Despite Legality, Employee Arbitration Pacts Are No Panacea

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June 6, 2018, 12:44 PM EDT


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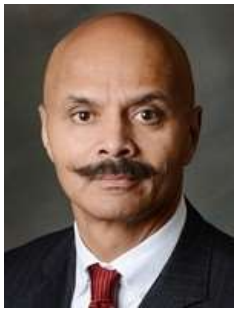
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On May 21, 2018, the U.S. Supreme Court in Epic Systems Corp. v. Lewis, a 5-4 opinion written by Justice Neil Gorsuch, ended a six-year dispute started by the National Labor Relations Board's 2012 decision in D.R. Horton.[1] The board in D.R. Horton held that mandatory arbitration agreements that contain class and collective action waivers violate Section 7 of the National Labor Relations Act. In rejecting the board's reasoning in D.R Horton, Justice Gorsuch wrote that the Federal Arbitration Act instructs that "arbitration agreements providing for individualized proceedings must be enforced" and neither the FAA nor the NLRA suggest otherwise. Therefore, employers do not violate the NLRA if they require workers to forgo the ability to pursue class actions by including the class waiver provisions in arbitration agreements that must be signed as a condition of employment.

While Epic Systems is clearly a business-friendly decision, employers should not rush to include such arbitration agreements and class or collective action waivers in their employment agreements before consulting with counsel. Such agreements and waivers may be beneficial in certain contexts, but they are not necessarily a fit for everyone. Arbitration agreements offer certain benefits. The proceedings and results are typically confidential, which helps an employer avoid bandwagon or copycat claims. Arbitration agreements also allow an employer to avoid litigation, which can be more expensive. However, there are negatives to arbitration as well.

Following are just a few reasons why employers should weigh the pros and cons of arbitration agreements and class waivers before wide-scale implementation.

Requirements in Arbitration

Discovery

Arbitration agreements must be fair to be enforceable. One way to void an arbitration agreement is to prove that it is unconscionable under state law. Unconscionability can be procedural (how the contract was formed) or substantive (the actual terms of the contract). Substantive unconscionability is more likely where the terms of the arbitration agreement are one-sided in favor of the employer or remove certain procedures or safeguards necessary for the employee to bring his or her claim. Thus, even in arbitration, certain procedures are still required.

For example, parties are entitled to discovery of evidence in arbitration, although it may be limited. Even if limited, however, a party must still be able to conduct sufficient discovery to prove his or her claim. If the discovery restrictions are too one-sided, the arbitration agreement may be found to be unconscionable under the relevant state's law. Allowing an arbitrator discretion to order additional discovery may save an otherwise unconscionable arbitration agreement, buy may also negatively impact any contractual limit to costs. What constitutes reasonable discovery depends on the type of case or the facts.

In smaller matters where discovery may already be limited by the circumstances of the case, requiring arbitration may have a negligible effect on the cost or outcome of the case.

Procedure

Another consideration of arbitration versus litigation is that arbitration is streamlined and may not provide certain practices present in litigation that enable parties to narrow the scope of issues before the arbiter. Parties in litigation may bring motions to dismiss or for summary judgment to resolve certain claims or the action entirely. Arbitration rules do not always explicitly provide for the availability of such motions and arbitrators may have discretion over whether to even consider such motions. Because those motions may not be readily available, a party may be forced to defend against all claims — meritorious and frivolous — at a hearing. For example, Rule 27 of the American Arbitration Association's Employment Arbitration Rules addressing dispositive motions states that an "arbitrator may allow the filing of a dispositive motion if the arbitrator determines that the moving party has shown substantial cause that the motion is likely to succeed and dispose of or narrow the issues in the case." The rule clearly gives arbitrators discretion to entertain such motions and does not provide them as a right. Thus, while there may be fewer steps prior to the arbitration hearing versus trial, the hearing may involve more issues and require additional witnesses and arguments that could have been dismissed earlier in litigation.

Available Remedies

Arbitration agreements must provide for recovery of all statutory remedies available to a party in court. The agreement cannot eliminate an individual's ability to bring certain claims or recover certain damages or penalties that would otherwise be available in the court system. This requirement also prohibits shortening a statute of limitations.

State Laws Not Covered

Additionally, some states have statutes that preclude arbitration agreements or avoid class waivers. For example, New York recently passed new legislation prohibiting predispute arbitration clauses for sexual harassment claims. This legislation only prohibits mandatory arbitration agreements where it is not inconsistent with federal law, so the FAA may still preempt the law. California's Private Attorney General Act is not preempted by the FAA because actions under PAGA are technically not class or collective actions and instead are brought by citizens through the state of California.

Cost

A single arbitration in place of litigation — class or individual — may be less expensive for an employer. However, reduced cost as a result of arbitration agreements and class waivers is not guaranteed. Depending on the employer's industry, one class action may be no more expensive to defend than a series of individual arbitrations. Also, one class action can resolve a dispute for all employees in the particular group while individual arbitrations could require constant relitigation of the same issue. Furthermore, even if a favorable result is attained in arbitration, there is no binding precedent requiring the next arbitrator to reach the same conclusion. Thus, in the context where more than one action is possible or likely, a class waiver may not be the best approach for an employer. Depending on the business or circumstances, handling such a dispute on a class basis may be preferable in order to attain a consistent result and improve efficiency, while avoiding the death by a thousand cuts caused by a parade of individual arbitrations.

Unpredictability

Some employers may prefer arbitrators to juries because of a belief that juries are unpredictable and sympathetic toward plaintiffs and employees. While there may be some truth to that belief, arbitrators can be nearly as unpredictable as juries because they are not as tightly bound by the law when making decisions. Furthermore, compared to judges, the range of arbitrator competency is much broader. While some judges are better than others, most are competent and knowledgeable about the relevant subject matter and litigation process, particularly on the federal bench. However, due to the volume of arbitrators with varying substantive backgrounds and experience, the fluctuation in competency from one arbitrator to another can vary widely.

Moreover, an arbitrator's decision is extremely difficult to overturn, even if it is incorrect or includes an error of fact or law. There are limited circumstances in which an arbitrator's decision may be reversed, but the standard is exceedingly high and difficult to overcome. Under the FAA, there are few grounds for appealing an arbitration award, such as serious misconduct or fraud by the arbitrator. Other challenges may be available in limited circumstances, such as the arbitrator deciding an issue that was not present at arbitration, remaking the contract in dispute, upholding an illegal contract, issuing an award that violates a statute or well-defined public policy, or selecting a remedy not authorized by law. If an employer values the ability to appeal an unfavorable decision, mandatory arbitration is not the most desirable option.

Union Implications

Another factor to consider in implementing arbitration agreements and class action waivers is the potential for the agreements to drive employees to a union. Unions are experienced in arbitration and representing a group of employees without requiring a class or collective action. Regardless of the decision in Epic Systems, a union will still be able to collectively represent a class of employees, and do so cost-effectively in a collectively bargained grievance and arbitration process. Preventing employees from using class or collective procedures in the court system may provide a union with an issue with which to organize the workforce. Any gain an employer experiences by avoiding class action litigation may be offset by the increased cost a union brings.

In summary, mandatory arbitration agreements containing class and collective action waivers may be suitable for some employers but not others. Companies should consult with counsel to determine which approach is best suited for their circumstances.

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[1] D.R. Horton, 357 NLRB 2277 (2012).