

EMPLOYEES IN THE WORKPLACE

Expert Analysis

Mandatory Arbitration: Searching for Fairness

Some things in life are just not fair. We learn that when we are very young. The bigger kid gets on the team, the more attractive kid becomes class president, and the kid with more money gets to have nicer things. We accept those realities even when we try to fight them. Arbitration, particularly as it is practiced in employment law, is not all that different. It is an unfair system that is forced or imposed on employees and consumers while disregarding our civil rights and liberties in favor of an abbreviated, and at times perverse, form of justice.

This is because arbitration lets employers contract around the procedural and substantive protections we enjoy in court. Through an employment contract, an employer can limit or eliminate an employee's access to discovery, shorten the statute of limitations for claims, and create the risk that the plaintiff may have to pay the defendant's attorney fees. All of this happens in a forum that, because of the deferential standard accorded to arbitration awards, is unaccountable to appeal or to the law.

Arbitration has become more widespread and more prevalent

By
**Wendi S.
Lazar**



in employment agreements and has been made a part of many a company's employment policy—even when the employee does not have an employment agreement or any other protection. In certain circumstances arbitration can be extremely productive, cost-efficient and expedient for the employee. For example, it can be preferable in a contract dispute where there are no civil rights issues at stake, nor attorney fees available, and has been employee-friendly in the financial services industry where regulated employees can participate in FINRA arbitrations to settle bonus claims and other equitable claims that otherwise would not be well received in New York courts on the law. However, forced arbitration in discrimination cases, where the plaintiff employee would otherwise have had existing federal rights and remedies (both statutory and common law), and the right to be heard in a federal court with a federal judge and the right to appeal, is blatantly unjust.

Moreover, employers frequently pay for arbitrations and therefore have come to provide financial support for the institutions that provide these services thereby pitting employees against the repeat customers on the employer side. No business (even one that should be non-partisan) will last if it does not keep its repeat customers pleased. While there are brilliant, well-educated arbitrators who are judicious and fair, the current system, by its very nature is skewed against employees by virtue of its pay-to-play system.

FAA and Economic Realities

Approximately 23 years ago, the Supreme Court articulated a strong policy favoring arbitration in the Federal Arbitration Act (FAA) and held that the policy extended to discrimination cases.¹ This made it clear that mandatory arbitration is here to stay. From the lowest wage worker delivering the ever-increasing number of packages we order online, to the managing director on Wall Street, the one thing that ties these employees together is that they will all have an arbitration clause in their contract. For these employees, the question as to whether arbitration clauses are permissible has been fought—and lost.

The economic realities force employees to sign arbitration clauses if they need and want a job. So what are employees to do when faced with

WENDI S. LAZAR is partner and co-chair of the executives and professionals practice group at Outten & Golden. CHRISTOPHER M. MCNERNEY, an associate at the firm, assisted in the research and writing of this article.

an arbitration clause in a job application? The contract (or at least the arbitration clause) will be offered on a take-it-or-leave-it basis, leaving no room to bargain for the right to sue in court—the most basic right assured at one time to every citizen in the United States.

What is worse is that employees are naïve and optimistic—never thinking they will have a legal problem at work or be discriminated against. They trust that they will be paid the minimum wage, the bonuses that they have earned, and the overtime that they worked. They certainly do not go into a job thinking that they are going to sue, or pay much mind to the clause in their contract limiting their ability to do so. In a striking statistic, St. John's University School of Law found that in the consumer context only 43 percent of respondents asked to review a sample contract noticed that it had an arbitration clause. Of those observant few, 61 percent believed that they would still have a right to sue in court despite the arbitration clause. Less than 9 percent realized both that the contract had an arbitration clause and that it would prevent litigation in court.²

These observations also appear to hold true in the employment context. As many plaintiffs' counsel will attest, it is often that a potential employee client only learns she has an arbitration clause (and what that means) in a lawyer's office during the initial consultation.

Defense of Unconscionability

So, what are the defenses against this unfair and inequitable system? Arbitration is still a "matter of contract," as the Supreme Court has consistently reiterated, and that means contractual defenses still apply.³ But if the contract was not entered into through mistake, fraud, or duress, or if there was a meeting of the minds, the main defense that remains is unconscionability.

In New York, to prove unconscionability, the standard is quite demanding. A litigant ordinarily must prove both procedural and substantive unconscionability:⁴ that she was improperly pressured at formation of the contract and lacked meaningful choice, and that the actual terms she agreed to were substantively unconscionable.⁵ Unlike the law in other states, in New York the mere fact that a contract is presented "on a 'take it or leave it' basis" (i.e. that it is a contract of adhesion) is insufficient to render the arbitration clause procedurally unconscionable.⁶

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As to substantive unconscionability, even if a plaintiff can surmount the difficult hurdle of defeating the presumption in favor of arbitrability, and even if the court agrees the provision is unconscionable, the defendant still has the option to waive the offending provision.

At least this is the holding from *Ragone v. Atlantic Video at Manhattan Center*. There, the employer's arbitration clause shortened the statute of limitations for all claims to 90 days after the claim arose and shifted attorney fees to the prevailing party and not just the prevailing plaintiff. Plaintiff argued that both provisions were substantively unconscionable as to discrimination claims⁷—and the U.S. Court of Appeals for the Second Circuit seemed to agree. In a section aptly titled, "A Note of Caution," the circuit stated that it viewed these provisions with "less than robust enthusiasm," and further elucidated its concerns.⁸ However, the circuit still enforced arbitration

because the employer promised to waive the enforcement of the unconscionable provisions.⁹

Declining to Enforce

Ragone was clearly based on New York contractual law. But, some recent cases, removed from the arbitration context, may challenge *Ragone* using very different contractual arguments. In fact, *Ragone* appears to be running counter to at least one emergent trend in New York law where courts are declining to blue pencil contractual clauses that overreach, are unfair or take advantage of the employee, and are simply not enforcing them. Two recent decisions, one in New York state court and one in New York federal court (and both dealing with covenants not to solicit or compete), are illustrative of this point.

First, in *Brown & Brown v. Johnson*, a New York appellate court declined to blue pencil an overbroad non-solicit provision, noting that modifying the provision would "enhance the risk" that employers would use their superior bargaining position to impose unreasonable anti-competitive restrictions "uninhibited by the risk that a court will void the entire agreement."¹⁰ Then, a New York federal court adopted *Brown's* reasoning in declining to enforce an overbroad non-compete.¹¹ *Veramark Techs. v. Bouk* found that a court should reject contracts where the "infirmities are so numerous that the court would be required to rewrite the entire provision."¹²

Together, these cases arguably stand for the proposition that in New York an employer should not be free to impose a facially unreasonable contractual term on an employee without having the clause rejected. Allowing an employer to waive a substantively unconscionable provision in an arbitration clause creates the same sort of improper incentives for an employer to overreach.

A proponent of arbitration will

likely respond with the refrain that there is a “liberal” (or broad) federal policy favoring arbitration.¹³ By this reasoning, cases refusing to blue pencil restrictive covenants stand apart from cases in the arbitration context. Indeed, a recent employer trend is to argue that the broad federal arbitration policy extends to the court’s analysis of severability, and that in light of the FAA a court should strike unconscionable clauses while maintaining the overall agreement to arbitrate.

contractual law outside the context of arbitration arguably are more persuasive precisely because they cannot be accused of having a bias against arbitration. An employer’s argument that an unconscionability finding in the arbitration context reflects precisely the hostility to arbitration that the Supreme Court has disallowed is much more difficult to make when the cases the plaintiff relied upon are outside the arbitration context.¹⁸

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This is effectively an argument that blue penciling should be favored in the arbitration context because of the FAA. (In a recent case litigated by the author’s firm, defendants made just such an argument before the Ninth Circuit, and it was adopted by the dissenting judge.¹⁴)

But such an argument seems to run contrary to *AT&T Mobility v. Concepcion*.¹⁵ There, the Supreme Court held that a California rule that class action waivers in arbitration agreements were unconscionable was preempted by the FAA and the broad federal policy favoring arbitration.¹⁶ The logic behind this holding was that to eliminate past judicial hostility to arbitration (the purported purpose of the FAA), a contract to arbitrate must be treated just like any other contract—and the California law was impermissibly targeted specifically at arbitration contracts.¹⁷ Taking *Concepcion* at its word, cases interpreting

Legislative Solution

All told, if the New York cases discussed above are indeed a trend, then the logic of *Ragone* will have to be reevaluated. But even if that happens, at this point the federal policy favoring arbitration is so entrenched in the courts that a legislative solution is the only way out of the mire. Despite the shibboleth that Congress is broken, recent legislation¹⁹ (and an executive order) may suggest that change is on the way.

Five years after the Franken Amendment and on July 31, 2014, President Barack Obama signed the Fair Pay and Safe Workplaces Executive Order. This order (to be implemented in 2016) will govern federal procurement contracts above \$500,000. It will provide two important changes. First, applicable corporations will have to disclose labor law violations from the last three years before they can

receive a government contract. And second, it will build off the Franken Amendment and direct companies with federal contracts of at least \$1 million that they cannot require that their employees arbitrate disputes under Title VII or related common law torts.

Before mandatory arbitration, employees were already disadvantaged in the United States by at-will employment and the cost of litigation. However, at least they had a choice. Whether we can ever return to a justice system that allows employees to sue in a court of law remains the challenge of employee and constitutional rights advocates and perhaps the single most important employment law issue facing our democracy.

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1. See *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991).

2. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2516432.

3. *AT&T Mobility v. Concepcion*, 131 S. Ct. 1740, 1745 (2011).

4. See, e.g., *Lawrence v. Miller*, 901 N.E.2d 1268, 1270 (N.Y. 2008).

5. *Ragone v. Atl. Video at Manhattan Ctr.*, 595 F.3d 115, 121-22 (2d Cir. 2010) (quoting *State v. Wolowitz*, 568 N.Y.S.2d 131, 145 (1983)).

6. *Ragone v. Atl. Video at Manhattan Ctr.*, 595 F.3d 115, 112 (2d Cir. 2010).

7. *Id.* at 123-24.

8. *Id.* at 125-26.

9. *Id.* at 124.

10. 115 A.D.3d 162, 172 (4th Dept. 2014).

11. *Veramark Techs. v. Bouk*, 10 F.Supp.3d 395, 407 (W.D.N.Y. 2014).

12. *Id.*

13. See, e.g., *CompuCredit Corp. v. Greenwood*, 132 S. Ct. 665 (2012).

14. *Zaborowski v. MHN Gov’t Servs.*, ___ F. App’x ___, No. 13-15671, 2014 WL 7174222 (9th Cir. Dec. 17, 2014).

15. 131 S. Ct. 1740.

16. *Id.* at 1746, 1750, 1753.

17. *Id.* at 1757 (“The [FAA] sought to eliminate that hostility [to arbitration] by placing agreements to arbitrate upon the same footing as other contracts.”) (citation and internal quotation marks omitted).

18. See also *Elite Logistics Corp. v. Hanjin Shipping Co.*, 589 F. App’x 817, 820 (9th Cir. 2014) (“Insofar as an application of state substantive unconscionability rules do not discriminate unfavorably against arbitration, they do not offend the FAA.”).

19. Franken Amendment to the 2009 Department of Defense Appropriations Act. This amendment (signed into law by President Obama in 2009), prohibits certain Department of Defense contractors from enforcing pre-dispute arbitration agreements that require employees to arbitrate claims under Title VII of the Civil Rights Act of 1964 as well as common law torts that relate to sexual assault or harassment.