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Labor and Employment and Senior Living and Long Term Care Law Update

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Don't Wait: Review Your Company's Arbitration Agreement Now

Many businesses ask their employees to agree to arbitration to resolve employment disputes because arbitration can be cheaper and faster than the court system. Arbitration can also be used as a shield to prevent the filing of class or collective actions brought on behalf of groups of employees. For this reason, many businesses include class action waivers in their arbitration agreements.

In 2012, the National Labor Relations Board (NLRB) ruled in the *D.R. Horton* case that class action waivers are unlawful if they prevent employees from filing class action claims in court or arbitration (see NLRB Strikes Down Arbitration Agreement Containing Class Action Waiver). Since then, most courts have disagreed with the NLRB, and have instead ruled that class action waivers are lawful, relying on the Federal Arbitration Act (FAA). While the U.S. Supreme Court has not yet ruled on this narrow issue, it has issued a series of recent decisions favoring arbitration agreements. But the legal landscape has now shifted for businesses operating in Alaska, Oregon and Washington, as well as the remaining states covered by the Ninth Circuit, Arizona, California, Hawaii, Idaho, Montana and Nevada.

On August 22, 2016, the Ninth Circuit Court of Appeals became the second circuit court to agree with the NLRB in a case known as *Morris v. Ernst & Young*. Given the split in the circuit courts, it seems likely that this issue will ultimately be decided by the U.S. Supreme Court. In the meantime, businesses operating in the Ninth Circuit should take this opportunity to review their arbitration agreements.

Overview of the Ninth Circuit's Decision

In *Morris v. Ernst & Young*, a three-judge panel ruled 2-to-1 that Ernst & Young's mandatory class action waiver violated the National Labor Relations Act (NLRA) because it forced employees to arbitrate work-related claims individually. Upon hire, Ernst & Young employees were asked to sign agreements that required them to: (1) pursue legal claims against Ernst & Young exclusively through arbitration; and (2) arbitrate only as individuals and in "separate proceedings." Agreement to arbitration was a mandatory condition of employment. Nonetheless, two Ernst & Young

employees brought a class and collective action in federal court, claiming they were denied overtime compensation. The employees argued that the contract violated Sections 7 and 8 of the NLRA. The trial court ordered the employees, and all others who felt aggrieved, to pursue individual arbitration claims, and dismissed the case. Upon appeal, the Ninth Circuit panel agreed with the employees that the class action waiver was not lawful.

Section 7 grants covered employees the substantive right to engage in "concerted activities for the purpose of…mutual aid or protection." Section 8 makes it "an unfair labor practice for an employer…to interfere with, restrain or coerce employees in the exercise" of their Section 7 rights. The Ernst & Young employees argued that, read together, Sections 7 and 8 of the NLRA prevent an employer from restricting its employees from acting in concert to improve the terms and conditions of their employment. Courts have long considered a class or collection action lawsuit that seeks to improve working conditions to be a "concerted activity" protected by the NLRA. The *Ernst & Young* majority also pointed out that the right to engage in concerted activities is a "substantive right," which cannot be waived in arbitration agreements.

The *Ernst & Young* majority ultimately concluded that employers cannot restrict concerted activities; class action waivers restrict a concerted activity; thus, class action waivers violate the NLRA. What makes this case difficult — and what has divided the circuits — is that the NLRA's ban on mandatory class action waivers conflicts with the Federal Arbitration Act. The FAA requires courts to enforce arbitration agreements according to their terms. But to enforce Ernst & Young's arbitration agreement, the Ninth Circuit would have to approve a class action waiver that arguably violates the NLRA.

The *Ernst & Young* majority joined the Seventh Circuit in finding that the NLRA and FAA do not actually conflict. The Ninth Circuit pointed to the FAA's "savings clause," which invalidates arbitration agreements that are otherwise illegal. Because the Ernst & Young class action waiver was illegal under the NLRA, the FAA's savings clause allowed the Court to nullify the waiver, even though to do so meant that the Court would not enforce the arbitration agreement according to its terms. In the majority's view, the whole point of the FAA's savings clause is to prevent conflict with other statutes.

The dissent joined the Second, Fifth and Eighth Circuits in concluding that courts can only override an arbitration agreement when there is a "contrary congressional command." In order for the NLRA to override the FAA's command to enforce arbitration agreements according to their terms, the dissent reasoned, the NLRA needed to expressly state that no arbitration clause shall be valid if it restricts employees' from acting in concert. Because no contrary congressional command exists, the dissent argued that the arbitration clause should be enforced as written. The dissent labeled the majority's ruling as "breathtaking in its scope and its error."

What Should Businesses Using Arbitration Agreements Do Now?

The case establishes bad law for businesses operating with the Ninth Circuit. It is possible that a full panel of Ninth Circuit judges will agree to hear the case and overturn the panel's decision, so it will be important to monitor this development. Given the ubiquity of class action waivers in arbitration agreements, as well as the widening circuit split on how to balance the NLRA and the FAA, the issue seems destined for Supreme Court review. The current makeup of the Court and the pending appointment make forecasts difficult. As of now, businesses in the Ninth Circuit should consider whether to revise their arbitration agreements.

The Ninth Circuit was clear that arbitration agreements in employment contracts are still valid. The court noted that arbitration is "encouraged by" the NLRA. What invalidated Ernst & Young's clause was not the arbitration provision, but the class action waiver. A contract that mandates employees to bring their claims in a judicial forum, but pursue them individually is likewise invalid under the NLRA. Under the Ninth Circuit's reasoning, as long as employees can pursue work-related claims collectively, employers can still include dispute forum provisions in their employment contracts.

The Ninth Circuit signaled that the main problem with Ernst & Young's class action waiver was its mandatory nature. Businesses may still be able to ask employees to sign class action waivers so long as the waiver is not a condition of employment. Some businesses have included provisions allowing employees to opt out of the arbitration agreement, which the Ninth Circuit panel seemed to approve. Businesses should review their arbitration agreements and consult with legal counsel to make informed decisions whether to modify their agreements.

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