Viking Cruises to a Win for California Employers: Supreme Court Closes PAGA's Backdoor to Avoid Arbitration Agreements (For Now)

Insights
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Employers can enforce arbitration agreements in California to the extent they require an employee to arbitrate individual claims under the state's Private Attorneys General Act (PAGA), according to an 8 to 1 SCOTUS ruling that was issued today. The Court also held that once the employee's individual claims under PAGA are compelled to arbitration, the employee would not have standing to bring a representative claim under PAGA on behalf of other aggrieved employees. However, the Court left open the possibility that the California Legislature could revise PAGA to allow an employee to bring representative claims in Court, even if the employee does not share any claims with the other employees they seek to represent. Employers have been clamoring for this ruling, as this decision marks the end of an eight-year battle to treat agreements to arbitrate representative actions in the same manner as waivers of class and collective actions. You should be prepared to make immediate adjustments to your alternative dispute resolution agreements, assess any existing representative litigation to capitalize on this hard-fought relief from PAGA's abuses, and prepare for potential legislative changes to PAGA. Here's what you need to know about the ruling.

Key Takeaways

In two prior cases, the SCOTUS has held that the Federal Arbitration Act (FAA) preempted a state law deeming class action waivers unenforceable and reaffirmed that the FAA requires courts to enforce collective action waivers in arbitration agreements. Notably, however, the California Supreme Court held in *Iskanian v. CLS Transportation Los Angeles, LLC* that arbitration agreements containing PAGA representative action waivers were against public policy and unenforceable and that the FAA did not preempt this rule.

Under PAGA, employees can sue their employers on behalf of themselves for alleged California Labor Code violations they suffered and on behalf other employees for distinct violations. PAGA deputizes employees to recover civil penalties on the state's behalf, with seventy-five percent of the total penalties recovered remitted to the state and 25 percent to employees.

The SCOTUS delivered some relief to employers in its decision in *Viking River Cruises, Inc. v. Angie Moriana*. The ruling has four main holdings for you to digest:

- *Iskanian*'s rule that PAGA actions cannot be divided into individual and non-individual claims is preempted, so Viking was entitled to compel arbitration of Moriana's individual claim.
- PAGA provides no mechanism for a court to adjudicate non-individual PAGA claims once an individual claim has been committed to a separate proceeding.
- Under PAGA's standing requirement, a plaintiff has standing to maintain non-individual PAGA claims only if her individual claim in that action is maintained. As a result, Moriana would lack statutory standing to maintain her non-individual claims in court and the lower court should have dismissed those claims.
- *Iskanian*'s prohibition on wholesale waivers of PAGA claims is not preempted by the FAA.

History Leading Up to Viking Cruises Setting Sail: How the Backdoor Was Created

The Supreme Court's rulings in *AT&T Mobility, LLC v. Concepcion* (2011) and *Epic Systems Corp. v. Lewis* (2018) made clear that when parties agree to resolve their disputes via individual arbitration such agreements are fully enforceable under the FAA. Courts may not disregard bilateral arbitration agreements or "reshape traditional individualized arbitration" by applying rules that demand class-wide or collective adjudication of certain claims. Both decisions proclaimed that the FAA requires courts to rigorously enforce arbitration agreements according to their terms – including terms for individualized proceedings – and preempts state law rules that interfere with such enforcement. First *Concepcion* held that the FAA preempted a state law deeming class action waivers unenforceable, then *Epic Systems* reaffirmed that the FAA requires courts to enforce collective action waivers in arbitration agreements.

However, the California Supreme Court's intervening decision in *Iskanian* in 2014 held that arbitration agreements containing PAGA representative action waivers were unenforceable and against public policy, and the FAA did not preempt this rule. The California Supreme Court reasoned in *Iskanian* that PAGA actions are different than the class actions in *Concepcion* and outside the purview of the FAA because PAGA actions are disputes between an employer and the state, not private disputes. Consequently, opponents argued that *Iskanian* created a backdoor whereby employees could avoid their arbitration agreements merely by asserting a PAGA claim.

Although *Epic* made clear that *Concepcion* extends beyond class-actions, the SCOTUS has repeatedly denied petitions seeking review of whether the FAA preempts *Iskanian*. With most of those petitions pre-dating *Epic*, the Court agreed to reconsider the California Supreme Court's rule through the uncomplicated vehicle presented by Angie Moriana.

Before commencing her employment as a sales representative for Viking River Cruises, Inc., Angie Moriana signed an agreement with the company agreeing to resolve all future employment-related disputes in bilateral arbitration and waiving the right to bring any such dispute as a class, representative or private attorney general action. The agreement expressly allowed Moriana to opt-

out of the waivers, but she chose not to. After her employment ended, Moriana filed a representative action against Viking asserting single cause of action under PAGA.

Based on Moriana's arbitration agreement, Viking moved to compel individualized arbitration. The trial court denied the motion, holding that Moriana's representative PAGA claim could not be compelled to arbitration under California law. The Court of Appeal affirmed, determining that *Iskanian* "remains good law" notwithstanding *Epic* because the collective action in *Epic* fundamentally differs from a PAGA claim in which the real party in interest is the state. Further, the Court of Appeal explained that because all PAGA claims are "representative" in that they are brought on behalf the state, Moriana alleged no personal claim for compensation that could be individually arbitrated. The California Supreme Court denied Viking's petition for review, and Viking requested review by the Supreme Court.

Supreme Court: FAA Preempts Conflicting State Rules

The framework of *Viking River*'s arbitration agreement was not undisputed. Rather, the Court's decision turned on the application of *Concepcion* and *Epic*. Accordingly, Viking argued that the Court's jurisprudence and Congress's intent in enacting the FAA demanded that the arbitration agreement at issue be enforced according to the terms Moriana agreed to, including a representative action waiver, as any arguments for a contrary application had been foreclosed by the Court's prior rulings. On the other side, Moriana argued that PAGA actions belong to the state and seek public rather than private relief. Therefore, she claimed, they cannot be waived by an individual, nor are they subject to the FAA's purview.

In its ruling, the SCOTUS vacated the California Court of Appeals' decision and remanded the case for further proceedings. In so doing, the Court repealed *Iskanian*'s anti-waiver rule for PAGA claims "insofar as it precludes division of PAGA actions into individual and non-individual claims through an agreement to arbitrate." The Court held the following:

- The arbitration agreement at issue was invalid to the extent it contained a "wholesale waiver of PAGA claims."
- Because the agreement's severability clause provided that any invalid portion of the waiver be severed and any remaining valid portion of the waiver must still be enforced, Viking is entitled to enforce the agreement to compel arbitration of Moriana's individual PAGA claim – meaning the claim she actually suffered.
- PAGA's standing requirement permits a plaintiff to maintain non-individual PAGA claims only if they also maintain an individual claim in the same action. Furthermore, PAGA's statutory scheme currently provides no mechanism for a court to adjudicate representative PAGA claims if an individual claim has been severed to a separate proceeding. Therefore, Moriana lacks statutory standing to continue to maintain her non-individual claims in court and those claims must be dismissed.

The Court clarified that PAGA actions are "representative" in two ways: (1) when they are brought by employees acting as agents of the state; and (2) when they are based on violations of the California Labor Code sustained by other employees. Thus, the Court found that *Iskanian* created two rules. First, *Iskanian*'s "principal rule" prohibits agreements that prevent parties from waiving their "representative standing" to bring PAGA claims in court or arbitration. Second, in *Iskanian*, the California Supreme Court adopted a rule invalidating agreements to separately litigate or arbitrate "individual PAGA claims for Labor Code violations that an employee suffered."

With respect to the former, the SCOTUS reaffirmed that – consistent with its prior decisions concerning class or collective-action waivers – a state law is inconsistent with the FAA if it requires parties to choose between arbitrating disputes using class procedures they did not consent to and that are inconsistent with arbitration's traditional forum or forego arbitration altogether. Based on that, Viking argued that *Iskanian*'s anti-waiver rule runs afoul of the FAA because PAGA actions are intrinsically representational and *Iskanian* requires the parties to choose between class arbitration or relinquish arbitration entirely. The Court disagreed, holding that nothing in the FAA or the Court's prior decisions establish a categorical rule mandating the enforcement of waivers of representative capacity. Further, the Court stated "single-agent, single-principal suits" are bilateral, even if not in the traditional sense of only two parties arbitrating exclusively in their individual capacities. Accordingly, there was no conflict between the FAA and *Iskanian*'s anti-waiver rule.

Nevertheless, the Court found there is a conflict between the FAA and PAGA's procedural structure. In a sharp deviation from how California has characterized PAGA actions to date, the SCOTUS found that PAGA claims are "individual" when premised on California Labor Code violations sustained by the plaintiff and "representative" when violations arise out of circumstances with other employees. Because PAGA permits a plaintiff to bring claims for violations she did not personally suffer, *Iskanian*'s secondary rule permits parties to "superadd new claims to the proceeding, regardless of whether the agreement between them committed those claims to arbitration," and defeats the "ability of parties to control which claims are subject to arbitration." *Iskanian*'s "indivisibility rule" thus coerces parties to opt for court and avoid their contractual agreement arbitrate individual claims. The SCOTUS held this result is incompatible with the FAA and requires reversal.

The Battle is Won, but the War is Not Over

While this ruling provides a positive answer for employers about the validity of PAGA waivers in arbitration agreements, it creates several uncertainties. First, the Court provided an entirely new mechanism to split PAGA claims into individual and non-individual claims. It remains to be seen how an "individual" PAGA claim will be litigated for California Labor Code violations that the plaintiff personally suffered.

Second, Justice Sotomayor's concurring opinion all but directs the California Legislature to modify the scope of statutory standing under PAGA. Under the current statutory scheme, Moriana's non-individual claims require dismissal because PAGA provides no mechanism for a court to adjudicate

such claims once the individual PAGA claim or claims are separated. We will have to see if the California Legislature quickly proposes an amendment to PAGA to fashion a mechanism for representative claims to survive in a judicial forum even when the individual claim is relegated to a separate proceeding.

In order for any PAGA "fix" to go into immediate effect, the California Legislature would need to pass such a measure by a 2/3 majority in both the Assembly and the Senate to send an emergency measure to the governor for signature. That's not entirely unlikely given the current makeup of the Legislature. Assuming such an amendment is passed, employers may be faced with addressing individual and non-individual actions in multiple forums simultaneously.

Viking provides one certain result: Courts will soon be inundated with defendants in active representative lawsuits filing motions to compel arbitration based on plaintiffs' agreement to individually arbitrate their PAGA claims. Even if the applicable arbitration agreements contain representative action waivers – provided there is a severability clause similar to the one in Moriana's agreement – employers may have success in compelling employees' PAGA claims for labor code violations they personally suffered and dismissing non-individual PAGA claims for violations suffered by others.

Employers may rejoice in this ruling to the extent it permits enforcement of arbitration agreements with respect to individual PAGA claims. The good news for employers is that *Viking* limits the scope of PAGA actions against them to claims with potentially modest penalties meant to correct mistakes, rather than claims with astronomical penalties that would jeopardize the entire business at the hand of a single employee and their lawyer.

You may need to revise your arbitration agreements to the extent they contain wholesale waivers of representative actions without severability clauses and prepare for the changing landscape of existing representational litigation. You should also prepare for potential legislative action to provide a PAGA plaintiff with standing to assert non-individual claims when their individual claims are ordered to arbitration.

We will continue to monitor developments in this area, so make sure you are subscribed to Fisher Phillips' Insight System to get the most up-to-date information. If you have questions about PAGA litigation and arbitration agreements, please contact your Fisher Phillips attorney, the authors of this alert, or any attorney in our California offices.

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