The California Supreme Court Curtails *Concepcion's* Protection of Arbitration Agreements

MSK Alert by Brett Thomas
November 2013

In *AT&T Mobility v. Concepcion*, the United States Supreme Court analyzed the extent to which a court could refuse to enforce an arbitration agreement because the terms are "unconscionable," meaning that one party did not have meaningful choice in negotiating the terms and the terms are unreasonably favorable to the other party. *Concepcion* held that, in the context of arbitration agreements in consumer contracts, the Federal Arbitration Act (FAA) prohibits courts from denying enforcement of an arbitration agreement on the grounds of unconscionability where the application interferes with the FAA's objectives of: (1) enforcing arbitration agreements according to their terms; and (2) facilitating informal, efficient, and streamlined proceedings tailored to the type of dispute at issue.

In *Sonic-Calabasas A., Inc. v. Moreno (Sonic II)*, the California Supreme Court for the first time analyzed the enforceability of an employment arbitration agreement in light of *Concepcion*. While at first blush the decision appears to be a victory for employers, the *Sonic II* decision narrowly applies *Concepcion* and creates more uncertainty for employers in terms of the enforceability of employment arbitration agreements.

The *Sonic II* Decision

In *Sonic II,* the Court considered whether an employer could compel arbitration of a wage claim filed with the California Department of Labor Standards Enforcement ("DLSE"), thereby forcing the employee to forfeit his right to adjudicate his wage claim through an administrative proceeding called a "Berman hearing." The California Supreme Court previously established a categorical rule prohibiting employers from requiring employees to waive the right to a Berman hearing in arbitration agreements. In *Sonic II*, the Court reversed its prior decision and held that, in light of *Concepcion*, its blanket rule prohibiting the waiver of Berman hearings violates the FAA.

The most important aspect of the *Sonic II* decision is its analysis of *Concepcion*.

Concepcion Is Narrowly Construed

In *Sonic II*, the California Supreme Court analyzed whether *Concepcion* affects a court's ability to invalidate employment arbitration agreements on unconscionability grounds. The Court found that unconscionability remains a valid reason to deny enforcement of an employment arbitration agreement or a provision therein, with certain limitations. Specifically, a court may not apply unconscionability rules if the result will go against the "fundamental attributes of arbitration" of having an informal, streamlined means of dispute resolution.

The Court explained that unconscionability should be determined by conducting an individualized assessment and "examin[ing] the totality of the [arbitration] agreement's substantive terms as well as the circumstances of its formation to determine whether the overall bargain was unreasonably one-sided." The Court also explained that a trial court should not only look at the terms of the agreement, but also analyze how the arbitration would be conducted in practice.

In addition, *Sonic II* creates some confusion as to the proper standard to apply for determining whether an agreement is substantively unconscionable. The Court describes the standard as whether the agreement is "unreasonably one-sided," whereas other courts previously have employed a "shock the conscience" standard that appears more restrictive. The Court did not decide "whether these different formulations actually constitute different standards in practice and whether one is more objective than the other," creating more uncertainty for employers seeking to enforce arbitration agreements. The Court clarified that unconscionability requires a substantial degree of unfairness that is more than a bad bargain.

ASK MSK

Q: What effect does *Sonic II* have on an employer's ability to require employees to sign arbitration agreements as a condition of employment?

A: *Sonic II* is consistent with prior case law in finding that employers may require employees to sign arbitration agreements as a condition of employment, but the lack of choice will be one factor a court will consider in determining whether the agreement is unconscionable. Employers should be very careful to draft fair agreements that are not unreasonably one-sided to avoid a finding of unconscionability.

Q: Did *Sonic II* address whether class action waivers in employment arbitration agreements are enforceable?

A: No, *Sonic II* did not involve an analysis of the enforceability of class action waivers. However, *Sonic II* clarifies that an employee may argue that a class action waiver is unconscionable, although it appears that the application of the unconscionability doctrine to class action waivers may be preempted by the FAA to the extent that it causes an interference with the fundamental attributes of arbitration. The California Supreme Court will analyze the enforceability of class action waivers in an employment arbitration agreement in its review of *Iskanian v. CLS Transportation Los Angeles, LLC*. (Please see the prior MSK Alert entitled "Labor and Employment Law 2013: A Year-End Review" for a discussion of the *Iskanian* case.)