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Mandatory Pre-Dispute Arbitration: Steps Need to Be Taken to Prevent Unfairness to Employees and Consumers

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Mandatory Pre-Dispute Arbitration

Self-interested critics only spinning truth about a process that has been approved by Congress

By Theodore O. Rogers Jr.

The essence of propaganda – or "spin" as it is often more delicately called – is constant repetition of distortions. The ongoing assault on arbitration of employment disputes represents a textbook illustration of the tactic.

The truth about arbitration is that it is a congressionally approved mechanism for resolution of claims that saves all parties time and expense. Plaintiffs have historically fared better in employment arbitration than in court. The U.S. Supreme Court, in its 1991 decision upholding mandatory arbitration of federal age discrimination cases, *Gilmer v. Interstate Johnson-Lane*,[1] addressed criticisms of arbitration and flatly rejected them, stating that they are "'far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes'."[2]

Those who try to portray arbitration as an unauthorized evasion of the courts ignore the fact that Congress explicitly endorsed arbitration as an alternative forum for the resolution of claims under congressional statutes by enacting the Federal Arbitration Act.[3] In the words of the Supreme Court, the FAA constitutes a "congressional declaration of a liberal federal policy favoring arbitration agreements."[4] Nor does arbitration result in the abrogation of substantive rights. The Supreme Court has confirmed that "'[b]y agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum'."[5]

Those opposing arbitration avoid discussion of the realities of employment litigation in the courts. The courts are overwhelmed by these cases, and the costs of litigating are onerous. A federal judge recently observed that in the

Continued on page 6.

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Steps need to be taken to prevent unfairness to employees, consumers

By Jean R. Sternlight

Courts, arbitral organizations and governmental agencies are increasingly recognizing that mandatory binding arbitration can be used both to disadvantage employees and consumers, and to evade legal requirements. Rather than merely allowing two willing and knowing businesses to achieve a quicker cheaper justice, as Congress intended when it passed the Federal Arbitration Act in 1925,[1] such clauses may permit a knowledgeable and powerful entity to trick or coerce individuals into effectively waiving their rights under federal or state law.

Aggressive policies, practices

For a while it appeared that the lessons most of us learned in civics class – that the legislature makes the law, which the executive enforces and the courts interpret – would be relegated to history. Emboldened by a series of U.S. Supreme Court decisions over the last decade, private parties such as employers, manufacturers and financial organizations began using binding arbitration agreements to skirt the public law, and public juries, with increasing intensity.

The U.S. Supreme Court's decision in *Gilmer v. Interstate/Johnson Lane*,[2] in which the justices rejected facial challenges to the validity of mandatory arbitration of an age discrimination case, in particular seemed to give lower courts the green light to uphold the validity of such arbitration provisions, using supposed "freedom of contract" concepts to insist that employees and consumers had relinquished their rights to go to court.[3]

As a result, a number of companies have forced their new or even current employees to sign documents in which they give up their rights to resolve disputes in courts – and

Continued on page 7.

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Sternlight,
continued from page 5.

typically before juries – as a condition of their future or continued employment. Then, when such employees seek to resolve contractual, statutory, or even civil rights claims against their employers, they are told that the suits can only be brought in arbitration, from which there is effectively no appeal.

Serious issues of coercion and unconscionability aside, at least affected employees typically are given something to sign, even if just an acknowledgment of receipt of a company handbook! Consumers too often haven't been afforded even that much of late. Last year, in *Hill v. Gateway 2000, Inc.*,[4] for example, the 7th U.S. Circuit Court of Appeals deemed purchasers of Gateway computers to have waived their rights to go to court when, unbeknownst to the consumers, the computers they purchased by phone arrived in a box also containing a lengthy warranty that included an arbitration provision on page 3 paragraph 10. In 1994, a state Superior Court in California similarly held that depositors who kept their money at Bank of America exchanged their rights to litigate for binding arbitration merely because they received, in an envelope containing other materials, an announcement from the bank providing in fine print that all future claims must be arbitrated.[5]

Drafters of such clauses claim that they benefit employees and consumers as well as the employers, manufacturers, banks and service providers who typically prepare the provision. They argue that arbitration is quicker and cheaper than litigation and that both disputants and the public at large will be better off if we trade in our right to litigate for binding arbitration.

Major flaws in argument

While binding arbitration potentially can be faster and cheaper than litigation, there are at least three major flaws with this argument. First, binding arbitration necessarily lacks the publicity, the jury trial and the right of appeal that are fundamental to our system of justice. Few of us could imagine or would wish to live in a society in which important issues of public policy were exclusively resolved in private, and virtually without appeal.

Second, drafters of arbitration clauses will inevitably be tempted to use arbitration clauses to provide themselves with various unfair advantages. For example, such clauses have been structured to allow disputes to be resolved by biased panelists, to *increase* claimants' dispute resolution costs compared to litigation by imposing high arbitration fees or setting the arbitration in a distant location, to shorten claimants' statutes of limitation, or to limit the types of relief that can be afforded to claimants, such as the availability of punitive or compensatory damages. Recognizing that arbitration can at times be more costly and less effective than litigation, drafting parties have sometimes reserved to themselves the option to litigate claims important to them, while limiting the consumer or franchisee to arbitral remedies.[6] Sadly, too many of such clauses have been upheld by too many courts.

If binding arbitration is indeed as wonderful and fair as its advocates claim, why make it mandatory? Why not provide adequate notice and explanations to inform actual and meaningful party choice?

Third, if binding arbitration were indeed always as wonderful and fair as its advocates claim, why make it mandatory? Why not allow employees, consumers or others to choose arbitration over litigation knowingly, after the dispute has arisen? Why not agree to place waivers of litigation and jury trial rights in bold writing, and to provide adequate explanations to persons who are exchanging their day in court for private arbitration? The frequently made response – that plaintiffs' lawyers will trick or coerce their clients into rejecting arbitration in favor of litigation – simply makes no sense. Even assuming such attorneys are unethical and willing to sacrifice their clients' interests to their own, why would attorneys operating on a contingent fee prefer a more costly and more time consuming remedy? They don't! Where binding arbitration is truly fair it is well accepted by plaintiffs' counsel. However, such attorneys do oppose unfair arbitration, as they should.

Time of retrenchment

As so often happens, over-reaching may once again be giving way to retrenchment, as the tide seems to be turning away from the "anything goes" approach of the earlier 1990s.

As a policy matter, the federal Equal Employment Opportunity Commission,[7] the federal Dunlop Commission[8] and a number of arbitration organizations – including the National Academy of Arbitrators[9] – have come out in opposition to mandatory binding arbitration imposed on employees. Numerous other groups of arbitrators have urged or required their members not to participate in arbitration that does not meet certain minimum due process requirements.[10]

Some courts, too, have begun to cut back, using a variety of techniques to strike at least the worst of such clauses. Several have voided egregious clauses on contractual grounds, such as unconscionability[11] or lack of consideration.[12] Others have refused to uphold pre-dispute "agreements" to arbitrate claims under specific federal statutes, such as Title VII, unless those agreements meet certain procedural[13] or substantive requirements.[14] This

spring, federal courts on both coasts went even further, holding that job bias claims under Title VII are generally not subject to mandatory arbitration.[15]

It is perfectly sensible to distinguish between those arbitration agreements entered voluntarily and knowingly by two businesses, and those imposed by a business on an employee or consumer. In fact, numerous European countries have been making such a distinction for years, protecting their employees and consumers against the likelihood of unfair arbitration agreements.[16]

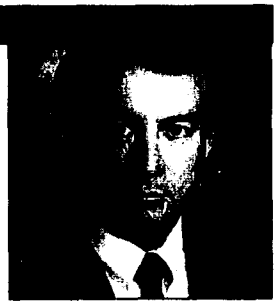
Those of us who value arbitration must continue to urge courts, legislators, policymakers, businesses and arbitrators to limit its use in these potentially unfair contexts. If we do not take action, we face a serious risk that the ultimate outcry against unfair arbitration will doom not only abusive misuses of arbitration, but also fair and valuable uses of this important dispute resolution technique.

Endnotes

1. 9 U.S.C. Section 1 et seq.
2. 500 U.S. 20 (1991).
3. This Fall, in Wright v. Universal Maritime Serv. Corp., 121 F.3d 702 (4th Cir. 1997), *cert. gr.* 66 U.S.L.W. 3575 (1998), the Court is expected to rule on the question of whether a union's entry into a collective bargaining agreement calling for arbitration may be found to have waived the rights of employee members to litigate civil rights claims against the employer in court.
4. 105 F.3d 1147, 1148 (7th Cir.), *cert. denied* 118 S. Ct. 47 (1997). *See also* Jean R. Sternlight, *Gateway Widens Doorway to Imposing Unfair Binding Arbitration on Consumers*, 71 Fla. B.J. 8, 9 (Nov. 1997).
5. Badie v. Bank of Am., No. 944916, 1994 WL 660730 at *3 (Cal. App. Dep't Super. Ct. Aug. 18, 1994).
6. Johnson v. Circuit City Stores, 148 F. 3rd 373, 377-79 (4th Cir.1998).
7. EEOC, *Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment*, 133 Daily Lab. Rep. (BNA) E-4 (July 11, 1997).
8. Report and Recommendations, Commission on the Future of Worker-Management Relations (the "Dunlop" Commission"), (Dec. 1994) at 33.
9. *See, e.g,* National Academy of Arbitrators Statement and Guidelines, 103 Daily Lab. Rep. (BNA) E-1 (May 29, 1997).
10. J.A.M.S./Endispute Arbitration Policy, in 9A Lab. Rel. Rep. (BNA), Mar. 26, 1996, at 534:521; American Arbitration Association , National Rules for the Resolution of Employment Disputes (1997).
11. Stirlen v. Supercuts, Inc., 60 Cal. Rptr. 2d 138, 143 (Cal. Ct. App. 1997) (rejecting as unconscionable arbitration clause which allowed the employer but not the employee to litigate certain claims); Hooters of America, Inc. v. Phillips, No. 4:96-3360-22, 1998 U.S. Dist. LEXIS 3962 (D. S. Car. March 12, 1998) (denying company's motion to compel arbitration because mandatory arbitration clause found to be unconscionable, in violation of public policy, illusory, and lacking in neutrality).
12. Gibson v. Neighborhood Health Clinics, Inc, 121 F.3d 1126, 1131 (7th Cir. 1997).
13. Renteria v. Prudential Ins. Co., 113 F.3d 1104, 1106 (9th Cir. 1997) (refusing, under Title VII, to enforce arbitration agreement where clause did not expressly put employee on notice of what she was waiving).
14. Cole v. Burns Int'l Sec. Servs., 105 F.3d 1465, 1465 (D.C. Cir. 1997) (upholding arbitration clause, given that employee would not have to pay any portion of arbitrator's fees or expenses, and based on assumption that appellate review would be sufficient to ensure arbitrators properly interpreted and applied statute).
15. Duffield v. Robertson Stephens & Co., 144 F. 3d 1182, 1185 (9th Cir. May 8, 1998); Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith Inc., No. Civ. A. 975 F. Supp. 190, 212 (D. Mass. Jan. 26, 1998).
16. *See* William W. Park, *The Relative Reliability of Arbitration Agreements and Court Selection Clauses in* INTERNATIONAL DISPUTE RESOLUTION: THE REGULATION OF FORUM SELECTION (Jack L. Goldsmith ed., 1997) at 30 (observing that "European legal regimes have generally required courts to disregard abusive prorogation agreements in consumer contracts").

A 'Constructive Compromise'

Enforce agreements, even if adhesive, but ensure participants a fair process



By Terry L. Trantina

Under the Federal Arbitration Act ("FAA") and most state arbitration acts, employees and consumers can be required by a predispute agreement to resolve their contract, common law and statutory claims through binding arbitration rather than through litigation in state or federal court.[1]

Such predispute agreements may be enforced even though the obligation to arbitrate may have been obtained on a "take it or leave it" basis, as long as the "adhesive" contract containing the obligation to arbitrate is not, in context, beyond reasonable expectations, unconscionable or oppressive. However, whether employees and consumers *should* be required by such adhesive predispute contract environments to submit their disputes to binding arbitration, and if so, under what set of circumstances, are different questions.

A clash in policies

These questions recall to the period when arbitration was viewed by the courts with suspicion and as an inferior means of resolving disputes. Today, our civil court system is underfunded, economically unavailable to many, unnecessarily adversarial and complex, and final decisions are usually many years in the making. As a result, it is now the stated public policy of our courts, both federal and state, that agreements to arbitrate can and should be enforced. Arbitration can be beneficial to all parties to a dispute because final and binding arbitration has a greater potential than our civil courts for resolving disputes quickly, with less cost, and with greater satisfaction for the participants without sacrificing the availability and enforceability of remedies.

There is not, however, universal agreement that arbitration has these potential benefits for consumers and employees, particularly where the obligation to arbitrate is based on a predispute agreement that is imposed on a "take it or leave it basis." The requirement to submit a dispute to arbitration rather than to the court system involves the waiver of a party's access to public courts, a jury and an appeal, as well as a reduction in the type and scope of discovery. Those opposing predispute arbitration clauses for consumers and employees claim it is unfair to impose a forfeiture of these important rights unless their waivers are fully informed and entirely voluntary, and the arbitration process itself is fundamentally fair – i.e., provides adequate due process and remedies.

I am convinced that the core truths of both propositions have merit. Today, arbitration does have the potential for more rapid, economical, amicable dispute resolution as well as overall satisfaction with the result – *and* predispute arbitration agreements should be enforced, but only if the obligation and consequences of the substitution of the required arbitration process for a day in court is both clear and fundamentally fair. After all, the only real bargaining power available on any aspect of these relationships is to accept the terms offered or seek better terms elsewhere. I favor enforcing the obligation in predispute agreements to arbitrate, in the workplace and the consumer marketplace, even though these environments are unquestionably characterized by uneven bargaining power. As in other areas where the interests of individuals and our society must be balanced, the answer is not to forgo the benefits of employer and consumer arbitration programs by prohibiting them *per se* or unduly burdening the right to impose a dispute resolution alternative by contract before the dispute arises.

Neither an outright ban nor a 'one size fits all' straightjacket solution is appropriate for the problem of predispute arbitration clauses in contracts of adhesion.

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Protocols provide guidance

The right answer is to provide employers and product/service providers the carrot-and-stick type of guidance, like that found in the 1995 Employment Due Process Protocol and the American Arbitration Association's 1998 Consumer Due Process Protocol, enabling employers and providers to develop arbitration programs and contracting processes that are both fundamentally fair and sufficiently consensual. These protocols provide guidelines rather than rules, and encourage flexibility to ensure that programs can be tailored to individual employer and consumer environments.

As these protocols demonstrate, the easiest hurdle is developing arbitration programs that have

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