An *Epic* Supreme Court Decision Enforcing Class Arbitration Waivers in Employment Agreements

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Roughly half of franchise agreements contain arbitration provisions. Christopher R. Drahozal, *Arbitration Clauses in Franchise Agreements: Common (and Uncommon) Terms*, 22 Franchise L.J. 81 (Summer 2002). Many times, the arbitration provision requires that claims be tried individually—prohibiting aggregation of claims into a class. In the last several years, the United States Supreme Court has issued a number of decisions enforcing class arbitration waivers.

In May, the Court issued its opinion in *Epic Systems Corp. v. Lewis*, 138 S. Ct. 1612 (2018), again addressing the question of the enforceability of class arbitration waivers—this time in the context of employment agreements. *Epic Systems* is a continuation of the Court's recent line of decisions enforcing class arbitration waivers, and any lingering doubt about the enforceability of class arbitration waivers in employment agreements was decidedly resolved in favor of arbitration.

The Backdrop to *Epic Systems*

Critical to understanding the majority's decision in *Epic Systems* is a review of the Court's most recent decisions addressing class arbitration waivers.

The first in the line of cases was *AT&T Mobility, LLC v. Concepcion*, 563 U.S. 333 (2011). In *Concepcion*, consumers argued that an arbitration provision prohibiting class arbitration contained in their telephone service contract was unenforceable under California precedent, which declared class action waivers unconscionable in consumer contracts of adhesion. *Id.* at 340. Rejecting the consumers' position, the Court held that California's prohibition was preempted by the Federal Arbitration Act (FAA) because it stood "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in enacting the FAA. *Id.* at 352. The Court explained that the FAA was designed to promote arbitration, and class arbitration sacrifices the principal advantage of arbitration: informality. *Id.* at 348. The Court noted that class arbitration is less expedient and increases risks to defendants because of the lack of procedural safeguards and, as a result, defendants are more likely to settle unmeritorious claims. *Id.* at 350. *Concepcion* was a pivotal foretelling of the Court's willingness to enforce class arbitration waivers, and to prioritize the FAA over other competing concerns and rules.

Two years later, the Court addressed merchants' challenge of a class arbitration waiver in their agreement with American Express. *American Express Co. v. Italian Colors Restaurant*, 570 U.S. 228, 231 (2013). The merchants brought a class action against American Express for violating antitrust laws. *Id.* They sought to invalidate their arbitration agreement arguing that individual arbitration would destroy any economic incentive to pursue antitrust claims—specifically where the cost of individual arbitration exceeded the potential recovery. *Id.* Enforcing the class arbitration waiver, the Court held that the cost of individual arbitration did not destroy the merchants' *right* to pursue their statutory remedy and, therefore, gave them effective vindication. *Id.* at 236-37.

In 2015, the Court addressed a service contract between consumers and DIRECTV that waived class arbitration. *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463 (2015). Unlike the two prior decisions, the contract provided that if the law of the customer's state makes the class arbitration waiver unenforceable, the arbitration provision "'is unenforceable.'" *Id.* at 466. Again refusing an opportunity to hold class arbitration waivers unenforceable and rejecting the lower court's

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attempt to maneuver around *Concepcion*, the Supreme Court reiterated that the FAA preempts state law. *Id.*at 471.

The *Epic Systems* Decision

At the same time that the Court was ruling in favor of class arbitration waivers in commercial and consumer contracts, a new wrinkle was developing for employment agreements subject to the National Labor Relations Act ("NLRA"). In a 2012 decision, the National Labor Relations Board ("NLRB") concluded that a class arbitration waiver violated Section 7 of the NLRA, which allows employees to engage in "concerted activities for the purpose of collective bargaining or other mutual aid or protection." *In re D.R. Horton*, 357 NLRB 2277, at *1.

The collision of the NLRB's new position and the Court's precedent enforcing class arbitration waivers resulted in a circuit split with the Sixth, Seventh, and Ninth Circuits holding that class arbitration waivers in employment agreements were unenforceable and the Second, Fifth, and Eighth Circuits holding them enforceable. As a result of the circuit split, three cases arrived at the Court: *Epic Systems Corp. v. Lewis* (7th Cir.); *NLRB v. Murphy Oil USA* (5th Cir.); and *Ernst & Young v. Morris* (9th Cir.). The consolidated cases each involved employees attempting to bring claims in court under the Fair Labor Standards Act and state law, despite their employment contracts' requiring individualized arbitration proceedings. The employees claimed the arbitration agreements were unenforceable because "class and collective actions are 'concerted activities' protected by § 7 of the NLRA." *Epic Systems*, 138 S. Ct. at 1617.

In *Epic Systems*, the Court again ruled in favor of arbitration—holding that individual arbitration agreements in employment contracts must be enforced and are not barred by the FAA's saving clause or the NLRA. *Id.* at 1632. The Court identified the question before it this way: "... should employees always be permitted to bring their claims in class or collective actions, no matter what they agreed with their employer?" *Id.* at 1619. The majority's opinion, written by Justice Gorsuch, recognized that the issue may be debatable as a matter of policy, but the decision was "clear" as a matter of law. *Id.*

The Court rejected the assertion that the NLRA compelled them to hold the arbitration agreements invalid and refused to read a right to class actions into the NLRA. *Id.* at 1624-27. Instead, the Court held that the FAA compelled the lower courts to enforce arbitration agreements according to their terms. *Id.* at 1621. The NLRA only secures employees the rights to organize unions and bargain collectively, but does not dictate "how judges and arbitrators must try legal disputes that leave the workplace." *Id.* at 1619.

By attacking the individual nature of arbitration, the employees interfered with a fundamental attribute of arbitration that would undermine the informality of arbitration—against the holding in *Concepcion*. *Id.* at 1622. Relying on *Concepcion*, the Court instructed that "courts may not allow a contract defense to reshape traditional individualized arbitration by mandating classwide arbitration procedures without the parties' consent"—regardless of what creative device it takes. *Id.* at 1623. Notably, the Court pointed out that it has rejected "*every*" effort to create a conflict between the FAA and other federal statutes that it has considered. *Id.* at 1627.

Justice Ginsburg wrote a dissent (in which Justices Breyer, Sotomayor, and Kagan joined) referring to the majority's opinion as "egregiously wrong," arguing that class arbitration waivers are unenforceable under the NLRA. *Id.* at 1633.

What Does *Epic Systems* Mean for Your Franchise Business?

Not surprisingly, the Court's decision continues the enforcement of arbitration agreements requiring individual arbitration over objections concerning their validity. *Epic Systems* clarified enforcement in a different context—employment agreements. The Court's decision is a significant rejection of attempts to evade employment arbitration provisions that contain class action waivers, despite the position taken by the NLRB in *In re D.R. Horton*.

Since the decision was issued in May, lower courts are relying on *Epic Systems* to enforce class arbitration waivers. In addition to resolving the circuit split, there are three practical takeaways for consideration:

First, both franchisors and franchisees should revisit their existing arbitration provisions to evaluate whether to include a class arbitration waiver. Recognizing that class arbitrations can present significant risk, complexities and exposure not present in individual arbitration,

many employers are in the process of revisiting their employment agreements to include a waiver of class arbitration. If you do not already have an arbitration provision, consider whether to include an arbitration provision containing a class arbitration waiver. Following *Epic Systems*, employers can be more confident in moving to compel individual arbitration of claims. Franchisees may want to consider entering arbitration agreements (with a class waiver) with their employees, especially given the exposure in wage and hour class actions. On the other hand, both franchisors and franchisees should understand the potential adverse effects from class arbitration waivers, including public relations and the potential for mass filings of individual arbitration demands against a company.

Second, developments in enforceability of class arbitration waivers are ongoing. Although courts generally enforce class arbitration waivers, *Epic Systems* does not answer all looming questions. Questions remain about the scope and applicability of class waivers in employment agreements, depending on the type of claims, including sexual harassment or discrimination claims. Further, class waivers are still facing challenges if they are not sufficiently conspicuous, so consider the placement and font size of your provision.

Epic Systems leaves an opening for Congress to revise the NLRA to expressly prohibit class action waivers: "The respective merits of class actions and private arbitration as means of enforcing the law are questions constitutionally entrusted not to the courts to decide but to the policymakers in the political branches where those questions remain hotly contested." Id. at 1632. Other attempts to bar class arbitration waivers at the federal level may develop, such as those by the Consumer Financial Protection Bureau ("CFPB"), which *Epic Systems* referenced by noting that Congress recently repealed the CFPB's rule against class action waivers. Reaction may also come from state legislatures attempting to limit enforceability of arbitration provisions in employment and other agreements (for example, recent efforts in California), raising FAA preemption issues. *See Concepcion*, 563 U.S. at 341 ("When state law prohibits outright the arbitration of a particular type of claim...[t]he conflicting rule is displaced by the FAA.").

Third, another great unknown remains: the enforceability of class action waivers outside of arbitration agreements. Even if you do not have an arbitration provision, you may want to consider including a class action waiver in your contracts. The Court's recent opinions on class arbitration waivers do not address enforceability of class action waivers outside of arbitration agreements.

Although there is a dearth of case law, and conflict among the recent cases that do address class waiver provisions outside of arbitration, some courts enforce class waivers even if not part of an arbitration provision. *See, e.g., Convergys Corp. v. Nat'l Labor Relations Bd.*, 866 F.3d 635 (5th Cir. 2017) (enforcing class waiver in employment case outside of arbitration context) and *McIntosh v. Royal Caribbean Cruises, Ltd.*, No. 17-CV-23575, 2018 WL 1732177, at *3 (S.D. Fla. Apr. 10, 2018) ("Class action waivers are enforceable outside the context of consumer arbitration."); *Meyer v. Kalanick*, 185 F. Supp. 3d 448, 458 (S.D.N.Y. 2016) ("*Concepcion*

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thus provides no basis on which to conclude that California law on the unconscionability of class action waivers would be invalid outside the arbitration setting.").

This conflict is not new for franchise attorneys. *Compare Bonanno v. Quizno's Franchise Co.*, LLC, No. CIV. A06CV02358CMAKLM, 2009 WL 1068744, at *8 (D. Colo. Apr. 20, 2009) (enforcing class action waiver pre-*Concepcion* in franchise agreement) and *Martrano v. Quizno's Franchise Co.*, No. CIV.A. 08-0932, 2009 WL 1704469, at *21 (W.D. Pa. June 15, 2009) (refusing to enforce class action waiver in franchise agreement). Therefore, franchise practitioners must continue to monitor the developments on the enforceability of class waivers inside and outside of arbitration.