



Management Alert

California Supreme Court Holds That Mandatory Employment Arbitration Agreements Do Not Preempt Labor Commissioner Claims

On February 24, 2011, in *Sonic-Calabasa A, Inc. v. Moreno*, the California Supreme Court issued an important ruling regarding the right of employees to have wage claims adjudicated before the California Labor Commissioner in so-called Berman hearings under Labor Code section 98. In a 4-3 decision authored by Justice Moreno (joined by Justices George, Kennard, and Werdegar), the Supreme Court held that a provision of a mandatory employment arbitration agreement requiring waiver of the right to a Berman hearing before the Labor Commissioner was both “contrary to public policy and unconscionable” and that California courts would not enforce such an agreement, despite the employer’s argument that the Federal Arbitration Act requires enforcement. The Supreme Court also held, however, that arbitration may be enforced after a Berman hearing if a party appeals the Labor Commissioner’s decision to the California Superior Court.

Case Background

The Plaintiff, Frank Moreno, worked for Sonic-Calabasas A, Inc. (“Sonic”), an auto dealership. Upon being hired by Sonic, Moreno signed an arbitration agreement requiring him to submit any disputes arising out of his employment to “binding arbitration under the Federal Arbitration Act (“FAA”), in conformity with the procedures of the California Arbitration Act.” The agreement covered “all disputes that may arise out of the employment context,” but specifically carved out exceptions for claims under the National Labor Relations Act and the California Workers’ Compensation Act, as well as claims brought before the Employment Development Department. The agreement also permitted Moreno to file and pursue administrative charges before the California Department of Fair Employment and Housing or the U.S. Equal Employment Opportunity Commission. The agreement was silent as to claims before the California Labor Commissioner.

Moreno resigned from Sonic and filed a Labor Commissioner claim for unpaid vacation pay, seeking resolution of his claim in a Berman hearing. Sonic petitioned the Superior Court for an order compelling arbitration of Moreno’s claim under the parties’ arbitration agreement. The Labor Commissioner intervened and opposed Sonic’s petition. The Superior Court denied the petition, allowing a Berman hearing to proceed, and Sonic appealed.

The Court of Appeal reversed, holding that the arbitration waiver of the Berman hearing was consistent with public policy. Moreno sought review by the Supreme Court, which reversed the Court of Appeal, holding that the right to a Berman hearing could not be waived.

The Supreme Court's Reasoning

In reaching this conclusion, the Supreme Court concluded that the Legislature has given employees, in the form of Berman hearings, an “unwaivable statutory right” to certain procedural advantages, including mediation, informal discovery, a one-way attorney fee provision, and the requirement that the employer must post bond if it disagrees with the result of the Berman hearing and appeals it in Superior Court. Because employees would lose these advantages if compelled to arbitrate wage claims they otherwise could bring in a Berman hearing, upholding the waiver of Berman hearings “would seriously undermine the efficacy of the Berman hearing statutes and hence thwart the public purpose behind the statutes.” Consequently, the Court held the Berman waiver provision unenforceable as inconsistent with public policy.

The Court also concluded that the Berman waiver was unenforceable on an independent ground: it was unconscionable, the Court said, because the Berman waiver stripped the employee of the statutory advantages the Legislature chose to bestow on employees seeking redress before the Labor Commissioner. According to the Court, “Requiring the employees to forgo these protections as a condition of employment can only benefit the employer at the expense of the employee.” These considerations rendered the waiver “markedly one-sided” and thus unconscionable.

Sonic contended that the FAA preempted the Court's holding, but the Court disagreed. The Court distinguished a U.S. Supreme Court decision in *Preston v. Ferrer* holding that the FAA preempts a California statute giving the Labor Commissioner exclusive jurisdiction over Talent Agencies Act claims even in the face of an arbitration agreement. The Court found this case different because: (1) *Preston* involved a challenge to the arbitration agreement as a whole and not a specific provision of the agreement; and (2) there were “fundamental differences between the two statutory regimes at issue,” specifically the special procedural considerations that the Legislature built into the statutes governing Berman hearings.

In dissent, Justice Chin (joined by Justices Baxter and Corrigan) argued that the arbitration agreement presented no public policy violation because the test is not whether the arbitration agreement will deprive the parties of some special advantages (since all arbitration agreements have that result), but whether the arbitration agreement permits an employee to vindicate his or her claims. Because Sonic's arbitration agreement provided the employee with that opportunity, the dissent argued that the agreement did not violate public policy. The dissent also noted that there is no express language in the Labor Code suggesting that Berman hearings constitute a non-waivable statutory right.

Nor was the arbitration agreement unconscionable, the dissent argued, because a Berman waiver is part of an overall arbitration agreement by which both parties gain advantages. When “[v]iewed from a broader perspective,” the dissent found that the arbitration agreement was not unfairly one-sided.

The dissent also disagreed with the majority's conclusion regarding FAA preemption. Questioning the majority's effort to distinguish *Preston*, the dissent argued that the FAA requires enforcement of an arbitration agreement even against a claim of primary adjudicative jurisdiction by an administrative agency. Moreover, the dissent argued, distinguishing *Preston* on the grounds that it involved a challenge to the contract as a whole instead of a challenge to just a portion of the contract was “irrelevant” since that circumstance was material only to the threshold determination of whether the court or the arbitrator makes a decision, not the ultimate issue of FAA preemption. Taking issue with the majority's logic that there was no FAA

preemption because of the special procedural advantages the Legislature attached to Berman hearings, the dissent also noted that the U.S. Supreme Court had expressly held that “the FAA’s preemptive policy requiring enforcement of arbitration agreements according to their terms applies ‘notwithstanding any substantive *or procedural* policies to the contrary.’ ” The fact that the Legislature attached special procedural advantages to Berman hearing statutes that may benefit employees was ultimately inconsequential to the question of whether FAA preemption applies.

What This Case Means for Employers

This decision is yet another example of California courts’ aversion to arbitration in the employment context. Employers with mandatory employment arbitration agreements should take note of this decision and consider how best to defend Labor Commissioner claims when arbitration may be an option.

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