

Plaintiff

[The “Opt-Out” Trap](#)

New battlefield in employers’ effort to avoid class liability through arbitration clauses

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Employees recently won a significant victory when the Ninth Circuit Court of Appeals held that arbitration clauses forbidding employees from joining together in a single proceeding are unlawful under the National Labor Relations Act. (See *Morris v. Ernst & Young*, ___ F.3d ___, 2016 WL 4433080 (9th Cir. Aug. 22, 2016).)

Under *Morris*, as a matter of first impression in this Circuit, an employer’s mandatory arbitration agreement that forbids class proceedings in all forums is a violation of the NLRA’s guarantee of the right of employees to engage in “concerted action.” After *Morris*, an employer may be able to compel an employment class action to arbitration, but the employer will not be able to avoid a class proceeding altogether.

In light of *Morris*, a defense-side weapon known as an “opt- out” provision is likely to appear much more frequently in routine employment arbitration provisions. Such a provision – often buried at the end of a long, dense, mandatory contract – gives the employee an opportunity to take affirmative steps to “opt out” of the arbitration agreement within a certain period of time after accepting it. For example, the contract may state that by submitting a written request to opt out of arbitration within thirty days after accepting the agreement, the employee can avoid being bound by the arbitration terms.

Although an opt-out provision may seem at first glance like a benefit for employees, the employer’s transparent purpose for including the clause is to insulate the arbitration agreement from later attacks by the employee. Employers know that few, if any, employees will discover the opt-out clause, and that those who do will be unlikely to decide to begin their employment relationship by informing the employer that they are taking affirmative steps to preserve their right to sue the company in court. Employers are including the clause because an employee’s failure to follow the opt-out steps will place the employee in a worse position with respect to participating in a class or collective action than if there had been no opt-out clause at all.

Defeating the right to “concerted action”

Employees who fail to take affirmative steps to “opt out” of an arbitration agreement may lose the NLRA-provided right to engage in concerted action, which, as *Morris* recognized, includes the substantive right to engage a class or collective action. The arbitration agreement in *Morris* had no opt-out provision, and on that basis, the court specifically distinguished an earlier Ninth Circuit case, (*Johnmohammadi v. Bloomingdale’s, Inc.*), where the presence of an opt-out provision had led the panel to hold that there was no NLRA violation. (755 F.3d 1072, 1076 (9th Cir. 2014).) The *Johnmohammadi* court concluded that because the employee had not taken the steps to opt out of the arbitration agreement, she had voluntarily given up her right to engage in concerted action going forward.

Like *Morris*, *Johnmohammadi* was a matter of first impression in the Circuit, and although it is currently the law, *Johnmohammadi* may be on uncertain footing. The Seventh Circuit recently singled it out for criticism, pointing out that it allows employees to prospectively waive their right to engage in concerted action under the NLRA, which is contrary to longstanding precedents of the Seventh Circuit and the National Labor Relations Board (“NLRB”). (See *Lewis v. Epic Sys. Corp.* (7th Cir. 2016) 823 F.3d 1147, 1155.) Some lower courts in other circuits have expressly not followed *Johnmohammadi*. (See *In re: Fresh & Easy, LLC*, 2016 WL 5922292, at *12 (Bankr. D. Del. Oct. 11, 2016)) (“[T]he fact that the Plaintiff was given an opportunity to opt out of the Arbitration Agreement does not alter the Court’s determination that the Class Waiver is unenforceable.”); (*Curtis v. Contract Mgmt. Servs.*, 2016 WL 5477568, at *6 (D. Me. Sept. 29, 2016) (same).) In addition, the NLRB, to whom federal courts owe deference when interpreting the NLRA, has held, post-*Johnmohammadi*, that class waivers, even when accompanied by an opt-out clause, violate the NLRA right to engage in concerted action. (See *On Assignment Staffing Services, Inc.*, 362 NLRB No. 189 (2015).) The NLRB has indicated that it will be filing an *amicus* brief in a pending Ninth Circuit case involving a class waiver accompanied by an opt-out provision. (See *O’Connor v. Uber Techs. Inc.*, Case No. 15-17420 (Oct. 14, 2016 appearance of NLRB as *amicus curiae*.)

But so long as it remains the law in this Circuit, *Johnmohammadi* provides a strong incentive for California employers to use opt-out provisions in an effort to avoid facing class liability.¹

Insulating unconscionable terms from court review

A second potential harm to employees who fail to opt out is that they may be foreclosed from challenging provisions that would otherwise be struck down as unconscionable. The Ninth Circuit recently held that the presence of an opt-out clause prevented a finding of procedural unconscionability. See *Mohamed v. Uber*, _ F.3d _, 2016 WL 4651409 (9th Cir. Sept. 7, 2016).² Because substantively unconscionable provisions may not be used to invalidate a contract unless there is also some degree of procedural unconscionability, courts may allow the mere presence of an opt-out clause to insulate substantively unconscionable provisions from court review. As a result, provisions that have long been held substantively unconscionable may now be imposed upon employees simply because they fail to discover and take affirmative steps to exercise an opt-out right.

The Ninth Circuit appears to be taking a more extreme position on this issue than California law would support. The California Supreme Court, in (*Gentry v. Superior Court* (2007), 42 Cal.4th 443) held that a contract was procedurally unconscionable even though it contained an opt-out provision, but recent Ninth Circuit decisions have not taken *Gentry* into account. If this trend continues, it will result in federal courts giving a seemingly unjustifiable level of protection to substantively unconscionable contract provisions merely because an opt-out clause is buried in the contract, even when normal indicia of procedural unconscionability are present.

Using opt-out provisions to avoid PAGA claims

One type of group claim that employers have failed to eliminate through the use of opt-out provisions is representative claims under the Private Attorneys General Act (“PAGA”), (Cal. Lab. Code, § 2699 et seq.) Both the California courts and the Ninth Circuit have recently held that blanket waivers of representative PAGA claims in arbitration agreements (i.e., waiving the right to bring such claims in arbitration and the right to bring them in court) are unlawful, and both have also rejected employer arguments that the presence of an opt-out provision cures the illegality. (See *Sakkab v. Luxottica Retail N.A., Inc.* (2015) 803 F.3d 425 *Securitas Sec. Servs. USA, Inc. v. Super. Ct. of San Diego Cnty* (2015) 234 Cal.App.4th 1109.) The courts have reasoned that blanket PAGA waivers are impermissible because the Legislature enacted PAGA to empower employees to enforce the Labor Code as representatives of the state, and permitting private parties to enter into pre-dispute waivers of that power would frustrate public policy.

Opt-outs and smartphone “contracting”

The fact that many putative contracts are now entered into by the tap of the screen on a smartphone increases certain hazards for employees by making it easier for employers to “roll out” new contract terms that are unfavorable to the employee. Moreover, a smartphone is less conducive to reviewing a dense, lengthy document. For example, in the smartphone-based sharing economy, in which the main form of interaction between workers and the company is via smartphone app, the company can simply update its terms and require the worker to “click” to accept them before receiving another assignment.

It is, of course, a fiction that workers will review and digest the lengthy and complex agreement, understand how it differs from the prior agreement, and decide whether to accept the new terms. In reality, they will simply click “accept” so that they can continue working. If the updated agreement adds an opt-out provision, the worker may just have unknowingly “clicked” away his or her right to engage in future collective claims against the company.

On the other hand, this evolving technology may give rise to new opportunities to attack arbitration agreements. When individuals are asked to accept terms of which they have not had fair notice, the issue of contract formation can be fertile grounds for a challenge. (See, e.g., *Segouros v. TransUnion Corp.* (7th Cir. 2016) 817 F.3d 1029 (consumer did not assent to service agreement containing arbitration clause by clicking “I Accept” button on website). Helpfully for plaintiffs, courts “do not apply the so-called ‘presumption in favor of arbitrability’ . . . [when] the parties contest the *existence* of an arbitration agreement . . .” (*Goldman, Sachs & Co. v. City of Reno* (9th Cir. 2014) 747 F.3d 733, 742.) In addition, the burden is on the

employer, as the party seeking to enforce the contract, to prove by a preponderance that a valid contract was formed. (*Ashbey v. Archstone Prop. Mgmt., Inc.* (9th Cir. 2015) 785 F.3d 1320, 1323.)

The more clearly a plaintiff's attorney can illustrate for the court how the employer used the new technology to ensure that the employee would be unlikely to learn of the opt-out agreement, the greater the chances of establishing procedural unconscionability. As aggressive as the Ninth Circuit has recently been in allowing opt-out provisions to remove plaintiffs' rights, its decisions can be read to show that the door is still open for arguments that opt-out provisions were unfairly buried in an agreement. (See, e.g., *Kilgore v. KeyBank, Nat'l Ass'n* (9th Cir. 2013) 718 F.3d 1052, 1059 (noting that arbitration with opt-out provision was not "buried in fine print").)

The future of *Morris* and the likely growing use of opt-out clauses

The Circuits are split on the applicability of the NLRA to class-action waivers in arbitration agreements. The *Morris* decision puts the Ninth Circuit and the Seventh on one side of the split (notwithstanding their disagreement about the effect of an opt-out provision), and the Second, Fifth, and Eighth Circuits on the other, with petitions for *certiorari* now pending in four of the cases.³ The issue is also pending and fully briefed in the Fourth, Sixth, Eleventh, and D.C. Circuits. Given the great importance of the issue, it is likely that the Supreme Court will soon settle the question. If the Supreme Court agrees that blanket class waivers violate the NLRA, the question of whether an opt-out provision cures that violation will take on even greater importance.

There are good reasons to believe that the Supreme Court will affirm *Morris*.

First, *Morris* undoes much of the harm to employment class actions in California that was caused when the Supreme Court held that the Federal Arbitration Act ("FAA") preempted California courts' prohibition on many class-action waivers as unconscionable, (see *AT&T Mobility v. Concepcion* (2011) 563 U.S. 333), and the four dissenting votes in *Concepcion* (Justices Ginsburg, Breyer, Sotomayor, and Kagan) now make up half of the Court. They may soon be joined by a new colleague who, like them, reads the FAA less expansively than the *Concepcion* majority did.

Second, the Supreme Court has been presented with a circuit split in which the reasoning of two Circuits holding that class waivers violate the NLRA, *Morris* (9th Cir.) and *Lewis* (7th Cir.), provides a rigorous explanation of why the earlier decisions by other Circuits going the other way, some of which addressed the issue in little depth, are incorrect. The most recent circuit to confront this issue, the Second Circuit, stated that it "might well be persuaded, for the reasons forcefully stated in Chief Judge Wood's and Chief Judge Thomas's opinions in *Lewis* and *Morris*, to join the Seventh and Ninth Circuits and hold that [a class] waiver . . . is unenforceable under the NLRA," but the court was constrained by a prior Second Circuit panel's decision. (*Patterson v. Raymors Furniture Co., Inc.*, 2016 WL 4598542, at *2 (2d Cir. Sept. 2, 2016) (petition for cert. filed Sept. 26, 2016) (U.S. No. 16-388).)

Morris and *Lewis* examine the language of the NLRA and the FAA, explain that the FAA's savings clause preserves contract defenses to arbitration agreements 'upon such grounds as exist

at law or in equity,’ 9 U.S.C. § 2, and conclude that the right to concerted action in the NLRA is a ground existing in law. (See, e.g., *Lewis*, 823 F.3d at 1158 (the “savings clause ensures that . . . there is no irreconcilable conflict between the NLRA and the FAA.”) This accords with the view of the NLRB. The decisions rejecting the NLRA argument fail convincingly to harmonize the statutory language or undermine the reasoning of the Seventh and Ninth Circuits and the NLRB.

The California Supreme Court, however, reached a different conclusion from *Morris* in 2014, holding that a class waiver was not unlawful under the NLRA. (See *Iskanian v. CLS Transp. Los Angeles, LLC*, (2014) 59 Cal.4th 348, 367-74.) At the time *Iskanian* was decided, no federal court of appeals had adopted the NLRB’s view that class waivers violate the NLRA, and the arbitration agreement in *Iskanian* left room for joint and consolidated claims in arbitration, unlike many blanket class and collective action waivers. (*Id.* at 374.) Still, as a strategic issue, plaintiffs’ class action employment attorneys considering where to file a case should note that the California Supreme Court has been less favorable than the Ninth Circuit on the NLRA issue (*Iskanian*) but more favorable on courts’ ability to find procedural unconscionability notwithstanding the presence of any opt-out provision (*Gentry*).

Going forward, even if opt-out clauses remain a valid tool for employers, some employees (likely only those who have a lawyer) will actually succeed in opting out. This raises additional questions. For example, when an employee succeeds in opting out of an arbitration agreement with a class waiver and then seeks to bring a class action on behalf of his co-workers, most of whom have *not* opted out, will courts allow the opt-out to proceed collectively on behalf of the whole group? This issue is beginning to be explored in the courts. (See, e.g., *Bickerstaff v. Suntrust Bank* (Sup. Ct. Ga. 2016) 788 S.E.2d 787 (named plaintiff’s timely rejection of arbitration tolled the opt-out deadline for putative class members) (petition for cert. filed Oct. 7, 2016) (U.S. No. 16-459).)

Opt-outs are the latest chapter in the long story of employers seeking ways to insulate their practices from classwide challenge, and plaintiffs seeking ways to ensure that they and their colleagues have effective tools for enforcing the employment laws.

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Subject Matter Index

[Class Actions](#), [Employment - In General](#)

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