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Client Alert

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California Supreme Court Severely Limits Use of Class Waivers in Arbitration Agreements

In an important victory for employees, a closely divided California Supreme Court has held that class arbitration waivers in employment arbitration agreements may not be enforced where "the prohibition of classwide relief would undermine the vindication of the employees' unwaivable statutory rights and would pose a serious obstacle to the enforcement of the state's overtime laws." *Gentry v. Superior Court*, No. S141502, 2007 WL 2445122, at *1 (Cal. Aug. 30, 2007). Although the Court stated that this may invalidate only *some* waivers, its holding that such waivers are unenforceable whenever a court determines "that class arbitration would be a significantly more effective way of vindicating the rights of affected employees than individual arbitration," *id.*, may, as a practical matter, be the death knell for class waivers insofar as wage-hour claims are concerned.

Factual Background

Robert Gentry was hired by Circuit City in 1995. At that time, he received a packet that included an "Associate Issue Resolution Package" and a copy of Circuit City's "Dispute Resolution Rules and Procedures," pursuant to which employees were afforded various options, including arbitration, for resolving employment-related disputes. The arbitration procedure included a class arbitration waiver. The packet also contained a form that advised Gentry that he had 30 days to consider the agreement, that he should contact the company with any questions, and that he could consult with an attorney if he wished. Gentry was advised that he could opt out of the arbitration program, without penalty, by mailing the appropriate form to Circuit City within 30 days. Gentry did not do so.

Later, after his employment with Circuit City had ended, Gentry filed a class-action suit in court seeking overtime wages allegedly due both to himself and to other employees. The trial court granted Circuit City's motion to compel arbitration and ordered Gentry to arbitrate his claims on an individual basis. The Court of Appeal agreed, but the Supreme Court, dividing 4-3, reversed.

The Majority's Reasoning

The majority emphasized that Gentry's claims to overtime were based on rights "conferred by . . . statute [and] are unwaivable." *Id.* at *4. As the Court had previously held, "'arbitration cannot be misused to accomplish a de facto waiver of these rights.'" *Id.* at *5 (quoting *Little v. Auto Stiegler, Inc.*, 29 Cal. 4th 1064, 1079 (2003)), and it concluded "that under *some* circumstances," a class waiver would lead to such a de facto waiver. *Id.* at *6 (emphasis added).

The majority wrote that to make such a determination, a trial court must consider (1) the modest size of the potential individual recovery, (2) the potential for retaliation against members of the class, (3) the fact that absent class members may be ill informed about their rights, and (4) "other real world obstacles to the vindication of class members' right[s] to overtime pay through individual arbitration." *Id.* at *11. If the trial court "concludes, based on these factors, that a class arbitration is likely to be a significantly more effective practical means of vindicating the rights of the affected employees than individual litigation or arbitration, and finds that the disallowance of the class action will likely lead to a less comprehensive enforcement of overtime laws for the employees affected . . . it *must* invalidate the class arbitration waiver . . . . " *Id.* at *11 (emphasis added). This inquiry, wrote the majority, is similar to the one that a trial court already makes to determine whether class actions are appropriate. The majority wrote that it did "not foreclose the possibility that there may be circumstances under which individual arbitrations may satisfactorily address the overtime claims of a class of similarly aggrieved employees . . . [b]ut class arbitration

waivers cannot . . . be used to weaken or undermine the private enforcement of overtime pay legislation by placing formidable practical obstacles in the way of employees' prosecution of those claims." *Id.* at *11.

The case, ultimately, is to be remanded to the trial court, which is to determine whether "class arbitration would be a significantly more effective means than individual arbitration actions of vindicating the right to overtime pay of the group of employees whose rights to such pay have been allegedly violated . . . ." *Id.* at *12. If the trial court invalidates the waiver, "then the parties may proceed to class arbitration or, if the parties wish, have the matter brought in court . . . unless the trial court invalidates the arbitration agreement altogether" as unconscionable. *Id.* The majority observed, however, that if the trial court invalidates the wavier, the issue of unconscionablity might become moot, because it was unclear if, at that point, the employee would continue to resist arbitration or whether the employer would continue to seek it.

What Does It Mean for Employers?

As a practical matter, the almost certain import of *Gentry* is that class action waivers in arbitration agreements are unlikely to be enforced in wage-hour suits. As the dissent argued, a holding that a trial court must find such a waiver invalid in any circumstance in which it would find a class action appropriate in a wage-hour suit means that "[f]or all practical purposes . . . such agreements are forbidden, and meaningless, in this context." *Id.* at *20 (Baxter, J., dissenting). And the majority's assertion that its ruling was limited to cases where systematic denial of overtime pay to a class of employees was alleged was illusory, as "[s]uch assertions would appear, by necessity, in any complaint seeking to litigate overtime-pay claims in a class proceeding." *Id.* at *23 n.2.

In fact, the bar that the majority has raised for the enforcement of such a waiver is a high one. Moreover, it is unclear what evidence an employer will be required to present to the trial court to sustain its burden. All that can now reasonably be predicted is that proceedings on the enforcement of arbitration agreements that contain such waivers likely will be complicated, protracted and costly.

Gentry also reaffirms the care that California employers must take in drafting arbitration agreements, and that agreements that do not provide employees with all the same remedies and virtually all the same procedural rights as are available in a court proceeding are vulnerable to attack. Employers who have or who are contemplating such agreements should carefully review them and carefully consider the wisdom of any class waivers.

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