RECENT DECISIONS PROVIDE FURTHER GUIDANCE ON ARBITRATION PROVISIONS

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A number of recent court decisions have answered several questions regarding arbitration clauses in employment contracts. These decisions define more precisely the legal requirements for lawful arbitration clauses and should be reviewed by employers to ensure that any arbitration policy or agreement is enforceable. What follows is a brief description of each of these important holdings.

Armendariz v. Foundation Health Psychcare Services, Inc.: Although it was decided in the year 2000, any discussion of arbitration in the employment context in California must begin with Armendariz. The California Supreme Court in Armendariz held that employment agreements requiring the employee to arbitrate disputes are enforceable as long as the arbitration clause does not affect the employee's statutory rights and is not unconscionable. To reach this standard, the arbitration agreement has to meet certain minimum requirements: (1) provide for neutral arbitrators, (2) provide for more than minimal discovery, (3) require a written award, (4) provide for all of the types of relief that would otherwise be available in court, and (5) not require employees to pay either unreasonable costs or any arbitrators' fees or expenses as a condition of access to the arbitration forum.

Little v. Auto Stiegler, Inc.: The Little case extended the Armendariz standards to other employment claims, e.g., a claim for wrongful termination in violation of public policy. In Little, the California Supreme Court stated that courts should first consider two "gateway issues" of arbitrability: whether there is an effective agreement to arbitrate between the parties and whether the agreement covers the dispute at issue. If necessary, an additional consideration is to determine whether an illegal clause can be saved by severing the offending provision.

As was stated in Armendariz, the Little court held that to be enforceable the arbitration agreement must satisfy traditional contract standards of conscionability. The doctrine of unconscionability has a "procedural" as well as a "substantive" element, the former focusing on "oppression" or "surprise" due to unequal bargaining power, the latter on "overly harsh" or "one-sided"

results. The arbitration agreement must be both substantively and procedurally unconscionable to be unenforceable, but not necessarily in the same degree. For example, the more substantively oppressive the contract term, the less evidence of procedural unconscionability will be required to reach the conclusion that the agreement is unenforceable.

Omar v. Ralph's Grocery Company: In Omar, a California Court of Appeal addressed the question of whether the trial court or an arbitrator should consider a waiver issue. The plaintiff asserted that the issue of waiver was properly before the court pursuant to Code of Civil Procedure section 1281.2(a) (allowing the court to determine if the right to compel arbitration has been waived), while the defendants contended that because the arbitration agreement is governed by the Federal Arbitration Act (FAA) and did not incorporate California law, Code of Civil Procedure section 1281.2(a) was inapplicable and federal law applied. The appellate court concluded that an arbitrator must determine the issue of a waiver because, unlike the decisions based on section 1281.2(a), all of the respondent's waiver allegations involved non-litigation conduct and required interpretation of the arbitration agreement. Thus, the court held that the FAA establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay or a like defense to arbitrability.

Nyulassy v. Lockheed Martin Corporation: In Nyulassy, the employee signed a settlement agreement to resolve a dispute with his employer's predecessor. The settlement agreement was the result of negotiations during which the employee was represented by his own attorney. The settlement included a new employment agreement which provided for the mandatory arbitration of employment disputes.

In a subsequent dispute, the employer moved to compel arbitration. The trial court denied the motion and the appellate court confirmed the ruling, finding that the arbitration clause in the employment agreement was both procedurally and substantively unconscionable. First, the arbitration clause in the employment agreement was substantively unconscionable as it was one-sided and required only the employee to arbitrate issues. In addition, the employment agreement also required the employee to submit to discussions with his supervisors in advance of, and as a condition precedent to, having his dispute resolved through binding arbitration. The appellate court held that this employer-controlled mechanism suggested that the employer would receive a "free peek" at the employee's case and would thereby obtain an advantage in any subsequent arbitration. Moreover, the unilateral arbitration clause placed time limitations of 180 days on the employee's assertion of any claims against the employer, a shorter period than the applicable statutes of limitations.

The employment agreement was a standard form utilized by the employer and the terms were supposedly nonnegotiable. Thus, the agreement was also procedurally unconscionable; even if the employee was able to negotiate other aspects of his employment agreement with the employer, the lack of negotiation concerning the arbitration clause was sufficient to determine unconscionability. Indeed, the fact that the parties were represented by counsel and entered into the agreement "post dispute" did not necessarily mean the agreement was not unconscionable. The appellate court also approved the trial court's decision to refuse to sever the offending sections of the agreement because the entire agreement was "permeated" by unconscionability.

Fitz v. NCR Corporation: In Fitz, the employer provided its employees with a brochure informing them of its arbitration policy. The employees were not given a chance to negotiate the terms of the policy; rather, they were deemed to agree to the terms by continuing to work for the employer for one month after the company sent the brochures or by accepting any benefit of employment.

The *Fitz* court found the policy to be procedurally unconscionable due to the inequality of bargaining power between the employer and the employees which resulted in the employees not having any meaningful choice in deciding whether to accept the terms of arbitration. Substantively, the terms of agreement limited discovery to depositions of merely two individuals and, in addition, one expert witness expected to testify in the arbitration. Moreover, the terms exempted claims which the employer was most likely to bring against employees, such as disputes over intellectual property, while requiring the arbitration of claims employees were most likely to bring, such as allegations of discrimination. The court held that these two provisions rendered the brochure substantively unconscionable. Finally, Fitz determined that since there was more than one unlawful provision in the arbitration agreement, the agreement could not be made legal by simply striking the offending provision.

Conclusion: As these cases demonstrate, employment arbitration clauses are subject to ongoing attacks by plaintiffs' lawyers. While this constant criticism requires employers to diligently revise their arbitration clauses as appropriate, the effort is worthwhile; arbitration remains a cost-effective alternative to court litigation. Read carefully, these recent decisions provide new and detailed guidance for California employers seeking to implement enforceable arbitration agreements and/or policies. Employers should therefore review their employment arbitration clauses with legal counsel to ensure that they are consistent with current law.

Mr. Scott would like to thank Falk Jellissen for his contribution to this article. Falk, who comes to us all the way from Munich, Germany, has joined ECJ as an intern for a second consecutive year. He has just completed his German bar examination and is obtaining additional credit in the area of American employment law.