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2012Kenneth M.  
Jones, Esq.Questions  
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## Drafting Arbitration Agreements and Navigating Between State Law and the FAA

By Kenneth M. Jones

As we have written previously, arbitration can be a cost-effective and preferable choice for many employers, and for that reason, many employers utilize arbitration agreements in the employment context. But as we have also discussed, employers need to be careful in drafting arbitration agreements to avoid having a court consider the agreement unenforceable, leading to the civil court litigation that arbitration agreements seek to avoid in the first place. Added to that, the sometimes-conflicting views of state and federal courts, not to mention the inconsistent application of existing law by state courts to arbitration agreements, can make an employer's task even more difficult. A recent decision by a California Court of Appeal, however, may demonstrate how a 2011 United States Supreme Court case may bring some welcomed clarification in this area for employers.

This past June in *Iskanian v. CLS Transportation*, 206 Cal. App. 4th 949 (Cal. Ct. App. June 4, 2012), a California Court of Appeal upheld an employer's arbitration agreement that required employees to waive their ability to bring class-action lawsuits. While the California Supreme Court has since accepted an appeal of the decision, putting the lasting effects of the court of appeal's decision in some doubt, the decision demonstrates the importance of relying on the Federal Arbitration Act ("FAA") when drafting arbitration agreements and motions to compel arbitration. The decision also shows the difficulty employers sometimes face in the intersection of state and federal law on the subject of arbitration.

In August 2006, Mr. Iskanian filed a class action complaint against CLS Transportation ("CLS") alleging a variety of wage claims, including that CLS

failed to pay overtime and provide meal and rest breaks. CLS moved to compel individual arbitration pursuant to an agreement Mr. Iskanian signed, which contained a class-action waiver. The trial court found that the agreement was not procedurally or substantively unconscionable and granted the motion to compel arbitration. However, soon after the trial court made that ruling, the California Supreme Court issued a ruling in a separate case, *Gentry v. Superior Court*, 42 Cal. 4th 443 (Cal. 2008). Broadly speaking, the *Gentry* court mandated that class-action waivers should be invalidated where class actions are a more effective means of vindicating the rights of aggrieved employees than individual arbitration or litigation. The *Gentry* court outlined a four-factor test that courts were to apply in deciding whether class waivers are unenforceable. After the *Gentry* decision, Mr. Iskanian appealed the trial court's order, and the state appellate court sent the case back to the trial court, directing it to reconsider its granting of CLS's motion in light of the *Gentry* ruling. When the case was sent back to the trial court, CLS voluntarily withdrew its motion to compel individual arbitration, and the case proceeded to litigation.

That was not the end of the matter, however. While the *Iskanian* matter was still in litigation, the United States Supreme Court issued a decision in *AT&T Mobility v. Concepcion*, 131 S.Ct. 1740 (2011), in April 2011. In *Concepcion*, the Supreme Court reiterated the rule that the principal purpose of the FAA is to ensure that arbitration agreements are enforced according to their terms and held that "[r]equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA." After *Concepcion*, CLS renewed its earlier motion to compel arbitration, and the trial court again granted it. Mr. Iskanian then appealed the matter again.

This time, however, the California Court of Appeal sided with CLS. The *Iskanian* court interpreted *Concepcion* as conclusively invalidating the *Gentry* test, and it affirmed the trial court's order compelling Mr. Iskanian to individually arbitrate his claims. The *Iskanian* court held that the FAA preempts previous California law, which held, among other things, that class-action waivers in arbitration clauses as to employees' unwaivable rights were contrary to public policy. In rejecting CLS's argument that the *Gentry* rule was based on public policy and as a consequence *Concepcion* should not apply, the *Iskanian* court found that the *Concepcion* ruling applies even where employees are attempting to vindicate state statutory rights, such as overtime pay. The *Iskanian* court reiterated *Concepcion*'s mandate that "states cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons." The court also noted that "[t]he sound policy reasons identified in *Gentry* for invalidating certain class waivers are insufficient to trump the far reaching effect of the FAA."

Based on this reasoning, the *Iskanian* court also addressed Mr. Iskanian's claims under California's Private Attorney General Act ("PAGA"), which permits individuals to pursue certain individual claims as well as claims on behalf of others. The *Iskanian* court noted that a different

California Court of Appeal held in *Brown v. Ralphs Grocery Co.*, 197 Cal. App. 4th 489 (Cal. App. Ct. 2011), that *Concepcion* does not apply to a plaintiff's claims under PAGA but disagreed with that ruling: "We recognize that the PAGA serves to benefit the public and that private attorney general laws may be severely undercut by application of the FAA. But we believe that the United States Supreme Court has spoken on the issue, and we are required to follow its binding authority."

As noted earlier, however, the California Supreme Court has accepted an appeal on the case, and it may take a year or two for it to issue a decision. The lower court decision suggests a possible trend of increased deference to the FAA by California courts, which would be welcome news to employers. In recent years, the California state courts have been all over the map in terms of enforcing arbitration agreements. There have been a number of cases where a court has refused to enforce an arbitration agreement based on principles of California statutory law. But there have been almost an equal number of cases where a court enforced an arbitration agreement.

No matter on which side the California Supreme Court decision ultimately falls, employers moving to compel arbitration in California should, when possible, remove cases to federal court before filing the motion. Given that the FAA is a federal statute, federal courts are more likely than state courts to compel arbitration. Even if the case cannot be removed and must stay in state court, it behooves employers to advance a strong argument that the failure to enforce the agreement would frustrate the purposes of the FAA.

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