Calif. PAGA Ruling Devalues Arbitration For Employers

By **Lindsay Hutner, Sam Hyde and Taylor Hall** (July 26, 2023)

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The California Supreme Court's July 17 ruling in Adolph v. Uber Technologies Inc. was perhaps one of the most anticipated employment law rulings this year.

In its opinion, the court ruled that a named plaintiff in an action under California's Private Attorneys General Act maintains standing to pursue PAGA penalties on behalf of other allegedly aggrieved employees, even if the plaintiff's individual claims are compelled to arbitration under the Federal Arbitration Act.[1]

Pursuit of PAGA penalties on behalf of other allegedly aggrieved employees are known as nonindividual or representative PAGA claims.

This decision purports to resolve the standing question left open by the U.S. Supreme Court's 2022 decision in Viking River Cruises Inc. v. Moriana.

California Supreme Court Justice Goodwin Liu, writing for a unanimous court, concluded that standing under PAGA turns on the statutory definition of an "aggrieved employee."[2] The court reasoned that a PAGA plaintiff need only show that they: (1) were employed by the alleged violator; and (2) allegedly suffered a violation of the Labor Code.

Standing is not undone, the court ruled, if the plaintiff's own claims are sent to arbitration. The court further held that a plaintiff's aggrieved status is not altered by defenses proven by the defendant — other than those that show the plaintiff was not aggrieved — including a prior release of the PAGA claim by the plaintiff, or individual recovery being barred by the statute of limitation.

The court also clarified how the course of individual arbitration could alter the standing calculus. Only if the arbitrator determines the plaintiff is not an aggrieved employee — i.e., suffered no violation of the Labor Code at any time in the course of the plaintiff's employment, including before the limitation period — will the plaintiff lose standing to pursue a nonindividual action in superior court. [3]

Thus, from the employer's perspective, it will not be enough to simply win in arbitration against the named plaintiff. To stop the nonindividual action, the employer may have to set aside all affirmative defenses it could normally assert against liability toward the individual named plaintiff and litigate the core issue of whether a Labor Code violation occurred at any time — effectively limiting its defense to a rebuttal of the plaintiff's case-in-chief.

This aspect of Adolph dramatically expands traditional notions of standing. It promotes an individual plaintiff's ability to litigate PAGA claims on behalf of other aggrieved employees even where that plaintiff has no chance of recovery — and may have even expressly released his or her PAGA claims.

This holding is no doubt significant for employers, especially those who may have settled individual PAGA claims or have other successful affirmative defenses at arbitration. Indeed, successful defenses in arbitration that do not go to the plaintiff's aggrieved status will seemingly not defeat the plaintiff's ability to persist in pursuing claims concerning violations toward others.

This holding also undercuts the value of compelling an individual PAGA claim to arbitration. Arbitrating most individual PAGA claims to conclusion will likely only result in a Pyrrhic victory for employers — unless the plaintiff's nonaggrieved status is proven, employers will likely have to face the challenge of relitigating the same issues with the same plaintiff in superior court. Employers will surely need to evaluate early on the wisdom of arbitrating or settling individual PAGA claims at all.

Adolph's standing analysis also leaves a door open to federal preemption arguments. Where an arbitration is resolved based on a procedural defense — as opposed to aggrieved status — it is left to the state court to resolve whether the named plaintiff is an aggrieved employee.

But that issue likely falls within the parties' agreement to arbitrate. Such a result may frustrate a party's contracted-for rights under the Federal Arbitration Act and may be subject to preemption.

Implications for Employers

Complete compliance with the Labor Code is challenging, even with the best planning and counseling. Even where fully compliant, an employer may be sued based on ambiguous Labor Code requirements.

Prevention of a PAGA action is the best cure. As a starting point, employers should review and confirm that their current wage and hour practices and policies comply with the Labor Code. If not, update them.

Providing refresher training to employees and managers on Labor Code compliance is also wise. Additionally, employers should use a Donohue protocol — which stems from the California Supreme Court's 2021 decision in Donohue v. AMN Services LLC — to deter meal-period claims and the like.

In this latter regard, well-intentioned employers sometimes use employee-friendly practices that actually encourage class or collective actions. Automatic payment of meal-period premiums for facially noncompliant time punches may be argued by a plaintiff to be a concession of, and common proof of, actual violations, allowing recovery beyond the paid meal-period premium, including PAGA penalties.

As importantly, employers should avoid any compensation practice the legality of which may involve judgment calls. Use of bonuses to incentivize particular behaviors is a prime example.

Such bonuses may need to be factored into the regular rate of pay, which is used for calculating overtime, meal, rest and sick pay. If they are factored in, the correct formula to calculate the regular rate may vary based on additional factors. Though often viewed as generous benefits to employees, such practices can be a magnet for lawsuits. Simplicity may lead to less litigation.

When a PAGA notice arrives, employers' counsel should quickly assess areas of concern and identify a go-forward strategy — including, where appropriate, whether to settle early, move to compel arbitration or proceed in court.

Conclusion

When it comes to PAGA claims, Adolph may lessen employers' collective appetites for individual arbitration. Unless an employer is confident it can prove the employee did not suffer a Labor Code violation at any point during his or her employment, arbitrating the named plaintiff's PAGA claims is unlikely to dispose of the nonindividual claims.

Employers will be forced to bear the considerable costs of individual arbitration only to wind up back in court. As Adolph stands, individual arbitration agreements may be a less effective tool in defending against PAGA actions as we move into the back half of 2023.

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[1] Adolph v. Uber Techs., Inc., No. S274671, 2023 WL 4553702 (Cal. July 17, 2023).

[2] See Cal. Lab. Code § 2699(c).

[3] Adolph, 2023 WL 4553702, at *8.