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UNDERSTANDING ARBITRATION OF PAGA CLAIMS

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The laws governing arbitration agreements when it comes to PAGA are complicated. They can be better understood, however, by understanding a few key points. First, the courts distinguish between individual PAGA claims and non-individual PAGA claims. They are not what you might think they are. Individual PAGA claims are claims in which an employee is representing the state in bringing the claim. Non-individual PAGA claims are claims brought by one employee on behalf of other employees. Both are considered representative claims.

Viking River Cruises 142 S. Ct. 1906 ("*Viking*"), decided on June 15, 2022, considered a 2014 case, *Iskanian* that held that PAGA waivers (of the right to a jury trial) are invalid in two circumstances: 1) when a plaintiff is a representative of the state (an individual claim), and 2) when an individual and non-individual PAGA claim would have to be separated (the "*Iskanian* Rules"). The Court in *Viking* upheld the first *Iskanian* Rule, confirming that a PAGA waiver is invalid when a plaintiff is representing the state, but struck down the second *Iskanian* Rule and gave an employer the right to enforce an arbitration agreement in a non-individual PAGA action even if it was brought with an individual PAGA case, as long as the Federal Arbitration Act ("FAA") applies to the case. If the FAA does not apply, both *Iskanian* Rules still apply.

The FAA says a court must compel arbitration if: 1) a valid arbitration agreement exists, and 2) the dispute is covered by the agreement.

In *Shams v. Revature LLC*, 2022 WL 3453068, decided August 17, 2022, the U.S. District Court in California found an arbitration agreement entered into as a condition of employment was valid under the FAA and based on its interpretation of *Viking*. It granted a motion to compel arbitration of non-individual claims and heard arguments on how to handle the individual PAGA claims. The *Shams* Court first considered whether the arbitration agreement was valid and found that it was valid. It pointed out that *Viking* said that waiver of jury trial (referred to in *Viking* as a class action waiver) in "any dispute as a class, collective or representative action" under PAGA was prohibited, *Viking* at 1911. The *Shams* case was a different situation in that the waiver makes clear it applies to only non-individual PAGA claims (claims brought by an employee on behalf of other employees, rather than on behalf of the state) and not to individual PAGA claims (claims brought on behalf of the state). Based on this, the *Shams* Court found that the arbitration agreement was valid.

Chamber of Commerce of the United States v. Bonta ("Bonta"), a Ninth Circuit Court of Appeals case decided originally on September 15, 2021, but then withdrawn on August 22, 2022, for rehearing, struck down two California statutes as unconstitutional. Both statutes penalize employers for requiring arbitration agreements to be signed as a condition of employment. The case gave a nice history of arbitration agreements that brings clarity to the underlying issues in most cases about arbitration agreements.

Historically, there were two judicial doctrines arising from case law that were long standing for years until the turn of the 20th Century. One made reducing the jurisdictional rights of the courts illegal. The other allowed a party to withdraw from arbitration at any time during arbitration. The FAA was a response to these two doctrines that lawyers and judges alike agreed were outdated. The purpose of the FAA was to ensure that arbitration agreements were enforceable in accordance with their terms. Making sure those agreements were also voluntary became the focus of the courts after the FAA passed. Many cases have invalidated arbitration agreements that were not considered to be voluntary – such as contracts of adhesion (contracts that cannot be negotiated), or contracts that are so one sided they are unconscionable (unfair or oppressive).

California Labor Code Section 432.6 was, in theory, supposed to make sure that arbitration agreements were entered into voluntarily. In practice, it prohibits an employer from limiting the forum for hearing a dispute covered by the California Fair Employment and Housing Act. Arbitration does just that. It limits the forum for hearing a dispute. An agreement to arbitrate is a waiver of the right to a jury trial in a court of law. Other Code Sections penalized employers for violating Section 432.6. Labor Code Section 433 makes violation of Article 3 of the Labor Code, which includes Section 432.6, a misdemeanor. CA Government Code Section 12953 makes violation of Section 432.6 an unlawful employment practice. Both were found to be unconstitutional by the Ninth Circuit in *Bonta*.

The Ninth Circuit issued an injunction finding that the California Code Sections likely violated the FAA. It based its decision on the Supremacy Clause of the U.S. Constitution, Article VI, clause 2, which says:

"This Constitution, and the laws of the United States ... shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the Constitution or laws of any State to the contrary notwithstanding."

Courts have determined that arbitration contracts must be on equal footing with other contracts. In other words, a contract to arbitrate cannot be unenforceable if another contract would not be unenforceable under the same circumstances. In addition, a state law can be preempted if it is an obstacle to the execution of the full purpose of an act of Congress – a federal law.

The Ninth Circuit analyzed both these arguments but found Labor Code Section 433 and Government Code Section 12953 unconstitutional because of the penalties imposed for violations. The Court said: "A state law that incarcerates an employer for six months for entering into an arbitration agreement 'directly conflicts with § 2 of the FAA.' citing *Casarotto*, 517 U.S. at 687,

116 S.Ct. 1652. An arbitration agreement cannot simultaneously be 'valid' under federal law and grounds for a criminal conviction under state law." *Chamber of Commerce of United States v. Bonta* (9th Cir. 2021) 13 F.4th 766, 781, *reh'g granted, opinion withdrawn* (9th Cir. 2022) 45 F.4th 1113.

The Court remanded the case for rehearing consistent with its opinion making the two California laws penalizing an employer for entering into an arbitration agreement with an employee as a condition of employment unconstitutional. The Court also tackled the standing issue and found that all that is required to have standing to bring a non-individual PAGA claim is that the plaintiff must be an aggrieved employee and one or more of the alleged violations must have been against the employee.

But then even the *Bonta* Court itself perhaps became confused by its own opinion and withdrew it leaving a big question mark on the issues of constitutionality of CA Labor Code Section 432.6, 433 and Government Code Section 12953 and leaving open too, the question of standing to bring a claim on behalf of the state if a non-individual claim is arbitrated.

How has all this affected PAGA claims? It depends on who you ask. Some say they have declined. Others say they are full speed ahead. Clearly, employers have some new tools in their belts until the many open issues are resolved.

What's next for arbitration agreements in California is anyone's guess. Everyone expects to see new legislation eventually pass in California once again, challenging the right of California employers to require arbitration agreements as a condition of employment. But for now, the enforceability of these code sections and case law prohibiting arbitration as a condition of employment under the FAA, is questionable at best.

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