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Client Alert Commentary

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A Win for Employers: US Supreme Court Rules Class Waivers Are Lawful

The Supreme Court clarified that employers who maintain or adopt arbitration agreements with class waivers may avoid class action wage and hour lawsuits, clearing the way for employers to reduce potential exposure.

The US Supreme Court has ruled[1] in *Epic Systems Corp. v. Lewis* that arbitration agreements in which employees waive their right to bring class or collective actions, and are limited to bringing their claims on an individual basis in arbitration, are enforceable. The ruling resolves recent confusion concerning the enforceability of such waivers.[2]

Justice Gorsuch delivered the highly anticipated decision on May 21, 2018, in which the Court ruled that the Federal Arbitration Act of 1925 (FAA) mandates that courts enforce the parties' class action waivers in arbitration agreements, and neither the FAA's "saving clause" nor the National Labor Relations Act of 1935 (NLRA) requires otherwise.

The decision resolves three pending circuit court cases[3] in which employees had entered into mandatory arbitration agreements containing class waivers. Despite their agreements to arbitrate employment-related disputes on an individual basis, the employees pursued their wage and hour claims under the Fair Labor Standards Act (FLSA) on a class action basis, arguing that class waivers are unlawful under Section 7 of NLRA.[4]

The Court noted that Section 7 of the NLRA, which protects employees' rights "'to self-organization, to form, join, or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection'"[5] primarily concerns employees' rights to bargain collectively.[6] The Court refused to infer that class and collective actions are the types of "concerted activities" Section 7 protects that cannot be waived by agreement.[7]

The Court ruled that disregarding the class waivers would run afoul of the FAA, which requires courts to enforce arbitration agreements as written, subject only to a saving clause that allows courts to invalidate arbitration agreements "'upon such grounds as exist at law or in equity for the revocation of any contract.'"[8] Such a saving clause, the Court ruled, is limited to defenses that apply to *any contracts*, *and not just arbitration contracts*, such as the defense of fraud, duress, or unconscionability,[9] and nothing in the NLRA suggests a clear and manifest intent from Congress to override the FAA for individual arbitration agreements containing class waivers.[10]

The ruling is a victory for employers who maintain mandatory arbitration agreements with class waivers, or who wish to adopt such a practice. The ruling renders pursuing FLSA (and similar state law claims) less attractive to employees and plaintiffs' attorneys if arbitration agreements containing class waivers are in place. This is because the claims will be less cost-effective to pursue as individual matters and less likely to yield significant damages than they would as class or collective actions.

Although the decision resolves the enforceability of arbitration agreements containing class waivers generally, employers should continue to be mindful of state laws that may undermine arbitration agreements, such as case law that applies generally to contracts. This includes case law that invalidates unconscionable contracts,[11] and state law claims in which the plaintiff acts on behalf of the state — such as under California's Private Attorneys General Act of 2004 (PAGA)[12] — which courts have held cannot be waived.[13]

Key Takeaways

- Employers with arbitration agreements containing class action waivers can rest a little easier knowing that a key obstacle to enforcement has been cleared.
    - Employers should consider reviewing their arbitration agreement form with counsel to minimize the risk that the agreement will be invalidated due to unconscionability or for other reasons.
- Employers without an arbitration agreement containing a class waiver should discuss the pros and cons of adopting one with counsel.
    - For many businesses, enforceability of a class waiver may mean that arbitration is more attractive than previously.
    - Employers should be mindful that arbitration is not a panacea, and, some cases may entail overlapping claims not subject to arbitration, such as PAGA claims.

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Endnotes

[1] The decision was split, 5-4. Justices Gorsuch, Roberts, Kennedy, Alito, and Thomas joined the majority, and Justices Ginsburg, Breyer, Sotomayor, and Kagan dissented.

[2] Previously, courts have routinely enforced employees' class waivers in arbitration agreements. In 2012, however, the National Labor Relations Board (NLRB) took the position that the National Labor Relations Act of 1935 (NLRA) nullifies the Federal Arbitration Act of 1925, which generally obligates courts to enforce the parties' arbitration agreements pursuant to their terms, in cases in which the arbitration agreements include a class waiver, after which some circuits have either agreed with the NLRB or deferred to the NLRB's interpretation of the NLRA under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).

[3] *Lewis v. Epic Sys. Corp.*, 823 F.3d 1147 (7th Cir. 2016), *cert. granted*, 137 S. Ct. 809 (2017); *Morris v. Ernst & Young LLP*, 834 F.3d 975 (9th Cir. 2016), *cert. granted*, 137 S. Ct. 809 (2017); *Murphy Oil USA, Inc. v. National Labor Relations Board*, 808 F.3d 1013 (5th Cir. 2015), *cert. granted*, 137 S. Ct. 809 (2017).

[4] *Epic Sys. Corp. v. Lewis*, No. 16-285, 2018 WL 2292444, at *9-13 (U.S. May 21, 2018).

[5] *Id.* at *9 (quoting 29 U.S.C. § 157).

[6] *Id.*

[7] *Id.* at *9-11.

[8] *Id.* at *6 (quoting 9 U.S.C. § 2).

[9] *Id.* at *6-7. The employees in the cases before the Court did not allege that their individual arbitration agreements were unenforceable as a matter of fraud, duress, or unconscionability, which does not include defenses based on alleged violation with other federal laws that apply to arbitration contracts only and not to any contracts generally, the Court clarified. *Id.*

[10] The Court also ruled that the NLRB is not entitled to deference under *Chevron*. Under *Chevron*, when interpreting an ambiguous statute, courts should defer to the agency that administers such statute. *See Chevron*, 467 U.S. at 841-44. *Chevron* deference does not apply in the circuit court cases before the Court because the NLRB has attempted to interpret not just the NLRA but both the NLRA and the FAA, and reconciliation of two potentially conflicting statutes is a matter for the courts. *Epic Sys. Corp.*, 2018 WL 2292444, at *13-14.

[11] *See, e.g., Armendariz v. Found. Health Psychcare Servs., Inc., 2*4 Cal. 4th 83 (2000) (applying unconscionability standards to invalidate mandatory pre-dispute employment arbitration agreement).

[12] Cal. Lab. Code § 2698.

[13] In *Iskanian v. CLS Transportation Los Angeles, LLC*, 59 Cal. 4th 348, 360 (2014), the California Supreme Court held that while a class action waiver was enforceable, the waiver could not extend to PAGA claims because the plaintiff in a PAGA action acts on behalf of the state in enforcing the law. In *Sakkab v. Luxottica Retail North America, Inc.*, 803 F.3d 425 (9th Cir. 2015), the Ninth Circuit Court of Appeals upheld the "*Iskanian* rule," holding that PAGA representative action waivers were unenforceable in any contract, not just arbitration agreements, and, therefore, did not violate the FAA. To date, the US Supreme Court has repeatedly refused review of the "*Iskanian* rule" regarding the arbitrability of PAGA claims.