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CLASS AND COLLECTIVE ACTIONS

The use and enforceability of class action waivers in arbitration agreements in the United States

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INTRODUCTION

This article examines the use of class action waivers as a means of reducing the risk and expense associated with defending class and collective actions in the US. Class actions can be very time-consuming and expensive to defend, even when a claim lacks merit, and can present potentially catastrophic damages. The use of class actions has been a potent tool in litigation, and its abuse has resulted in the enactment of legislation specifically designed to restrict class action abuse, such as the Class Action Fairness Act 2005 (CAFA).

Nearly two decades ago, to decrease class action risk, some businesses started to include class action waivers within the arbitration provisions of consumer contracts and in stand-alone arbitration agreements with employees. Although some courts were initially hostile to class action waivers and refused to enforce them, over the years, and following some recent decisions from the US Supreme Court, class action waivers in arbitration agreements are increasingly being enforced and have become an effective means of reducing class action risk.

However, although the courts are now much more likely to enforce class action waivers, potential obstacles remain, for example:

- The courts continue to scrutinise class action waivers and may invalidate such provisions under contract formation and enforcement principles. Federal legislative efforts have, so far, unsuccessfully, targeted the use of class action waivers in consumer contracts.
- States have begun enacting laws and regulations purporting to prohibit employers from requiring their employees to sign arbitration agreements or arbitrate certain types of claims (such as discrimination).

We expect continued, if not increased, focus on class action waivers by the courts and government agencies in 2020.

This article therefore discusses the enforcement of class action waivers, identifies trends and particular areas of concern, and discusses the continuing uncertainty and other special issues related to the use of class action waivers in the context of employment.

FEDERAL ARBITRATION ACT

The cornerstone of class action waivers is their inclusion within an agreement to arbitrate. Arbitration clauses are now commonly found in:

- Contracts to purchase goods or services.
- Customer account agreements.
- Employee agreements.

The arbitration clause specifies the types of claims that must be arbitrated (ranging from narrow issues or claims to "any and all" claims or disputes between the parties).

By including a class action waiver in an arbitration clause, the Federal Arbitration Act (*9 USC §§ 1-16*) (FAA) is invoked. The FAA provides the legislative framework in the US for enforcing arbitration agreements, as well as for enforcing arbitral awards. The FAA was enacted to ensure that arbitration agreements were "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract" (*9 USC § 2*). Under the FAA, if an asserted claim falls within the parties' arbitration agreement, either party can ask the court to compel the other to resolve the claim in arbitration (*9 USC § 4*) and stay (or sometimes dismiss) the lawsuit pending the outcome of the arbitration (*9 USC § 3*). Provided the parties' relationship "involves" interstate commerce (which is construed broadly in favour of such a finding), the FAA applies regardless of whether the lawsuit is filed in a state or federal court (*9 USC § 1-2*).

A critical factor in successfully enforcing class action waivers is the pro-arbitration policy embodied in the FAA. This policy is routinely cited by courts when rejecting challenges to class action waivers contained in arbitration clauses and was emphasised in the Supreme Court case of *Moses H Cone Mem'l Hosp v Mercury Constr. Corp, 460 US 1, 24-27 (1983)*. In this case, the Court stated that the FAA is a "congressional declaration of a liberal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary", and further, that "as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." The policy was reiterated in *Southland Corp v Keating, 465 US 1, 10, 14 (1984)*, where the Supreme Court emphasised that the FAA represents a broad "national policy favoring arbitration", which was enacted to overcome "the old [judicial] hostility toward arbitration" and to address "the failure of state arbitration statutes to mandate enforcement of arbitration agreements" (*see also New Prime Inc v Oliveira, 139 S Ct 532, 543 (2019); Nitro-Lift Techs, LLC v Howard, 568 US 17, 20 (2012)*). Based on these decisions, numerous courts have enforced class action waivers within arbitration clauses by relying heavily on the Supreme Court's guidance that any doubts about whether an arbitration clause will be upheld should be resolved in favour of requiring arbitration.

Importantly, the FAA pre-empts state laws that are inconsistent with the FAA. Therefore, state laws or rules purporting to limit or prohibit arbitration will generally be rejected as inconsistent with the FAA. This issue was emphasised by the Supreme Court in *AT&T Mobility LLC v Concepcion, 563 US 333, 341-344, 351 (2011)*, where the Court invoked the supremacy of the FAA when rejecting decisions of the California state court, which held that class action waivers were unconscionable in certain types of consumer contracts (*see below, Rejection of unconscionability challenges and removal of obstacles*). The Supreme Court found that although

"unconscionability" (that is, a defence to contract formation based on principles of unfairness (*see below, Initial refusal to enforce class action waivers*)) is a ground that "exist[s] at law or in equity for the revocation of any contract", states cannot circumvent the FAA's mandate to enforce arbitration agreements, even when such laws are "desirable for unrelated reasons" (*see also Kindred Nursing Centers Ltd P'ship v Clark, 137 S Ct 1421, 1426-1428 (2017)*).

CONSUMER CONTRACTS

This section discusses the enforceability of class action waivers in consumer contracts.

Initial refusal to enforce class action waivers

Despite the background described above, many of the lower US courts initially refused to enforce arbitration agreements that contained class action waivers based on a number of challenges. The most common and successful challenge to class action waivers was based on contractual unconscionability. These unconscionability challenges focused on both:

- Procedural unconscionability (that is, the manner in which the contract was formed).
- Substantive unconscionability (that is, the assertion that the terms of the contract itself were so unfair as to render the contract unenforceable).

The success of these challenges culminated in California's "Discover Bank Rule", following a California Supreme Court decision striking down a class action waiver (*Discover Bank v Superior Court, 113 P 3d 1100 (Cal 2005)*). Under this rule, the courts in California could refuse to enforce class action waivers when all the following grounds of contractual unconscionability were applicable:

- When the class action waiver was included in a non-negotiable consumer contract of adhesion.
- When the likely claims would involve a small amount of damages.
- When the claims alleged a scheme to cheat consumers.

Based on this rule, it became virtually impossible to enforce class action waivers in California. Furthermore, although the California decisions drew the most attention, a number of other state and federal courts similarly refused to enforce class action waivers, including courts in Alabama, Florida, Illinois, Michigan, New Jersey, Tennessee, Washington, and West Virginia.

Aside from unconscionability challenges, arbitration clauses that contained a class action waiver were attacked on a number of other grounds, including (among others):

- Lack of mutuality (the consumer was required to arbitrate disputes but not the business).
- Limitations on damages (such as excluding punitive or statutory damages).
- Selection of a distant arbitral venue.
- Lack of clauses relating to the allocation of costs.

Either as an independent basis for invalidating the arbitration clause, or in tandem with an unconscionability challenge, these issues further increased the complexity and uncertainty surrounding the enforcement of consumer arbitration clauses and the corresponding class action waivers.

Rejection of unconscionability challenges and removal of obstacles

On 27 April 2011, the Supreme Court issued a landmark decision by ruling that the FAA pre-empted California's Discover Bank Rule (*AT&T Mobility LLC v Concepcion*). Specifically, the Court held that because the California rule of law "stands as an obstacle to the accomplishment and execution of the full purposes of objectives" of the FAA, it was pre-empted by the FAA. The Court started its analysis by emphasising the FAA's liberal policy favouring arbitration. The Court went on to note that "arbitration agreements [are] on equal footing with other contracts, and [must be] enforce[d] according to their terms". The Court recognised that contracts of adhesion were commonplace, but rejected those as the basis for striking-out class action waivers in consumer arbitration clauses. Accordingly, the Court upheld the arbitration provision (including its class action waiver) as written.

A key point to take away from the *Concepcion* decision is that, since arbitration agreements are on equal footing with other contracts, the courts cannot apply greater scrutiny to arbitration agreements than they would apply to any other contract. In other words, special rules cannot be created (either by legislatures or courts) that target or otherwise place more onerous requirements on arbitration agreements. In this case, because the Discover Bank Rule violated these principles (its restrictions applied only to arbitration contracts), the Supreme Court rejected it.

The Supreme Court issued another key arbitration decision two years later in *American Express Co v Italian Colors Restaurant, 133 S Ct 2304 (2013)*, where a restaurant owner alleged that American Express violated anti-trust laws by using its monopoly power to force merchants to agree to a form contract. In challenging the contract's class action waiver, the claimant argued that the cost of pursuing an individual arbitration for a federal anti-trust claim exceeded the potential individual recovery for such claims. The Court rejected the claimant's argument and upheld the class action waiver. In doing so, the Court reasoned that, while enforcing the waiver could, as a practical matter, bar "effective vindication"" of a federal statutory claim, this was permissible under the FAA, provided the arbitration clause did not prospectively waive a substantive statutory right.

Class action waivers after Concepcion

After the Supreme Court's ground-breaking decision in *Concepcion*, numerous federal and state courts upheld class action waivers in consumer arbitration clauses in the face of unconscionability challenges. Therefore, much of the uncertainty and potential expense in enforcing class action waivers was eliminated.

However, California still remains a battleground state on the issue. While many observers believed the *Concepcion* decision ended the state's historical hostility to class action waivers, the California Court of Appeals issued a decision invoking the Discover Bank Rule which refused to enforce a class action waiver, based on the theory that when the case was originally filed in the trial court, the Discover Bank Rule had not yet been overturned. However, the Supreme Court promptly and emphatically rejected this approach, and in doing so further embraced class action waivers: "[T]he [FAA] allows parties to an arbitration contract considerable latitude to choose what law governs some or all of its provisions, including the law governing enforceability of a class-arbitration waiver" (*DIRECTV, Inc v Imburgia, 136 S Ct 463 (2015)*).

While the *Imburgia* decision reinforces the view that class action waivers are not per se invalid and can be enforced, one area of continued frustration for businesses operating in California is the ability for claimants to assert representative claims under a variety of statutes, including California's Private Attorneys General Act (PAGA). These representative claims include (among other things) claims under section 17200 of California's Business and Professions Code, which prohibits unlawful, unfair, or fraudulent business acts or practices, and which has resulted in much litigation against business. The California courts have generally refused to force these types of lawsuits into individual (non-class) arbitrations, including in the employment realm. For example, see *Compare Correia v NB Baker Elec, Inc, 32 Cal Rptr 3d 177, 191-92* (*Ca Ct App 2019*) (holding that an employee cannot be compelled to pursue a PAGA representative action in arbitration ""based on an employee's predispute arbitration agreement absent some evidence that the state consented to the waiver of the right to bring the PAGA claim in court"), with *Schwendeman v Health Carousel, LLC, 2019 WL 6173163, at 7-9* (*ND Cal Nov 20, 2019*) (disagreeing with *Correia* and granting motion to compel arbitration of PAGA claim).

Even outside of California, some courts have invalidated class action waivers after *Concepcion*, such as in *Brewer v Missouri Title Loans, 364 S W 3d 486 (Mo 2012)*. In *Brewer*, the court focused not on whether the class action waiver itself was unconscionable, but rather, on whether the entire arbitration agreement was unconscionable. This approach is allowed under *Concepcion* and under the FAA's savings clause, which allows state courts to apply state law defences to the issue of contract formation. The Missouri Supreme Court concluded that the arbitration agreement (and its class action waiver) was indeed unenforceable as unconscionable under Missouri law, for the following reasons:

- The agreement was non-negotiable.
- There was a considerable disparity in the parties' bargaining power.
- The agreement was written in a manner that was hard for consumers to understand.
- The claimant produced evidence which showed that, realistically it would have been unlikely for it to be able to retain a lawyer to pursue an individual claim in arbitration.

Further, unlike *Concepcion*, in which AT&T waived its right to recover attorneys' fees, agreed to pay for the costs of arbitration, and agreed to pay up to double the customer's attorney's fees, the agreement in *Brewer* stated that the parties would bear their own costs and the company reserved the right to seek attorneys' fees.

As the *Brewer* case illustrates, despite the increased success by businesses in enforcing class action waivers, that result is by no means guaranteed. Whether or not a particular waiver will be enforced can turn not only on the circumstances and terms of the relevant arbitration provisions, but also on the jurisdiction in which the class action waiver is being challenged. Businesses should take care to stay abreast of this evolving area of law.

Factors that may help support court enforcement

Although the law continues to develop, and there is no one-size-fits-all approach for businesses wishing to include class action waivers as part of an arbitration strategy, certain factors have emerged from the court decisions which may provide useful guidance:

- Courts favour agreements that clearly and conspicuously evidence the parties' consent to arbitration, and in particular, that the parties waived the right to initiate or participate in a class action.
- Courts favour agreements that allow consumers to opt out of the mandatory arbitration within a reasonable period of time (such as within 60 days) after the agreement is consummated.
- Courts favour agreements that allow both parties to sue in a small claims court and seek injunctive or other equitable relief in the courts, without the need to arbitrate such claims.
- Courts favour agreements that include plain and understandable instructions on how the consumer can initiate an arbitration, including:
  - details on how to contact the designated arbitration tribunal(s); and
  - a detailed explanation of the steps that the consumer must take in order to initiate the arbitration.
- Courts favour agreements that provide for arbitration by a reputable and fair arbitration provider.
- Courts favour agreements providing that the arbitration can be conducted close to the consumer's residence or telephonically.
- Courts favour agreements that offset potential financial hardships by:
  - offering to pay for the arbitration in the event that the claimant is financially unable to do so otherwise; and
  - agreeing to pay the claimant's attorney's fees (in a reasonable amount and perhaps subject to a cap) if the claimant prevails in the arbitration.
- Courts favour agreements that do not restrict a claimant's potential monetary recovery. In other words, attempts at eliminating statutory or punitive damages should be avoided.

Other impediments to class action waivers

In addition to the complexities illustrated by the *Brewer* case (*see above, Class action waivers after Concepcion*), there are further potential impediments to the use of class action waivers, which are discussed below.

Contract formation is increasingly scrutinised. Following *Concepcion* and its progeny, some courts have focused on issues of contract formation to determine whether the consumer in fact agreed to arbitration and the class action waiver. This inquiry is largely confined to online transactions, where a consumer is deemed to have consented to arbitration by using the business's website to purchase goods or services. These contracts fall within the rubric of "clickwrap," "browsewrap," or "webwrap" agreements and their enforceability is beyond the scope of this article. However, it is important to note that the courts will refuse to enforce class action waivers and arbitration agreements in such agreements when the arbitration provisions were insufficiently conspicuous to ensure the consumer objectively agreed to their terms. Although later vacated by an appeals court, the Southern District of New York's decision in *Meyer v Kalanick, 200 FSupp3d 408 (SDNY 2016)*, provides a useful example of a class action waiver being invalidated in this context, as well as a cogent summary of the relevant legal landscape.

Some statutory claims are not arbitrable. In the consumer litigation context, some federal laws specifically prohibit arbitration and, by extension, corresponding class action waivers. The prohibitions include the following:

- The US Federal Trade Commission (FTC) has banned mandatory arbitration provisions in warranty claims made under the Magnuson-Moss Warranty Act (MMWA).
- A creditor who extends consumer credit cannot require an active duty member of the military or his/her dependent to submit to arbitration.
- In 2013, the US Consumer Financial Protection Bureau (CFPB) issued a rule amending the Truth in Lending Act (TILA) to (among other things) prohibit mandatory arbitration clauses in residential mortgage loans or home equity lines of credit.

Class action waivers can be waived if a party is not vigilant in seeking arbitration. Businesses wishing to take advantage of a class action waiver should be mindful that, if they fail to invoke an arbitration clause containing the class action waiver early in the litigation process, this could result in a court finding them to have waived their right to invoke arbitration.

The issue of what constitutes a waiver varies from jurisdiction to jurisdiction. However, most courts will consider a party to have waived their arbitration clause if the party's delay in seeking arbitration substantially prejudices the opposing party. Courts typically consider the cost incurred by the party opposing arbitration and the delay in the proceedings when examining prejudice. Courts are especially likely to find a waiver if they suspect that the party belatedly seeking to compel arbitration was forum shopping (that is, testing to see if they could obtain a favourable court decision (for example, on a motion to dismiss) before seeking to arbitrate the matter). To this end, businesses should be mindful of this issue, research the law in the jurisdiction in which any lawsuit is filed, and take steps to avoid a waiver.

Gatekeeper issues: who decides issues of arbitrability?

One unique issue that arises in litigating the enforceability of class action waivers in arbitration agreements is whether the court or the arbitrator makes certain "gateway" decisions. For example, if the arbitration provision provides that the arbitrator is to decide the

validity of the contract, then the arbitrator, and not the court, makes that gateway determination. Generally, there must be clear and unmistakable language in the agreement that the parties intended for the arbitrator to decide such gateway issues. These gateway issues might include:

- The validity of the contract.
- The validity of the class action waiver.
- Whether the arbitration can proceed as a class arbitration.

To retain judicial oversight on these key issues, most businesses carefully draft their arbitration clauses to ensure that the court (and not the arbitrator) decides gateway issues. This approach has found support when the issue has been considered by courts. For example, the US Court of Appeals for the Fifth Circuit recently joined six other federal circuit courts when it held that the availability of class arbitration is a threshold question of arbitrability to be decided by the courts absent clear and unmistakable language to the contrary in the arbitration or other agreement (*see 20/20 Commc'ns, Inc v Crawford*, 930 *F 3d 715 (5th Cir 2019) ("[T]he provisions cited by the employees do not clearly and unmistakably overcome the legal presumption—reinforced as it is here by the class arbitration bar—that courts, not arbitrators, must decide the issue of class arbitration."*)).

One advantage of having a court decide gateway issues (such as the enforceability of the arbitration decision) is that under section 16 of the FAA, an order denying a motion to compel arbitration or to stay a case pending arbitration can be immediately appealed, and often accompanied by a stay of the underlying case. This offers parties the advantage of having an appellate court review the trial court's decision on arbitration immediately and without the need to litigate the case to conclusion.

Regulatory and legislative efforts to limit class action waivers in consumer arbitrations

While US courts have become far more accepting of class action waivers, some regulators have expressed disdain for them, resulting in proposals that would dramatically limit the ability of some businesses to rely on pre-dispute class action waivers.

For example, in 2017 the CFPB published a rule (Arbitration Agreements Rule) banning the use of arbitration clauses by consumer financial services companies in their consumer contracts when combined with a restriction upon a customer's ability to file or join a class action lawsuit. However, on 1 November 2017, President Trump signed a joint resolution passed by Congress disapproving the Arbitration Agreements Rule under the Congressional Review Act (CRA). Pursuant to the joint resolution, the Arbitration Agreements Rule no longer has any force or effect.

Recent legislative efforts to revive the substance of the CFPB's now-defunct rule appear to have stalled. Two such efforts, the Arbitration Fairness for Consumers Act (*S 630*) and the House-passed Forced Arbitration Injustice Repeal Act (*S 610*), are both currently under review in various Senate committees. There appears to be a high likelihood, however, that should control of the Senate change in the near term, similar measures could successfully pass both houses of Congress.

EMPLOYMENT CONTRACTS

This section discusses special issues with class and collective action waivers that arise in the context of employment. Most commonly, class waivers are used in connection with employee arbitration agreements. The discussion within this section is set out as follows:

- The first section addresses the state of the law regarding the enforceability of class waivers in employee arbitration agreements.
- The second section discusses the contract formation factors that the courts will consider when assessing the validity of employee arbitration agreements.
- The third section highlights the unique federal and state law considerations impacting class waivers in employee arbitration agreements.
- The fourth section touches upon the limited use of class waivers in employment outside the context of arbitration.

Enforceability in employee arbitration agreements

Background. As discussed in the preceding sections, the FAA embodies federal policy that strongly favours the use of arbitration to resolve disputes (*see above, Federal Arbitration Act*). The FAA requires that arbitration agreements should be enforced as written, save for two exceptions:

- The first exception provides that, under the FAA, a court must enforce an otherwise valid arbitration agreement (including any class or collective action waiver contained therein) unless another federal statute contains a "contrary congressional command" that is sufficient to override the FAA's mandate (*CompuCredit v Greenwood, 132 S Ct 665, 670-669 (2012)*). The Supreme Court has repeatedly held that, for this exception to be satisfied, the federal statute must be clear in its "command" that arbitration is foreclosed. The Supreme Court has, for example, upheld the enforceability of an arbitration agreement containing a class/collective action waiver as applied to claims under the federal Age Discrimination in Employment Act (ADEA), reasoning that, while the ADEA expressly permits class actions, it contains no language barring arbitration (*Gilmer v Interstate/Johnson Lane Corp, 500 US 20 (1991)*).
- The second exception is the FAA's "savings clause". This provides that a court can decline to enforce an arbitration agreement based on "generally applicable" contract defences which provide "for the revocation of any contract" (*9 USC § 2*). However, if a defence normally thought to be generally applicable (such as fraud, duress, unconscionability, or illegality) is applied in a way that targets or uniquely disfavours arbitration, the Supreme Court has held that the defence will not be considered "generally applicable" under the FAA (*Concepcion, supra, at 346*).

The National Labor Relations Act (NLRA) does not prohibit class waivers in employment arbitration agreements. In recent years, the US National Labor Relations Board (NLRB) aggressively sought to bar the use of class action arbitration waivers in employee agreements through an expansive interpretation of the NLRA, a federal statute enacted in 1935 to protect the rights of employees and employers and facilitate collective bargaining between them. The NLRB's efforts focused on the interplay between the FAA and NLRA. However, on 21 May 2018, the Supreme Court—resolving a key circuit split—expanded *Concepcion* and concluded that class action waivers in employment agreements are enforceable and do not violate the NLRA (*Epic Systems Corp v Lewis, 138 S Ct 1612 (2018)*). The Court recognised the policy considerations advanced in opposition to the use of arbitration agreements in employment agreements but ultimately rejected the arguments, explaining that "Congress has instructed that arbitration agreements [such as those in employment agreements] must be enforced as written. While Congress is of course always free to amend this judgment, we see nothing suggesting it did so in the NLRA—much less that it manifested a clear intention to displace the" FAA.

On 14 August 2019, the NLRB confronted the issue for the first time after *Epic Systems* (*Cordua Restaurants, Inc, 368 NLRB No 43 (2019)*). Doing so, the Board held that:

- The FAA does not prohibit employers from promulgating arbitration agreements with class action waivers "in response to employees opting into a collective action".
- The FAA does not "prohibit[] employers from disciplining or discharging an employee who refuses to sign a mandatory arbitration agreement".

Courts will not compel parties to arbitrate claims on a classwide basis when an otherwise enforceable arbitration agreement is silent or ambiguous on the issue. On 24 April 2019, the Supreme Court answered the question whether class claims could be pursued in arbitration when the language in the arbitration agreement is ambiguous (*Lamps Plus, Inc v Varela, 139 S Ct 1407 (2019)*). The Supreme Court had previously held that a court cannot compel arbitration on a classwide basis when an agreement is "silent" on the availability of class arbitration (*Stolt-Nielsen SA v Animalfeeds International Corp, 559 US 662 (2010)*), but had not yet addressed what courts should do when an agreement is "ambiguous" on the point. Relying on *Stolt-Nielsen* and *Epic Systems*, the Court expanded its jurisprudence in favour of applying arbitration agreements as written, holding that "[c]ourts may not infer from an ambiguous agreement that parties have consented to arbitrate on a classwide basis". Accordingly, courts cannot compel arbitration of claims on a classwide basis if an arbitration agreement is ambiguous as to whether class arbitration is available (*see, for example, Price v Santander Consumer USA Inc, Civil Action No 3:19-CV-0742-B (ND Tex September 12, 2019)* (*applying Lamps Plus rationale to arbitration agreements covering Fair Labor Standards Act collective action claims and granting motion to compel individual arbitration*)).

General issues affecting enforceability

The enforceability of class action waivers in an employee arbitration agreement often turns on the circumstances and the terms of the agreement itself. As noted above, the FAA generally defers to state law contract formation principles to assess the validity of an arbitration agreement (*see above, Enforceability in employee arbitration agreements*). In an employment context, this involves analysing issues of valid consideration and whether the agreement is unconscionable. Some common examples of valid consideration in an employee arbitration agreement are:

- Offer of employment or continued employment.
- A salary rise or signing bonus.
- Providing additional vacation days.

Continued employment is by far the most controversial form of consideration. The majority view is that continued employment is sufficient consideration. However, at least one state court has held otherwise (*see Baker v Bristol Care, Inc, 450 SW 3d 770 (Mo 2014)*). Litigating the enforceability of class waivers in employee arbitration agreements often involves arguments that the agreement is unconscionable: an agreement found to be both procedurally and substantively unconscionable will be deemed unenforceable.

Procedural unconscionability focuses on the circumstances in which the employee entered into the agreement. This requires the court to consider, for example, the presence of any oppression, surprise or unequal bargaining power. While the dynamic between employer and employee often inherently involves a level of unequal bargaining power, this alone does not constitute procedural unconscionability. Rather, procedural unconscionability generally requires a combination of multiple factors, including:

- A "take it or leave it" clause in the arbitration agreement, so the employee does not have any meaningful opportunity to negotiate or reject its terms.
- Terms hidden in the middle of the agreement in small font.
- Failing to provide the employee with a copy of the actual arbitration agreement until after the waiver is signed.

Importantly, requiring employees to sign arbitration agreements as a condition of employment or continued employment, without the ability to negotiate the agreement's terms (a "take it or leave it" agreement) is common. And while this factor is often cited by claimants arguing for a procedural-unconscionability finding, it is rarely sufficient on its own to support such a finding. Nevertheless, employers sometimes seek to reduce the risk of a procedural-unconscionability finding by allowing employees to elect not to sign (or opt out of) the employer's standard arbitration agreement without risk to their continued employment.

Substantive unconscionability concerns the reasonableness of the terms in the agreement, the allocation of risk between the employer and the employee, and public policy. Some terms or conditions deemed substantively unconscionable in the employment context include:

- Limiting discovery mechanisms.
- Requiring employees to split fees with the employer or front the costs of arbitration.
- Shortening statutes of limitations or forms of recovery available.
- Imposing attorneys' fees on the employee if the employer prevails.
- Controlling who the arbitrator will be and not allowing the employee any say.

To avoid a potential finding that their arbitration agreement is substantively unconscionable, employers often agree to:

- Cover many or all costs of arbitration.
- A neutral procedure for selecting the arbitrator.
- Allow the employee to obtain exactly the same recovery or other relief that would be permitted were he/she to pursue his/her claim in court.
- Permit the employee to have some form of discovery in pursuing his/her claim in arbitration.

For the same reasons, employers will often include provisions stating that arbitration will proceed under the rules and procedures established by the American Arbitration Association or JAMS (widely recognised for their fairness to employees).

In addition, employers may include "severability" clauses in arbitration agreements, allowing a court to sever any provision that would otherwise render the agreement unconscionable. Employers can carefully draft the severability clause in a manner that excludes its application to the agreement's class waiver provision.

Special considerations arising under federal and state law

- **Exceptions arising under the FAA and other federal statutes.** Several sources of federal law restrict the use of arbitration agreements and can therefore have the practical effect of limiting (or potentially limiting) the ability to enforce corresponding class waivers. Three specific examples are discussed below:
- **FAA's express restrictions.** By its own terms, the FAA does not apply to workers in certain professions, including those engaged in interstate commerce, which courts interpret to mean only transportation workers engaged in interstate commerce. When this exemption applies, courts will look to state law (not the FAA) in assessing the validity of the arbitration agreement and class action waiver. For example, two California state courts concluded that the FAA did not apply to truck drivers, and therefore relied on state law principles to invalidate the drivers' arbitration agreements because they contained class action waivers (*Muro v Conerstone Staffing Sols, Inc, 20 Cal Rptr ed 498 (Cal Ct App 2018); Garrido v Air Liquide Industrial US LP, 194 Cal Rptr 3d 297 (Cal Ct App 2015)*). These decisions are particularly notable considering that the California Supreme Court previously held that, when the FAA applies, such agreements are enforceable (*Iskanian v CLS Transp LA, LLC, 559 Cal 4th 348 (Cal 2014)*).
- **Dodd-Frank Act's anti-arbitration provisions.** The Dodd-Frank Act contains express anti-arbitration provisions which bar agreements requiring the arbitration of claims under the Act. While unsettled, some courts have held that these provisions are limited to retaliation claims arising under the Sarbanes-

Oxley Act, and would therefore not affect the enforceability of arbitration agreements and corresponding class waivers concerning whistleblower retaliation claims under the Dodd-Frank Act itself (*see, for example, Daly v Citigroup, Inc, 939 F 3d 415 (2d Cir 2019); Khazin v TD Ameritrade, 773 F 3d 488 (3rd Cir 2014)*).

State law considerations. Despite the FAA and recent Supreme Court decisions expanding the enforcement of arbitration agreements (such as *Epic Systems*), some states have enacted laws and regulations regarding the enforcement of arbitration agreements in the employment context. For example, effective 1 January 2020, California passed a law prohibiting employers from requiring workers to arbitrate state law discrimination and labour code violations (*Assembly Bill No 51*). The law applies only to agreements "entered into, modified, or extended" on or after 1 January 2020, and is not "intended to invalidate a written arbitration agreement that is otherwise enforceable under the [FAA]" (*9 USC Sec 1 et seq*). Employers have already begun challenging this and other similar state laws as being pre-empted by the FAA. Indeed, on 30 December 2019, US District Court Judge Kimberly Mueller in Sacramento, California, issued a temporary restraining order halting enforcement of Assembly Bill No 51, finding that "plaintiffs have raised serious questions regarding whether the challenged statute is preempted by the [FAA] as construed by the United States Supreme Court" (*Chamber of Commerce v Becerra, et Al, No 2:19-cv-02456-KJM-DB (ED Cal December 30, 2019)*. Several weeks later, Judge Mueller issued a preliminary injunction extending the prohibition on the enforcement of Assembly Bill No 51 (*Chamber of Commerce v Becerra, et Al, No 2:19-cv-02456-KJM-DB (ED Cal February 7, 2020)*. That ruling is now on appeal before the United States Court of Appeals for the Ninth Circuit.

Additionally, in 2018, New York enacted a purported ban on mandatory arbitration of harassment claims. The law, which amended section 7515 of the New York Civil Practice Law and Rules, was originally drafted to prohibit the submission of sexual harassment claims to mandatory arbitration, but lawmakers expanded the prohibition in August 2019 to **all** discrimination claims. A decision from the US District Court for the Southern District of New York (*Latif v Morgan Stanley & Co LLC, Case No 18-cv-11528 (DLC) (SDNY June 26, 2019)*) held that the initial prohibition in section 7515 as to sexual harassment claims was inconsistent with the FAA and, therefore, unenforceable. The decision noted in a footnote that the amended version of section 7515 also "would not provide a defense to the enforcement of" the arbitration agreement at issue. No court has addressed the enforceability of section 7515 as amended following the decision in *Latif*, but litigation involving the amendment (which covers class claims) is inevitable.

Similarly, in 2018, the New Jersey Law Against Discrimination was amended to prohibit provisions "in any employment contract" that prospectively waive certain procedural and substantive rights, and to bar employers from taking any retaliatory action against a person who does not enter into "an agreement or contract" that contains such provisions. The amendment does not explicitly refer to arbitration agreements, but it could be read to prohibit employers from requiring employees to sign agreements to arbitrate employment disputes, including class claims. The law is currently being challenged on FAA pre-emption grounds in the case *New Jersey Civil Justice Institute, et al, v Grewal, Case No 3:19-cv-17518 (DNJ),* which was filed on 30 August 2019.

Further, state laws can also make it harder to enforce such class waivers in employee arbitration agreements. For example, California's PAGA allows employees to bring a claim on behalf of the state to recover civil penalties against an employer for its violations of the California Labor Code. The California Supreme Court in *Iskanian* concluded that class action waivers are unenforceable in relation to PAGA representative action claims. Specifically, the Court held that the FAA does not pre-empt California public policy to enforce wage-hour laws on behalf of the state because a PAGA claim is not a true dispute between two private parties, but rather a dispute between the state and an employer. Therefore, the Court reasoned that the FAA's presumption favouring the enforcement of arbitration agreements was inapplicable.

Class and collective action waivers outside of arbitration agreements

Some employers seek to use class waivers outside of employee arbitration agreements. For example, class action waivers may appear in severance agreements or as a stand-alone condition presented in employment application materials or an employee handbook. Currently, there is no consensus among courts regarding the enforceability of class waivers in these contexts. The NLRB might argue that, outside the arbitration context (which is what the Supreme Court addressed in Epic Systems and Lamps Plus), the FAA and its strong policy favouring arbitration are inapplicable and therefore the Supreme Court's decisions in those cases are irrelevant. By contrast, employers might argue that the FAA merely places arbitration agreements on equal footing with any other contract, and so the conclusion that class waivers are valid should not turn on the type of contract at issue.

Conclusion

Class waivers in both consumer contracts and employee arbitration agreements are generally enforceable in most jurisdictions, when correctly structured and implemented. In the consumer context, we expect increased judicial focus on contract formation issues and challenges to the entire contract (and not just the arbitration clause) as unconscionable. In the employment context, given the Supreme Court's recent decisions (such as those in *Epic Systems* and *Lamps Plus*), arbitration agreements with class action waivers are an effective means for fairly and efficiently resolving employee claims. That said, employers and litigants will have to wait and see whether and to what extent states will continue to pass legislation addressing arbitration agreements and class waivers, and how courts will review the interplay between state law and the FAA.

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