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Mandatory Arbitration in Employment Cases: Ugly Duckling or Beautiful Swan?

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Part 1 of a 3-Part Series

Many years ago, employers and management counsel across the country cheered the birth of mandatory arbitration provisions in employment agreements. For instance, when the U.S. Supreme Court decided *Perry v. Thomas*, it determined that because there is a clear federal policy favoring arbitration, an arbitration clause would be upheld despite a state law requiring a judicial forum for the employment claims at issue in the dispute. 482 U.S. 483, 491 (1987). And when the same Court decided *Gilmer v. Interstate/Johnson Lane Corp.* a few years later, it held that an inequality in bargaining power is not a sufficient reason to hold arbitration clauses in employment agreements unenforceable. 500 U.S. 20, 33 (1991). Arbitration was supposed to be the magic bean that would grow into a fortress of beanstalks protecting America's corporations from time-consuming, energy-sucking litigation. And even better, it was supposed to be inexpensive and generally designed to give employers the upper hand. After all, and arbitrator would never give a plaintiff as much as a jury of his (not 'our') peers, right?

Well, it was a good thought – and it was fun while it lasted.

Who Decides When a Case Goes to Arbitration? Arbitrators.

Courts across the country have been enforcing contractual arbitration provisions with increasingly few exceptions. In August 2015, the Ninth Circuit bolstered this trend by holding that where there is an arbitration provision, the very issue of arbitrability must be decided by none other than an arbitrator.

With all signs pointing toward arbitration, employers should revisit their arbitration provisions while asking whether the cost, effort, and loss of appeal rights are worth it.

What Happened?

In *Brennan v. Opus Bank*, an executive sued his former employer for breach of his employment agreement. The executive argued that the dispute should be resolved by litigation because the arbitration clause was unconscionable and thus unenforceable. The employer contended that an arbitrator, not the court, must decide the enforceability of arbitration clause.

The district court dismissed the suit and compelled arbitration. The Ninth Circuit affirmed. The court held that an arbitration provision incorporating the rules of the American Arbitration Association constitutes “clear and unmistakable” evidence that the contracting parties intended to delegate the issue of arbitrability to an arbitrator. Because incorporating the AAA’s rules is generally considered a best practice when it comes to drafting arbitration provisions, the court’s message is clear: arbitrators should decide which cases are subject to arbitration. Unsurprisingly, whenever an arbitrator determines arbitrability, it is almost certain that the arbitrator will choose arbitration.

What Does *Brennan* Mean for Employers?

Ten years ago, defense counsel widely considered arbitration as a sea change in employment litigation. For example, the U.S. Supreme Court enforced a provision in an employment agreement which delegated to an arbitrator the exclusive authority to resolve any dispute relating to the agreement’s enforceability. *Rent-A-Center, West, Inc. v. Jackson*, 561 U.S. 63 (2010). And in*Preston v. Ferrer*, the Court determined that arbitration provisions trump state laws giving primary jurisdiction to another forum, including administrative boards. 552 U.S. 346, 359 (2008). At the time, arbitration was thought to be both more efficient and less expensive than litigation. Disputes against individual plaintiffs could be resolved swiftly in arbitration without the added time and expense of discovery and motion practice required in complex cases.

Arbitration Can Be Costly

As it turns out, arbitration has not lived up to these expectations. Over time, the issue of class action waivers arose, increasing the number of complex and class disputes in the arbitration forum. The cost of arbitration has also exploded with the rapid increase in popularity of contractual arbitration. Single arbitrators charge several hundred dollars per hour in the most basic of cases. This cost is tripled in complex cases, which require a three-person panel.

In addition, the burden to pay for arbitration often falls on the employer. The *Brennan* decision could further increase costs because the issue of whether a dispute is arbitrable is now an issue for the arbitrator, not the court. It is highly unlikely that an arbitrator, who gets paid by the hour, would decide that he or she does not have jurisdiction over the parties’ claims and send the case back to court. Accordingly, the existence of an arbitration clause will almost certainly result in the case being resolved in arbitration, with the employer bearing the brunt of the expense.

Arbitration Can Be Inefficient

Although arbitration was once considered a more efficient forum, the procedural disadvantages to employers may outweigh the benefits. The time consuming procedures common to litigation—including discovery, motion practice, and dispositive motions—are all permitted in arbitration, too. The availability of these procedures remove the advantage of efficiency that arbitration is supposed to offer. Further, parties must pay the arbitrator throughout discovery disputes and motion practice. In some cases, it would be less costly to simply argue these issues in court before a judge, who does not charge by the hour.

Arbitration Can Eliminate Appeal Rights

Additionally, appeal rights are extremely limited in arbitration. For practical purposes, the arbitrator’s decision is final. This is particularly concerning in complex cases and class action arbitration, which did not exist when arbitration first came on the scene. Whereas a defendant could appeal a court’s

certification of a class, an arbitrator's certification of a class is a game changer for a defendant's case because this order cannot be appealed except in the rarest of cases.

What Should Employers Do?

Ultimately, *Brennan* is only one example of the many cases decided across the country weighing in favor of arbitration. For this reason, employers should revisit their employment agreements and other contracts with arbitration provisions to determine whether arbitration is the best forum to resolve disputes.

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