitration shows only that it incurred court costs and legal

expenses.” Sl. Op. at 26. (Citation omitted.) Costs are considered, rather, only when the delay in bringing a motion to compel arbitration is *unreasonable* or *unjustified*. Sl. Op. at 27. Neither applies here. Further, Iskanian did not establish other forms of prejudice that could possibly be grounds for finding waiver, such as a gain of information by CLS in court that it could not have gained in arbitration, or the loss of evidence from delay.

Representative Action Waivers That Preclude PAGA Claims Are Not Enforceable.

Holding

Having found that class action waivers are valid in arbitration agreements and that CLS did not waive its right to compel individual arbitration, the Court next turned to the enforceability of Iskanian’s waiver of “representative” actions, in particular, PAGA actions. The four justice majority (Justices Liu, Corrigan, Kennard and Chief Justice Cantil-Sakauye) held that that an agreement requiring a complete waiver of an employee’s right to bring a representative action in any forum, specifically here an action for civil penalties under the California Private Attorneys General Act (PAGA) Cal. Lab. Code §2698 et seq., is contrary to public policy and thus unenforceable. The majority concluded that a PAGA representative action is not a private dispute to which the Federal Arbitration Act applies and, therefore, the “FAA does not preempt a state law that prohibits waiver of PAGA representative actions in an employment contract.” Sl. Op. at 2.

Disagreement Among Courts Following Concepcion

The California legislature adopted the PAGA “to prescribe a civil penalty for existing Labor Code sections for which no civil penalty has otherwise been established, and to allow aggrieved employees . . . to bring a civil action to collect civil penalties for Labor Code violations previously only available in enforcement actions initiated by the state’s labor law enforcement agencies.” *Caliber Bodyworks Inc. v. Super. Ct.*, 134 Cal. App. 4th 365, 374 (2005). See also Sl. Op. at 32 (“The civil penalties recovered on behalf of the state under the PAGA are distinct from the statutory damages to which employees may be entitled in their individual capacities.”). Following the U.S. Supreme Court’s decision in *Concepcion*, the California state and federal courts disagreed on whether the reach of *Concepcion* extended to representative-action waivers under PAGA. With *Iskanian*, the California Supreme Court answered the question in the negative as to complete waivers of representative actions in any forum. Left unanswered is whether a more limited waiver would have been permitted.

The Majority’s Analysis Invalidating Waivers of Representative Actions in Any Forum

The majority began its analysis of the PAGA waivers with the observation that there was “no dispute that the contract’s term ‘representative actions’ cover[ed] representative actions brought under [PAGA].” Sl. Op. at 28. Explaining that a PAGA action is, by its nature, a “representative” action, the Justices concluded that the arbitration agreement in question prevented Iskanian from asserting a claim for PAGA penalties in *any* forum. Sl. Op. at 2.

The majority analogized PAGA to a *qui tam* action, with the exception that “a portion of the penalty goes not only to the citizen bringing the suit but to all employees affected by the Labor Code violation. The government entity on whose behalf the plaintiff files suit is always the real party in interest in the suit.” Sl. Op. at 33. The majority observed that PAGA is an action brought for the benefit of others and not solely for the benefit of him or herself. And while “anyone may waive the advantage of a law intended solely for his benefit,” a law “established for a public reason cannot be contravened by a private agreement.” Sl. Op. at 34. As such, the Justices concluded that “an employee’s right to bring a PAGA action is unwaivable” and an employment agreement cannot “eliminate [the choice of whether or not to bring a PAGA action] by requiring employees to waive the right to bring a PAGA action before any dispute arises.” Sl. Op. at 34-35.

Having concluded that a waiver of a PAGA representative action is against California public policy, the majority then examined whether the rule against PAGA waivers “frustrates the FAA’s objectives.” The majority concluded that it did not, 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.” Sl. Op. at 37 (emphasis in the original). “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.” Sl. Op. at 40. Because the majority concluded that the plaintiff is simply acting as an agent of the state, and because the state is not a party to the arbitration agreement, there is no conflict between the private contract to arbitrate and the FAA.

In finding no preemption, the majority appeared to distance its decision from the dictates of *Concepcion* and *Stolt-Nielsen*, which preclude a move from bilateral to multiparty arbitration without an express agreement. Instead, the justices explained that “[r]epresentative actions under the PAGA, unlike class action suits for damages, do not displace the bilateral arbitration of private disputes between employers and employees over their respective rights and obligations toward each other. Instead, they directly enforce *the state’s* interest in penalizing and deterring employers who violate California labor laws.” Sl. Op. at 41.

Finally, the majority rejected the argument advanced by the employer that PAGA “violates the principle of separation of powers under the California Constitution.” The employer argued that, by deputizing private counsel without providing oversight, the legislative branch interfered with the judicial branch’s ability to regulate the conduct of attorneys and thus interfered with the independence of the two branches of government. The majority disagreed. Even though PAGA deputizes private parties and their counsel to enforce the Labor Code, the majority concluded that the PAGA “does not present the same risks of abuse as when a city or county hires outside counsel to do its bidding.” Sl. Op. at 46.

Concurring Justices Agree with the Result but not the Rationale Put Forth by the Majority

Justices Chin and Baxter, in a separate concurrence, agreed that the PAGA representative action found in Iskanian's contract was illegal. However, they did so on different grounds. Questioning the majority's conclusion that PAGA claims fall outside of the FAA, the concurring opinion nevertheless determined that the complete waiver found in the arbitration agreement at issue was unenforceable. Conc. Sl. Op. at 1 ("[T]he arbitration agreement is invalid insofar as it purports to preclude plaintiff Arshavir Iskanian from bringing in any forum a representative action under [PAGA] and that this conclusion is not inconsistent with the FAA.")

Questions Left Unanswered By Iskanian

Are Non-Preclusive Representative Action Waivers Potentially Still Enforceable?

The main question left unanswered by *Iskanian* is whether it is possible to craft a waiver of a representative action without running afoul of *Iskanian*. First, any such waiver would have to not be absolute. In other words, the parties would need to be able to pursue representative actions in *some* forum. The inability to pursue them in *any* forum will not be upheld.

The majority did not conclusively decide whether a plaintiff can bring an "individual" PAGA action: "[W]hether or not an individual claim is permissible under the PAGA, a prohibition of representative claims frustrates the PAGA's objectives." Sl. Op. at 36. *See also* concurrent opinion at p. 4 ("Every PAGA action, whether seeking penalties for Labor Code violations as to only one aggrieved employee – the plaintiff bringing the action – or as to other employees as well, is a representative action on behalf of the state.") For years, the plaintiffs' bar has argued that there is no such thing as an individual PAGA action – that all PAGA actions are by their nature representative of all other "aggrieved employees." By contrast, defendants have argued that "representative" means on behalf of the state, so a plaintiff may bring a "representative" action under PAGA and seek penalties for only wrongs personal to the single plaintiff. By declining to side with the plaintiff on this point, the majority appears to have left open the possibility that an arbitration agreement may be fashioned to allow an individual PAGA action to proceed but, potentially, preclude collection of penalties on behalf of other employees. This is a point that could potentially be explored further by employers.

Will Defendants Be Able To Remove More PAGA Actions To Federal Court?

In discussing PAGA penalties, the majority confirmed what many PAGA practitioners previously thought: that the 25% of the penalty recovered under PAGA is distributed to "all employees affected by the Labor Code violation." Sl. Op. at 33. The Court's observation about penalty distribution is in direct contrast to *Cunningham v. Leslie's Poolmart Inc.*, 2013 WL 3233211 (C.D. Cal. June 25, 2013), where the District Court held last year that all 25% must go to the plaintiff.

The statement that the 25% not distributed to the state must go to all "employees affected" by the alleged violations may prove important for two reasons. First, it may reopen the door to

arguing that on removal, PAGA claims must be aggregated to meet the amount in controversy if, for example, a plaintiff chooses to bring them on behalf of a group of employees. And second, the statement that the penalties are distributed to all employees *affected* by the violations should provide ammunition to employers in convincing courts that any trial or other adjudication of PAGA penalties must be on an individual by individual basis (where such argument is appropriate, such as, for example, in claims for failure to pay wages owed, overtime, or missed meal/rest breaks).

How Will Parties And Courts Deal With Dual Proceedings?

Having concluded that the PAGA waiver was unenforceable, the court remanded the case to the trial court to determine how to proceed. “Iskanian must proceed with bilateral arbitration on his individual damages claims, and CLS must answer the representative PAGA claims in some forum. The arbitration agreement gives us no basis to assume that the parties would prefer to resolve a representative PAGA claim through arbitration.” Sl. Op. at 47.

The majority proposed a few options, including (a) agreement on a single forum to resolve PAGA and non-PAGA claims, or (b) bifurcation of claims, with individual claims proceeding in arbitration and PAGA claims in court and, if such bifurcation occurs, staying the arbitration pending the completion of PAGA court litigation. Sl. Op. at 47.

One other option, which the Court did not suggest, may also be to bifurcate, stay the litigation, adjudicate the underlying alleged violations in arbitration, and then determine what penalty, if any, would be assessed by the Court.

Litigants should carefully consider all options before initiating arbitration requests.

What’s Next?

Pundits speculate on whether the U.S. Supreme Court might take up on *certiorari* one or more holdings of *Iskanian*. We predict that both sides probably will file petitions for *certiorari*. Whereas the Plaintiff (and employee-advocacy groups) are likely to ask the Supreme Court to review *Iskanian’s* rejection of the NLRB’s position that class action waivers violate Section 7 of the NLRA, the Defendant (and employer-advocacy groups) are likely to seek Supreme Court review of *Iskanian’s* carve-out of PAGA representative claims from the FAA’s strong policy in favor of arbitration. We predict that the Supreme Court will be less interested in the former, given virtual uniform rejection of the NLRB’s position by the courts, and will be more interested in the latter, given its strong pronouncements in *Concepcion* and other cases that special carve-outs from arbitration agreements are invalid.

Unless and until the U.S. Supreme Court changes any aspect of *Iskanian*, we can expect more employers to implement arbitration agreements with class action waivers, which correspondingly may result in the filing of fewer employment class actions in California. That does not mean that plaintiffs will always concede arbitration, of course. California courts will



continue to scrutinize arbitration agreements for unconscionability. However, employers can overcome such challenges on the front end through careful drafting and implementation of their agreements. And the parties will not have to go through the rigors of *Gentry*-factor discovery before an arbitration motion can be decided. Courts should be able to shift cases to arbitration more quickly and allow arbitration to play out with less up-front costs to both parties.

Correspondingly, we can expect plaintiffs to file more “pure” PAGA representative actions in California courts when faced with arbitration agreements containing class action waivers. Or, potentially, plaintiffs may file more combination lawsuits that will force employers to decide whether to pursue arbitration knowing that some PAGA claims may need to stay in court.

Conclusion

The Supreme Court in *Iskanian* affirmed the FAA’s strong public policy in favor of arbitration, while – at the same time – creating an unwaivable right of employees to bring representative PAGA actions in some forum. Questions, however, remain unanswered. We should expect more clarification from the California and U.S. Supreme Courts on these and other tricky aspects of PAGA actions in the coming years. In the meantime, employers should enjoy the certainty that their class-action waivers are sound, as long as they have drafted and properly implemented sound arbitration agreements.