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ARTICLE

Uber v. Heller: Supreme Court applies the law of unconscionability to arbitration agreements and identifies a new role for the Court

In *Uber Technologies Inc. v. Heller*, 2020 SCC 16, issued on 26 June 2020, a majority of the Supreme Court of Canada invalidated the arbitration agreement between Uber and drivers who subscribe to Uber's ride or delivery-origination software.

The key points are:

- The majority of the Court identified a new exception to the rule of systematic referral to arbitration when applications are brought to stay legal proceedings that may be subject to an arbitration agreement, allowing the court to decide the matter when there is a real prospect that, if a stay is granted, the challenge may in fact never be resolved by the arbitrator.
- The majority significantly expanded the scope of the concept of unconscionability in the law of contract, particularly in the context of standard form contracts or contracts of adhesion, which are prevalent in the modern transactional economy.
- The majority left undisturbed the Court of Appeal for Ontario's finding that an arbitration agreement covering employment-related claims may amount to an unenforceable attempt to contract out of Ontario's *Employment Standards Act, 2000* (ESA).
- Parties should promptly assess their existing arbitration agreements, particularly those found in standard form contracts, to ensure that they are consistent with the approach taken by the majority of the Court and will remain enforceable.

The implications of *Heller* are likely to be far-reaching. In this bulletin, we will summarize the Court's judgment and then assess some of those implications, concluding with certain practical steps that may be necessary to address its potentially adverse effects.

Background

David Heller (Heller) entered into several agreements with Uber Technologies Inc. and its affiliates (Uber) in order to access Uber's ride or delivery-origination software. The agreements between Uber and Heller contained arbitration clauses requiring mediation and then arbitration, pursuant to the arbitration rules of the International Chamber of Commerce (ICC Rules). Amsterdam was named as the "place of arbitration."

Heller sought to bring a class action on behalf of Uber drivers seeking, among other remedies, a declaration that he and the other drivers are employees of Uber and, therefore, entitled to benefits under the ESA. Uber moved to stay the legal proceeding in favour of arbitration.

Divided Results in the Ontario Courts

In the Ontario Superior Court of Justice, Justice Perell stayed the legal proceeding in favour of arbitration. He found that the Ontario *International Commercial Arbitration Act* (ICAA) applied because the dispute was both international and commercial in nature. Justice Perell concluded, consistent with prevailing authority, that:

- Courts must enforce arbitration clauses that are entered into freely, unless prohibited by legislation, and that the ESA did not prevent the parties from arbitrating the dispute; and
- Notwithstanding the unequal bargaining power between the parties, Uber had not preyed upon or taken advantage of Heller in a manner that would have made the arbitration agreement unconscionable.

The Court of Appeal for Ontario reversed Justice Perell's judgment. In respect of the two principle issues identified above, the Court found that:

- The arbitration agreement was invalid as an illegal contracting out of the ESA. In making this finding, the Court determined that the "competence-competence" principle, which grants an arbitral tribunal the power to rule first on its own jurisdiction, was inapplicable to situations in which the validity of the arbitration agreement itself is challenged; and
- Even if the arbitration clause was not invalid as an illegal contracting out of the ESA, it was nevertheless invalid on the basis of unconscionability. In reaching this decision, the Court focused on (among other things) the potentially prohibitive cost of initiating arbitration under the ICC Rules and its apparent impression that, with Amsterdam deemed the legal "place of arbitration," the arbitration hearing would actually take place there.

Uber was granted leave to appeal to the Supreme Court of Canada.

Supreme Court of Canada's Judgment

The judgment of the majority of the Court was delivered by Abella and Rowe JJ, with Brown J concurring and Côté J dissenting.

Applicable Statute

On the issue of the applicable arbitration statute, the majority observed that s. 5(3) of the ICAA states that the Model Law applies to an "international commercial arbitration agreement". However, rather than only assessing the nature of the "arbitration agreement", the majority went on to characterize the nature of the parties' dispute, which it found could be done by examining the pleadings and assuming that the material facts they asserted were

true. On that basis, the majority found that the dispute did not concern an international commercial arbitration agreement, but rather engaged considerations of an employment relationship. Accordingly, the domestic *Arbitration Act 1991* was found to apply, as the relationship was not "commercial" in nature.

Jurisdiction to Determine the Validity Issue

Applying the *Arbitration Act, 1991*, the majority of the Court identified five grounds upon which the court may decline ordering a stay of court proceedings, including where the arbitration agreement is invalid. While affirming the Court's judgment in *Dell Computer Corp. v. Union des consommateurs*, 2007 SCC 34, [2007] 2 S.C.R. 801, which requires the referral of challenges to the arbitral tribunal "unless they raise pure questions of law, or questions of mixed fact and law that require only superficial consideration of the evidence in the record", the majority identified a new exception to the rule of systematic referral to arbitration.

This new exception was stated to apply in "abnormal" circumstances where there is a *bona fide* challenge to the arbitrator's jurisdiction that only the court can determine.

This new exception appears to require an assessment of two questions:

- Assuming the facts pleaded to be true, is there is a genuine challenge to arbitral jurisdiction?
- From the supporting evidence, is there a real prospect that, if the stay is granted, the challenge may never be resolved by the arbitrator?

Having found that Heller posed a genuine challenge to the validity of the arbitration agreement, the majority considered the second question. It found that the fees required by the ICC Rules to constitute a tribunal to hear the jurisdictional challenge, among other factors, resulted in a real prospect that Heller's arguments on jurisdiction would never be heard. It therefore considered that this was not a case in which the rule of systematic referral to arbitration should be applied, and that the court should instead determine the question of the validity of the arbitration agreement for itself.

Validity of the Arbitration Agreement

Having rebutted the presumption that challenges to arbitration agreements would be systematically referred to the arbitrator, the majority turned to the substantive challenge. Heller challenged the validity of the arbitration agreement on two grounds relating to (i) an alleged illegal contracting out of the ESA and (ii) unconscionability.

The majority determined the question on the second ground and did not find it necessary to reach the issues arising in respect of the ESA. The majority set out a two-part test to determine whether a contract (or, it appears, even a provision within a contract) is unconscionable. The test requires:

- Proof of inequality in the positions of the parties; and
- Proof of an improvident bargain.

This test appears to differ from the prevailing conception of unconscionability, because it does not require constructive or objective knowledge of the vulnerable position of the contracting party by the allegedly "stronger" contracting party, nor does it require an assessment of whether the "stronger" contracting party exploited or took unfair advantage of its counterpart. The focus seems to simply be on the apparent (and, notably, retrospective) wisdom of the bargain that was struck between two parties in unequal positions.

On the first branch of the test, the majority of the Court found that there was an inequality in bargaining power between Uber and Heller. Among other things, the majority relied on the fact that the contract was a standard form agreement that Mr. Heller had no ability to negotiate, there was an apparent gulf in sophistication between the parties, and the arbitration agreement did not spell out the details of mediating and arbitrating disputes under the ICC Rules, nor did it contain an explanation of Dutch law.

On the second branch of the test, the majority considered an improvident bargain to be one that, in the court's view, unduly advantages the stronger party or unduly disadvantages the weaker party. The majority found that the fees required by the ICC Rules were prohibitive to Heller based on (i) his income, (ii) their disproportionate size as compared to any foreseeable award, and (iii) the "impression" that the arbitration agreement provided that the arbitration would take place in the Netherlands.

Concurring and Dissenting Judgments

It is worth noting the concurring and dissenting decisions of Brown J and Coté J, respectively.

Brown J reached the same conclusion as the majority, but identified a narrower basis for that result, and one that did not require revising the law of unconscionability: the arbitration agreement was simply invalid because it was inconsistent with the public policy imperative to provide meaningful access to justice before an actual decision-maker. The problematic aspects of the arbitration agreement identified by the majority, he reasoned, engaged this basic principle, which made it wholly unnecessary to find that the arbitration agreement was unconscionable, or to redraw the limits of that concept.

Coté J dissented. She found that the ICAA was applicable, because, among other things, the focus of the statute is on the nature of the arbitration agreement, not the facts pleaded in support of a later-arising dispute. She also applied the conventional jurisprudence the Supreme Court of Canada has recently developed to support arbitration as an element of the system of civil justice, in particular the rule of systematic referral to arbitration, and found that no exception to that rule had been made out. In particular, she found, Heller's claim required more than a superficial review of the record, such that it should be left to the arbitrator to determine.

Coté J disagreed with the majority's approach to the concept of unconscionability, holding that it set the bar too low, especially given the prevalence of standard form contracts and the implications for the "gig" economy. She also held that the majority's reasons for finding that the bargain struck by Heller and Uber was improvident did not withstand scrutiny: the "place of arbitration" is not a reference to having a hearing in a particular place, but rather to the jurisdiction whose laws will govern the proceedings, the application of foreign law to the substantive agreement was separate from the alleged unfairness of the separable arbitration agreement, and the fees were payable by any party that commenced arbitration (and it would require evidence to determine unfairness).

However, finding that the court has a broad remedial jurisdiction to facilitate the arbitration process, she would have ordered a conditional stay, which would have required Uber to advance to Heller the funds required to initiate the arbitration, subject to a final order as to costs by the arbitrator. This approach would require the parties to abide by their commitment to arbitrate their disputes, while providing recourse against certain problematic aspects of the way in which they implemented that commitment.

Analysis and Practical Implications

This case raises important issues for the practice of arbitration in Canada and for the operation of contract law generally, but especially in respect of standard form contracts.

Arbitration Practice

The decision to apply the domestic *Arbitration Act, 1991*, to this case has two consequences. First, it clearly excludes employment matters from "commercial" disputes for the purposes of the ICAA. As a result, international companies that contract with employees in Canada can expect their arbitrations to be governed by the domestic arbitration statutes, which are unique to each province and arguably exclude the international standards envisaged by the ICAA. Second, future international arbitrations under the ICAA or its counterparts in the common-law provinces may be partially insulated from the approach taken in this case. Unlike the Court of Appeal for Ontario, the majority did not confirm that the outcome of the case would be the same regardless of the applicable statute.

It is also useful to consider how this issue would be approached in Québec, under its civil law system. Under Québec private international law, characterizing the contract between Uber and Heller as an employment contract would trigger the application of Article 3149 of the Civil Code of Québec (CCQ), which prohibits agreements to waive the jurisdiction of domestic courts in employment contracts and consumer contracts.

Since it was not disputed that the contract between Heller and Uber was international, Article 3149 could have prohibited the operation of the arbitration agreement in any event. Given Article 3149, parties contracting with persons in Québec should be reminded that the validity of their arbitration agreements will likely depend on the characterization of the substantive contract in which the arbitration agreement is found.

For domestic arbitrations, the majority was evidently concerned about the possibility that its decision to expand the grounds for rebutting the rule of systematic referral to arbitration could invite dilatory tactics. The majority articulated "ways to mitigate this concern", such as security for costs, full indemnity costs where a party ignores arbitral jurisdiction, and damages for breach of contract (*i.e.* a valid arbitration agreement). While it will be important to monitor the development of these potential "mitigating" practices, to the extent they are workable in reality, the result in this case emphasizes the need for parties to ensure that their arbitration agreements are clearly drafted, workable, and valid.

Doctrine of Unconscionability

This case will also have a significant effect on the application of the doctrine of unconscionability in Canada.

This is particularly so given the factors the majority relied upon to find unconscionability and the finding that it is no longer necessary to demonstrate either objective or constructive knowledge of a counterparty's vulnerability or an element of intentional "advantage-taking" before invalidating an agreement, or parts of it, as being unconscionable.

As explained by Brown J, "the stakes are high here. Concluding that a standard form contract is sufficient to satisfy unconscionability's procedural requirement would open up the terms of every such contract for review on a measure of substantive reasonableness." There is much to be said in support of Brown J's assessment that the majority's decision "drastically expands the scope of unconscionability" and "provides very little guidance for the doctrine's application".

Nevertheless, the approach of the majority is now the law, and it will be necessary to address how it operates in practice. The majority appears wary of the potential for standard form contracts to "create an inequality of bargaining power" and highlights in particular "choice of law, forum selection, and arbitration clauses that violate the adhering party's reasonable expectations by depriving them of remedies".

In navigating this new rule, there is likely to be a heightened focus on ensuring the "accessibility" of standard form contracts. In order to avoid a finding of invalidity, the majority encouraged drafters to "to make them more accessible to the other party or to ensure that they are not so lop-sided as to be improvident, or both."

Québec's civil law approach is not dissimilar. Abusive clauses in a consumer contract or a contract of adhesion may be invalid (Article 1437 CCQ). Québec courts usually defer the analysis of whether an arbitration clause was abusive to the arbitrator, in accordance with the prevailing rule of systematic referral to arbitration. (See, for instance, *Groupon Canada Inc. c. 9178-2243 Québec Inc.*, 2015 QCCA 645 applying *Rogers Sans-fil Inc. c. Muroff*, 2007 CSC 35 (CanLII), [2007] 2 RCS 921, para. 15). The majority's analysis may well encourage Québec courts to further scrutinize dispute resolution clauses in standard form contracts with regard to their fairness and equity.

Resolving Employment Law Disputes

Having reached its decision on the basis of unconscionability, the majority of the Court expressly declined to address the question of arbitration agreements in the context of the ESA.

Parties are therefore left with the decision of the Court of Appeal for Ontario, which held that the exclusive arbitration provision under the contract deprived an individual of certain procedural rights under the *ESA* and, on that basis, was invalid. Courts typically apply this principle to overtime agreements, hours of work agreements and, most often, termination provisions that attempt to limit an employee's rights to statutory minimums on termination.

Across the country, particularly in Ontario, a virtual cottage industry has grown up attacking termination provisions on the basis that they provide less than minimum statutory entitlements. Courts take a narrow reading of contractual provisions that address employment standards, viewing employment standards legislation as remedial and intended to protect the interest of employees. In termination cases, courts are reluctant to deprive employees of their common law entitlements.

What makes *Heller* unique, at least at the Court of Appeal, is that it applies the basic employment law principle in the context of an arbitration provision and the deprivation of procedural rights under the *ESA*, as opposed to a substantive right. Increasingly, employers are including arbitration provisions in employment contracts. The practice, widespread in the United States, is slowly picking up steam in Canada. In drafting these provisions, lawyers must ensure that procedural rights under the *ESA* and, for that matter, other statutes such as human rights statutes, are preserved.

The decision is unlikely to open the floodgate to claims that individual employment contracts in Canada are unconscionable. Most individual employment agreements reflect some bargaining between the parties, do not contain onerous arbitration provisions and are enforceable in the province in which they are entered. While there is a perception that employers hold greater bargaining power over employees, this is often a misconception in many sectors of our economy.

Class Proceedings

The judgment of the Supreme Court devotes comparatively little attention to the interaction between arbitration clauses and class proceedings. Indeed, Brown J observed that, "[w]hile Mr. Heller may be able to pursue a class action by combining his claim with other individuals in a similar position, that is of no moment here."

It is true, as Brown J goes on to note, that class proceedings legislation is procedural in nature and is not intended to alter substantive rights. While consumer protection legislation in various provinces invalidates arbitration clauses to the extent that they would apply to "consumers", the Supreme Court has held previously that, in other contexts, legally enforceable arbitration clauses can preclude parties from participating in class actions (see *Telus Communications Inc. v. Wellman*, 2019 SCC 19).

Future cases will have to decide whether the enforceability of an arbitration clause is an individual issue that must be answered separately for each class member or group of class members, or can be determined on a class-wide basis.

Conclusion

It will be important to monitor the application of this judgment to future arbitration agreements in Canada, but there are certain steps that parties should take now:

- Review existing arbitration agreements, particularly in employment contracts, contracts with parties with weaker bargaining positions, or standard form contracts of adhesion, and assess the clarity and accessibility of the dispute resolution procedures that have been adopted.
- Consider whether it is appropriate and possible to tailor the arbitration agreement in such contracts to, for example, expressly provide:
  - that hearings will be held at a location near the counterparty (or to be selected by them);
  - that hearings will be held virtually;
  - that the filing and other costs of low-value claims will be paid or subsidized by the party in the stronger position; and
  - other steps that increase the accessibility of arbitration as a practical dispute resolution mechanism.

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