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ARBITRATION

Recent U.S. Supreme Court decisions have upheld the enforceability of arbitration agreements under the Federal Arbitration Act, Orrick attorneys Joe Liburt and David Smith say in this BNA Insights article. But the California Supreme Court recently held that mandatory waivers of representative claims under the state's Private Attorneys General Act are precluded by state law.

The authors critique the state high court's reasoning and identify issues its decision has spawned in PAGA litigation.

Key Questions Remain After *Iskanian*

BY JOE LIBURT AND DAVID SMITH

The California Supreme Court's recent decision in *Iskanian v. CLS Transportation Los Angeles, LLC*, 59 Cal. 4th 348 (2014), holds that mandatory waivers of representative Private Attorneys General Act claims are unenforceable under California law (12 WLR 996, 6/27/14). The decision leaves open several important questions, not least whether the California Supreme Court's attempt to remove PAGA claims from the reach of the Federal Arbitration Act will succeed in light of the U.S. Supreme Court's slew of recent arbitration decisions commencing with *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011), (81 DLR AA-1, 4/27/11).

Question No. 1: Can Representative PAGA Claims Be Exempted From the FAA on the Basis of *Iskanian's* Public/Private Distinction? *Iskanian* reasons that they can, on the ground that the FAA does not cover "public" disputes. *Iskanian* purports to have surveyed U.S. Supreme Court precedent and found no cases that apply the FAA to "public" disputes. There are several responses to this public/private distinction. First, the U.S. Supreme Court has repeatedly made clear recently that the FAA displaces any state rule that purports to exempt a particular type of claim from the FAA, "even if it is desirable for unrelated reasons." *Concepcion*, 131 S. Ct. at 1747, 1753. That is precisely what *Iskanian* does.

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Second, the public/private distinction is dubious not only because *Iskanian* provides no affirmative case law support for the proposition that PAGA claims (or other allegedly *public* disputes) are outside the FAA's scope—and the U.S. Supreme Court makes no such distinction in its recent decisions—but because there is Ninth Circuit authority that applies the FAA to California claims that, similar to PAGA, courts have characterized as "public" claims. In *Ferguson v. Corinthian Colleges, Inc.*, 733 F.3d 928 (9th Cir. 2013), the Ninth Circuit held that the FAA preempts California's *Broughton-Cruz* rule that *public* injunctive relief claims cannot be arbitrated.

At issue in *Ferguson* was whether arbitration could be compelled on plaintiffs' request for injunctive relief under California's unfair competition law (UCL), false advertising law, and Consumer Legal Remedies Act (CLRA). These statutes are similar to PAGA in that a plaintiff acts as a "private attorney general" under the CLRA and acts "for the interests of itself, its members or the general public" under the UCL. *Id.* at 932-33.

Third, as Justice Chin noted in his *Iskanian* concurrence, a PAGA dispute arises "first and fundamentally" out of the *private* employment relationship. *Iskanian*, 59 Cal. 4th at 395 (Chin, J., concurring). To say that an employee suing her employer under PAGA so as to obtain money for herself and other employees (and the

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government) is in no way a ''private'' dispute is a curious assertion.

Indeed, the employee receives a monetary award; the employee is in charge of pursuing and litigating the PAGA action; the employee controls what allegations are in the complaint; the employee defines the group of employees whom he or she seeks to represent; and the employee can decide when to settle the claim.

Question No. 2: Does Iskanian Successfully Thread the FAA Loophole by Applying Generally Applicable State Law? *Iskanian* purports to prohibit prospective waivers of representative PAGA claims in arbitration provisions based on Civil Code sections 1668 and 3513. Although *Iskanian* characterizes this as an application of general contract law in order to avoid *Concepcion*'s holding against arbitration-specific state law rules, *Concepcion* makes clear that when a generally applicable state law doctrine is ''applied in a fashion that disfavors arbitration,'' that application of the state law doctrine is preempted by the FAA because it ''stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'' *Concepcion*, 131 S. Ct. at 1747, 1753.

An argument can be made that the manner in which *Iskanian* applies these state law principles to arbitration agreements disfavors arbitration and stands as an obstacle to the accomplishment of the FAA's purposes. As the U.S. Supreme Court explained, ''[t]he FAA mandates interpretation of an arbitration agreement in a manner that leads to arbitration, not away from it. States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons.'' *Concepcion*, 131 S. Ct. at 1753.

Question No. 3: Is It Possible to Bring an Individual PAGA Claim? The pre-*Iskanian* cases are all over the map on this. *Compare, e.g.*, *Quevedo v. Macy's, Inc.*, 798 F. Supp. 2d 1122, 1141, C.D. Cal., 2011 (''[Plaintiff's] PAGA claim is plainly arbitrable to the extent that he asserts it only on his own behalf.'') *with Reyes v. Macy's, Inc.*, 202 Cal. App. 4th 1119, 1123, 2011 (''A plaintiff asserting a PAGA claim may not bring the claim simply on his or her own behalf but must bring it as a representative action and include 'other current or former employees.' '')

***Iskanian* does not hold that plaintiffs cannot bring "individual" PAGA claims. Indeed, *Iskanian* seems to assume that an "individual" PAGA claim can be asserted, but states that barring "representative" claims frustrates the public policy behind the PAGA statute.**

Iskanian fundamentally changed the parlance of ''representative'' claims. Before Prop. 64 amended California's Unfair Competition Law, the courts and bar referred to non-class UCL claims in which the plaintiff represented other individuals as ''representative'' claims. When the California Supreme Court held in *Arias v. Superior Court*, 46 Cal. 4th 969 (2009), that a PAGA plaintiff did not need to obtain class certification to represent other ''aggrieved employees,'' such claims were similarly referred to as non-class ''representative'' claims because the plaintiff could represent other individuals. Consequently, many arbitration agreements contain provisions intended to ensure that employee arbitrations are not ''representative'' in the commonly understood sense of representing other employees.

Iskanian assigns a broader meaning to ''representative''— not merely representing other individuals, but ''representing'' the state as the ''agent'' or ''proxy'' of the state. Thus, whereas pre-*Iskanian* it was commonly understood that an ''individual'' claim, by definition, was not a ''representative'' claim, under *Iskanian* every PAGA claim is a ''representative'' claim (in the sense of representing the state), regardless of whether it is an ''individual'' claim or a claim brought on behalf of many ''aggrieved employees.''

This new nomenclature is significant. *Iskanian* does not hold that plaintiffs cannot bring ''individual'' PAGA claims. Indeed, *Iskanian* seems to assume that an ''individual'' PAGA claim can be asserted, but states that barring ''representative'' claims frustrates the public policy behind the PAGA statute. *Iskanian*, 59 Cal. 4th at 384.

Under *Iskanian*'s analysis, because any PAGA claim is inherently a ''representative'' claim (in the sense of representing the government), *Iskanian*, 59 Cal. 4th at 387, a compelled waiver of ''representative'' claims is not allowed under California law because it necessarily means the compelled waiver of *all* PAGA claims, whether individual or on behalf of other ''aggrieved employees.''

Moreover, *Iskanian* insists that ''an employee is free to forgo the option of pursuing a PAGA action'' altogether, *Iskanian*, 59 Cal. 4th at 387, and it would be odd to require every PAGA claim to represent all ''aggrieved employees,'' not least because such a rule could create a race to judgment among competing PAGA plaintiffs who necessarily would have entirely overlapping claims if the rule were that every PAGA claim must represent all other ''aggrieved employees.''

If, indeed, individual PAGA claims can be brought, then an arbitration agreement that requires any PAGA claim to be arbitrated as an individual claim does not bar PAGA claims from being pursued in any forum. And even if an arbitration agreement bars ''representative'' PAGA claims and such language is held invalid under *Iskanian*'s reasoning (because every PAGA claim is a ''representative'' claim in the sense of representing the government), the agreement may yet reach the same result if it has other language requiring any dispute to be an ''individual'' claim, or otherwise specifies (without specifically barring ''representative'' claims) that the employee cannot combine or join claims with other employees. *See* Cal. Civ. Code § 1599 (''Where a contract has several distinct objects, of which one at least is lawful, and one at least is unlawful, in whole or in part, the contract is void as to the latter and valid as to the rest.'').

Question No. 4: What About the "Vindication of Substantive Statutory Rights" Argument Against PAGA Waivers? The FAA's ''effective vindication'' exception, permitting the invalidation of an arbitration agreement when arbitration would prevent the ''effective vindication'' of a *federal* statute, does not extend to *state* statutory claims. *See Ferguson*, 733 F.3d at 936.

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Moreover, *Iskanian*'s explanation of the essence of a PAGA claim defeats a ''vindication of substantive statutory rights'' theory. A PAGA claim allows an employee plaintiff to serve as a ''proxy or agent of the state's labor enforcement agencies.'' *Iskanian*, 59 Cal. 4th at 380 (quoting *Arias*). As *Iskanian* makes clear, ''[t]he government entity on whose behalf the plaintiff files suit is always the real party in interest in the suit.'' *Id.* at 382.

An argument that employees have made with some regularity is that class action waivers and other representative action waivers effectively prevent them from vindicating their substantive statutory rights. After *Iskanian*, this argument must fail as to PAGA claims because the ''proxy'' plaintiffs do not have substantive PAGA rights. A plaintiff who is merely a ''proxy'' for the ''real party in interest'' (which *Iskanian* clearly says is the government) cannot forgo any ''substantive'' right because the ''proxy'' does not have a substantive right of his own to forgo. This is consistent with the California Supreme Court's prior holding that PAGA ''does not create property rights or any other substantive rights. Nor does it impose any legal obligations.'' *Amalgamated Transit Union v. Superior Court*, 46 Cal. 4th 993, 15 WH Cases2d 803, Cal. Super. Ct. 2009 ; *see also Radcliffe v. Lowe's HIW, Inc.*, C.D. Cal., 2:11-cv-02517, 6/30/11. (''A party may waive claims under the Private Attorney General Act because the Act does not create substantive statutory rights.''). Rather, PAGA is ''simply a procedural statute allowing an aggrieved employee to recover civil penalties—for Labor Code violations—that otherwise would be sought by state labor law enforcement agencies.'' *Amalgamated Transit*, 46 Cal. 4th at 1003.

Furthermore, the law is clear that the government itself is not bound by a private arbitration agreement, *see E.E.O.C. v. Waffle House, Inc.*, 534 U.S. 279 (2002), and thus the government cannot possibly be waiving any substantive law enforcement right it has by virtue of an employee signing an arbitration agreement that requires a PAGA claim to be arbitrated on an individual basis. *See also* Cal. Lab. Code § 98.3 (providing for state enforcement actions against employers on behalf of employees).

One corollary of the government not being bound by a private arbitration agreement is that an individual entering into a private arbitration agreement cannot be the government's agent or proxy *at the time* she signs the arbitration agreement (an individual cannot both be the government's agent and not be the government's agent at the same time as to the same subject matter, and we know from *Waffle House* that an individual is not the government's agent when signing a predispute arbitration agreement because the government is not bound by it).

Thus, an arbitration agreement's prospective waiver cannot harm the State because employees do not represent the State's interests until the dispute arises. Indeed, employees are not and cannot be ''proxies'' or ''agents'' of the State until they file a PAGA action. The mere signing of a private arbitration agreement by an individual who is not a State agent cannot and does not waive any government rights to pursue enforcement actions against employers. *See Waffle House*, 534 U.S. at 294. As *Iskanian* reiterates (citing *Arias*), neither the state nor any other ''aggrieved employee'' loses the ability to pursue a PAGA claim until a judgment is entered. *Iskanian*, 59 Cal. 4th at 380-81, 387. Consequently, one individual's voluntary agreement to bring any PAGA claim on an individual basis cannot deprive anyone else of any PAGA rights they may have.

Question No. 5: Does an Opt-Out Provision Entirely Avoid Iskanian's Holding? *Iskanian* held: ''we conclude that an arbitration agreement *requiring* an employee *as a condition of employment* to give up the right to bring representative PAGA actions in any forum is contrary to public policy.'' *Iskanian*, 59 Cal. 4th at 360 (emphases added). The *Iskanian* arbitration agreement was mandatory—there was no opt-out procedure. But what if an employee can opt out of the arbitration agreement entirely? In that case, the agreement would not be required, nor would it be a ''condition of employment.'' Because the *Iskanian* agreement was mandatory, *Iskanian* did not directly address this scenario.

Conclusion : The answers to these questions are forthcoming because they are being litigated actively in courts throughout California. Stay tuned.