Waiver of PAGA Action in Employment Arbitration Agreements Invalidated Despite AT&T v. Concepcion

Can California employers secure enforceable arbitration agreements from their employees that waive the right to pursue representative actions under the Labor Code Private Attorneys General Act (“PAGA”) in court? On July 12, 2011, the California Court of Appeal held in Brown v. Ralphs Grocery Co. that these waivers are not enforceable under California law. Focusing on what it believed to be the fundamental differences between class actions and PAGA representative actions, the court held California prohibits waivers of PAGA actions in a way that does not run afoul of the U.S. Supreme Court’s recent decision in AT&T Mobility LLC v. Concepcion, 131 S.Ct. 1740 (2011). (Click here for a discussion of the U.S. Supreme Court’s decision in AT&T Mobility LLC v. Concepcion.)

The court meanwhile declined to decide whether AT&T Mobility invalidates current California rules prohibiting class action waivers in employee-employer arbitration agreements.

Background

Terri Brown began working for Ralphs as a security guard in 2005. She agreed to Ralphs’ Mediation and Binding Arbitration Policy (“Arbitration Agreement”), which waived her right to have employment-related disputes arbitrated on “a class action basis,” “as a private attorney general,” or in a “representative” action brought on behalf of “other persons alleged to be similarly situated.” Just in case the point might otherwise be missed, the Arbitration Agreement also stated that “there are no class actions or Representative Actions permitted under this Arbitration Policy.”

Although she signed the Arbitration Agreement, Brown nevertheless filed a class action complaint against Ralphs, seeking recovery for various alleged violations of the California Labor Code and Unfair Competition Law, and recovery of civil penalties in a representative capacity under PAGA. Ralphs petitioned to compel arbitration under the Arbitration Agreement. Brown opposed the petition, arguing: (i) the class action waiver was unconscionable and therefore unenforceable; (ii) the representative action waiver also was unenforceable; and (iii) the presence of these two unconscionable waivers rendered the Arbitration Agreement unenforceable in its entirety.

The trial court agreed with Brown that both the class action and representative action waivers were unconscionable, thereby
rendering the entire Arbitration Agreement unenforceable.

After Ralphs appealed the denial of its petition to compel arbitration, the U.S. Supreme Court decided *AT&T Mobility*, holding the Federal Arbitration Act (FAA) preempted the California *Discovery Bank* rule prohibiting class action waivers in arbitration agreements.

**The Issues On Appeal**

The court reviewed the following issues:

1. Did Brown fulfill her evidentiary burden to establish the four factors required under *Gentry v. Superior Court*, 42 Cal.4th 443 (2007) in order to invalidate a class action waiver in an employment arbitration agreement?

2. In light of *AT&T Mobility*, does the FAA preempt state law that prohibits waivers of representative actions in arbitration agreements?

**The Court of Appeal’s Decision**

On the first issue, the court held that Brown failed to establish the following four Gentry factors: (i) modest size of potential individual recovery; (ii) potential for retaliation against members of the class; (iii) absent members of the class may not be informed about their rights; and (iv) other real world obstacles to the vindication of class members’ rights through individual arbitration. The court thus reversed the trial court’s ruling invalidating the class action waiver. The court did not reach the issue whether, under *AT&T Mobility*, the FAA preempts the rule in Gentry against enforcing waiver of class actions in employee-employer arbitration clauses.

On the second issue, the court held under *AT&T Mobility* the FAA does not preempt a California rule against waivers of representative actions in arbitration agreements. The court relied on what it believed were fundamental differences between class actions and representative actions, noting that a public right, such as that created under the PAGA, could not be waived if such a waiver is contrary to state law. The court then noted that a PAGA plaintiff “acts as the proxy or agent of state labor law enforcement agencies, representing the same legal right and interest as those agencies,” which contrasts “with the private individual right of a consumer to pursue class action remedies in court or arbitration.”

The court went on to conclude that permitting a waiver of a PAGA representative claim in arbitration would undermine PAGA, as a single-claimant arbitration action would not have the deterrent effect that the California Legislature intended when it enacted the PAGA.

Because the trial court had not considered whether the PAGA waiver provision, by itself, warranted non-enforcement of the entire arbitration agreement, the Court of Appeal remanded the matter to the trial court to exercise its discretion accordingly.

**What Brown Means For Employers**
By not reaching the issue of whether AT&T Mobility has nullified the effect of the Gentry rule against class action waivers in employment disputes, the Court of Appeal missed a chance to provide guidance on an issue that will certainly recur. Most employment law practitioners believe that AT&T Mobility clearly does overturn Gentry. However, they also recognize the anti-arbitration sentiment that appears to be present in the California judicial system, especially with respect to claims that California law is preempted by federal law.

Where the Brown decision does provide guidance, it invites plaintiffs seeking to avoid arbitration to rely on PAGA representative actions, which can be brought without asserting the PAGA claim as a class action. The prospect that a plaintiff can bring a representative action in an arbitral context, which lacks the due process guarantees that an employer would have in court, may be a factor dissuading some employers from implementing arbitration agreements. However, many employment law practitioners believe that the Brown case was wrongly decided.

By: Fred Sanderson and Brian Wong

Fred Sanderson is a partner in the Sacramento office and Brian Wong is an associate in Seyfarth’s San Francisco office. If you would like further information please contact your Seyfarth Shaw LLP attorney, Fred Sanderson at asanderson@seyfarth.com or Brian Wong at rwong@seyfarth.com.