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Arbitration: A Positive Employment Tool and Potential Antidote to Class Actions

by Gregg A. Gilman, J.D., and David Sherwyn, J.D.

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EXECUTIVE SUMMARY

The use of arbitration for employment and other workplace disputes has been the topic of much controversy. In examining various aspects of arbitration, this paper proposes arbitration as a fair and appropriate process for responding to employees' workplace issues. The value of arbitration is notable, particularly considering the potential costs of litigation. Even considering *Wal-Mart v. Dukes*, the 2011 Supreme Court decision which tightened the requirements for certifying a class in a class action, employers are concerned that the expense or judgments resulting from litigation will put an entire company at risk. From the employees' stance, a major argument against arbitration is the perception that the process favors employers. Indeed some statistics show that employers do win most arbitration cases. However, employers generally settle legitimate grievances when possible, leaving the questionable cases to emerge into arbitration or litigation. Another source of unfairness for employees is the difficulty of finding counsel for arbitration, but this occurs largely because less money flows through the arbitration process. In sum, the analysis presented here presents arbitration as the fairest, most economical, and speediest procedure to properly address employees' complaints if a settlement cannot be reached.

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Arbitration: A Positive Employment Tool and Potential Antidote to Class Actions

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More than two years have elapsed since employers let out a sigh of relief when the Supreme Court overturned the 9th Circuit decision in *Wal-Mart v. Dukes* and decertified the class of plaintiffs suing Wal-Mart, the nation's largest employer, for sex discrimination.¹ The class consisted of approximately 1.5 million of the retailer's former and current female employees.² While the details of the lower and Supreme Court decisions are beyond the scope of this paper, the lesson for many employers was the fear that class actions, regardless of merit, could put an entire company at risk. While the obvious response, "don't violate the law," should seemingly resolve that fear, the fact is that many employment lawsuits, such as wage and hour or discrimination cases, are often difficult to defend. This may occur because: (1) the law is unclear; (2) there are shades of gray in employment decisions, (3) it is difficult to ensure compliance in large multi-state or multi-national corporations, or (4) sometimes companies face "bad facts" even when they did not violate the law. Although defending the allegations of one employee or even a group is expensive, most employers are able to do this. Defending a class action, however, often requires resources beyond what many employers can marshal. In this paper, we propose a way to avoid such costly litigation: arbitration.

¹ 131 S.Ct. 2541.

² *Id.* at 2547.

Arbitration of employment related lawsuits has been an alternative to litigation for employers since the early 1990s. Since that time the following four broad questions have surrounded arbitration: (1) what is arbitration and is it fair?; (2) can employers require arbitration of employment lawsuits?; (3) can arbitration agreements prevent class actions?; and (4) should an employer implement an arbitration policy? This report addresses these four questions. Briefly, the answer to question 1 is discussed in the next section, which defines arbitration, the answer to questions 2 and 3 is yes, and the answer to question 4 depends on the employer's situation, as we explain in the final section of the paper. After discussing the question of what is arbitration and whether it is fair, we explain the legal evolution that makes arbitration an option for employers who wish to trade litigation for arbitration and avoid class actions. Finally, we describe the employers who should, and should not, implement arbitration policies.

What Is Arbitration?

When discussing arbitration of employment disputes we are referring to mandatory “pre-dispute” arbitration. There is no dispute over whether post-dispute the parties to any case can choose to avoid the court system and arbitrate the case instead—but it is an extremely rare instance when both parties to a dispute will choose arbitration over litigation once the dispute has occurred.³ Arbitration and litigation each offers its own particular set of advantages and disadvantages. This means that both sides will often agree that the arbitration seems to be a better process for dispute resolution before a dispute occurs. After the dispute arises, however, it is almost inevitable that one side will seek to exploit the advantages of litigation and will refuse to arbitrate.

Looking at the advantages and disadvantages of each, most knowledgeable observers will agree that the differences between arbitration and litigation can be put into three categories: (1) facts; (2) disputes over the time and cost; and (3) conjecture or opinion over fairness.

Facts. Let's start with the arbitration facts that everyone agrees on. First, arbitration is less formal than litigation.⁴ Procedures that you would find in court are either relaxed or not in place at all. Instead, arbitration takes place in a conference room, not a court; arbitrators are not judges (e.g., there is no reason to stand when they enter the room); the rules of evidence are relaxed; and written documents need not comply with court rules with regard to font, margins, table of contents, and the numerous other requirements. This is why many em-

ployers whose employees pursue cases *pro se* will not have a lawyer present the case.⁵ Non-lawyers can be effective advocates in arbitration, while they are not permitted to play that role in court.

Second, arbitration is private,⁶ whereas litigation is public. Thus, unless the court seals the record, a rare occurrence, all allegations, briefs, depositions, and proceedings are part of the public record. Third, it is difficult to appeal an arbitration decision.⁷ In litigation, on the other hand, some appeals are automatic and, in some cases, the court of appeals examines the case *de novo* (taking a fresh look with no regard to the prior decision). In other cases, the appeals court can overturn a decision for a judicial error in law with regard to the substance (e.g., a misunderstanding of what constitutes sexual harassment), evidence, or jury instructions. In contrast, to overturn arbitrations the moving party must prove one of “four specifically enumerated situations. That is, the moving party must demonstrate corruption, fraud or undue means in procurement of the award, evident partiality or corruption in the arbitrators, specified misconduct on the arbitrators' part, or [that] the arbitrators exceeded their powers.”⁸ The Second Circuit also recognizes an additional basis, manifest disregard of the law, to vacate an arbitration award.

Arbitration Is Faster and Less Expensive than Litigation

Because it is less formal, private, and difficult to appeal, arbitration should be faster and less expensive than litigation. This conclusion is, however, disputed by some of arbitrations' proponents and critics.⁹ Most of those disputing the long-held belief that arbitration is faster and less expensive are those who were parties to arbitrations which took an exceedingly long time to conclude and cost substantial amounts of money for attorneys' fees, experts, depositions, and, the added expense, the arbitrator. While there is anecdotal evidence contesting those long-held time and money beliefs, the empirical evidence supports the assertion that arbitration is, in fact, cost and time effective.¹⁰

⁵ *Id.*

⁶ *Id.* at 1562.

⁷ See *id.* at 1579.

⁸ *DuBois v. Macy's Retail Holdings, Inc.*, 2013 U.S. App. LEXIS 20301, *2 (2d Cir. Oct. 4, 2013.)

⁹ See: David S. Sherwyn, J. Bruce Tracey, & Zev J. Eigen, *In Defense of Mandatory Arbitration of Employment Disputes: Saving the Baby, Tossing Out the Bath Water, and Constructing a New Sink in the Process*, 2 U. Pa. J. Lab. & Emp. L. 73, 100 (1999) (stating that arbitration is less expensive than litigation partly because lawyers do not need to spend as much time to arbitrate as they would to litigate the facts of a court case).

¹⁰ See: David Sherwyn *et. al.*, *Assessing the Case for Employment Arbitration: A New Path for Empirical Research*, 57 Stan. L. Rev. 1557, 1567-78 (2005).

³ See: David Sherwyn, *Because It Takes Two: Why Post-Dispute Voluntary Arbitration Programs Will Fail to Fix the Problems Associated with Employment Discrimination Law Adjudication*, 24 Berkeley J. Emp. & Lab. L. 1 (2003).

⁴ David Sherwyn *et. al.*, *Assessing the Case for Employment Arbitration: A New Path for Empirical Research*, 57 Stan. L. Rev. 1557, 1575 (2005).

Several years ago, Lewis Maltby, president of the National Workrights Institute, found that the average litigation case took nearly two years (679.5 days) to resolve, while the mean for arbitration was 8.6 months.¹¹ Arbitration advocates point to a shorter time period as a positive aspect of arbitration. Again, the data studied arise out of cases that were actually litigated or arbitrated and not the thousands that are resolved before the formal filings. Unlike the win–loss comparisons, there is little empirical controversy: arbitration is faster than litigation.

In fact, Maltby’s study actually underestimates the time difference between the two forms of adjudication. Maltby analyzed resolutions not trials.¹² Accordingly, Maltby’s data include motions which reduce the time period at issue for litigation, but do not really affect arbitration, where dispositive motions are rare. In Maltby’s data set, 60 percent of the “litigated” cases were resolved through a motion (and the employer won 98 percent of those cases).¹³ Thus, Maltby was comparing arbitrations; where the parties almost always had the opportunity to present their cases, against litigation, where 60 percent of cases were decided by court on a motion alone. Even with motions providing a built in “time advantage,” cases in litigation still took 2½ times as long as those in arbitration to be resolved.

In a more recent study, Eisenberg and Hill compared arbitrations and trials, unlike Maltby’s focus on resolutions.¹⁴ They separated civil rights cases from other employment claims in the arbitration and state court data, but their federal court data included both. Based on 172 cases, Eisenberg and Hill found that the average amount of time to adjudicate a non-civil rights case was 250 days.¹⁵ The 42 AAA civil rights arbitration cases that they studied took, on average, 276 days.¹⁶ The mean time for state court non-discrimination trials was 723 days ($N = 170$), state court discrimination trials, 818 ($N = 163$); and federal court trials, 709 days ($N = 1,430$).¹⁷ Thus, as expected, when deleting motions, the disparity between time to arbitrate versus litigate is even greater.

The comparative cost of arbitration and litigation is more challenging to pin down. Litigation costs vary widely,

¹¹ Lewis L. Maltby, *Private Justice: Employment Arbitration and Civil Rights*, 30 Colum. Hum. Rts. L. Rev. 29, 55 (1998).

¹² *Id.*

¹³ *Id.* at 47.

¹⁴ Theodore Eisenberg & Elizabeth Hill, *Employment Arbitration and Litigation: An Empirical Comparison* (N.Y. Univ. Sch. of Law, Public Law and Legal Theory Paper Series, Research Paper No. 65, 2003).

¹⁵ *Id.* at 19-20.

¹⁶ *Id.*

¹⁷ *Id.*

because a party’s counsel’s rate and staffing will have a huge effect on the cost of adjudication. Still, it stands to reason that extensive discovery, motions, jury instructions, and other procedures inherent in litigation will increase costs and fees as compared to the more straightforward process of arbitration.

Fairness of Arbitration

The biggest dispute over arbitration is fairness. The issue here is that most employment law scholars and other employee advocates contend that arbitration is unfair to employees.¹⁸ While statistics do appear to support this conclusion, we note that these data are flawed. What is missing in the data is a baseline of the percentage of cases that have merit. Lacking such a baseline, scholars compare arbitration results with litigation results. If they find higher success rates in litigation they immediately contend that arbitration is unfair, but this comparison does not account for cases without merit. If we had such a baseline of meritorious cases, we could compare the two systems against the “right” answer, but this is not possible.

Scholars have compared litigation win rates to arbitration win rates.¹⁹ Some of these studies include dispositive motions (where employers win 98 percent those granted) and some don’t include those motions. Studies that exclude motions are inherently flawed, because they compare litigation that survived summary judgment against arbitration cases where there was no motion filter. There are other reasons why “bad” arbitration cases pollute the data. One example is the *pro se* policy we mentioned, that is, under many employer arbitration policies the company will not bring a lawyer if the employee also does not bring one.²⁰ Thus, there are a large number of arbitrations where the employee is *pro se*. It is difficult for an employee to take a case to federal court *pro se*. Thus, cases in litigation, before surviving motions must survive another test: whether a plaintiff’s lawyer will invest time and money in the case. Plaintiffs’ lawyers are rational actors who have no incentive to take cases with a low probability for success and thus, they weed out bad cases.

¹⁸ See, e.g.: Alexander Colvin, *Empirical Research on Employment Arbitration: Clarity Amidst the Sound and Fury?*, 11 EMP. RTS. & EMP. POL’Y J. 405, 406 & n.3 (2007) (citing Katherine Van Wezel Stone, *Mandatory Arbitration of Individual Employment Rights: The Yellow Dog Contract of the 1990s*, 73 Denver U. L. Rev. 1017, 1019–20 (1996).

¹⁹ See e.g.: William M. Howard, *Arbitrating Claims of Employment Discrimination: What Really Does Happen? What Really Should Happen?*, Disp. Resol. J., Oct.-Dec. 1995, at 40; Theodore Eisenberg & Elizabeth Hill, *Employment Arbitration and Litigation: An Empirical Comparison* (N.Y. Univ. Sch. of Law, Public Law and Legal Theory Paper Series, Research Paper No. 65, 2003).

²⁰ See: David Sherwyn et. al., *Assessing the Case for Employment Arbitration: A New Path for Empirical Research*, 57 Stan. L. Rev. 1557, 1586 (2005).

Finally, we contend that employers who have implemented companywide arbitration policies should never lose, and indeed for some employers that is the case. The reason for this assertion is twofold. First, mandatory arbitration policies typically include a grievance process that precedes arbitration and includes a mediation step.²¹ After hearing the employees' cases during the grievance and mediation steps, the employer has a good idea of the facts of the case. At this point the employer's counsel or HR professional decision maker should be able to judge whether an employee's claim can succeed before an arbitrator or any trier of fact. (In that regard, we note that a decision maker who makes the wrong call will not be the decision maker much longer.) More to the point, employers, their lawyers, and their HR professionals are risk averse.²² Settling a case to avoid the cost of defense or the fear of a ruling not supported by the facts is a perfectly acceptable cost of doing business. With that in mind, suppose we separate the world of cases into three categories: (1) dead bang winners for the employee; (2) cases that could go either way; and (3) dead bang winners for the employer. We contend that the vast majority of employers with mandatory arbitration provisions only take the third category to arbitration and thus, their success rate often is, and, should be, extremely high. The employee advocate scholars ignore this argument and, instead, focus on the so-called repeat player effect.

Several scholars have made a career out of showing that repeat player employers fare better than single player employers.²³ These scholars suggest that arbitrators are biased in favor of those who may hire them again. These scholars predicate their wholesale attack on a pillar of employment relations policy, arbitration, by arguing that unions provide a check on arbitrators' inherent lack of integrity and thus, without this check, arbitrators will follow the money regardless of the facts and their own professional standards. It is somewhat amazing that without anything more than results that may be just (again there is no baseline), these scholars attack the entire profession of labor and employment neutrals as people who have no professional integrity and who,

²¹ Alexander Colvin, *Employment Arbitration: Empirical Findings and Research Needs*, 64-Oct Disp. Resol. J. 6, 11 (2009) (showing that companies adopt "internal grievance procedures, such as internal management appeals boards, mediation, or peer review" preceding arbitration).

²² See generally: Scott Baker, *A Risk-Based Approach to Mandatory Arbitration*, 83 OR. L. REV. 861 (2004).

²³ See, e.g.: Lisa B. Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 Emp. Rts. & Emp. Pol'y J. 189 (1997); Lisa B. Bingham, *Is There a Bias in Arbitration of Nonunion Employment Disputes? An Analysis of Actual Cases and Outcomes*, 6 Int'l J. Conflict Mgmt. 369 (1995); and Lisa B. Bingham, *On Repeat Players, Adhesive Contracts, and the Use of Statistics in Judicial Review of Employment Arbitration Awards*, 29 McGeorge L. Rev. 223 (1998).

instead, see each case as opportunity to build a résumé that will convince the employer to choose them again.

One counter to this argument is, what about the plaintiffs' bar, that is, the attorneys who regularly represent employees? The employee advocate scholars dismiss the role of the plaintiffs' bar as if plaintiffs' lawyers have no role in choosing arbitrators or keeping them honest.²⁴ An interesting question arises: Why do plaintiffs' lawyers fail to play the role of the union in employment arbitration? The answer is that they refuse to take these cases. The follow-up question is, why do plaintiffs' lawyers oppose arbitration? After all, arbitrators have been resolving employment disputes for more than half a century. It is faster and less expensive to arbitrate than to litigate, which should mean that plaintiffs' lawyers would have an incentive to take these cases and provide the counter to the employer in the arbitrator selection process.

The reason that this does not occur can be found by looking at arbitration cases in the financial services industry. Highly compensated employees in that industry have no trouble finding counsel to arbitrate their cases, but those earning middle class wages are less likely to find willing counsel.

We contend that plaintiffs' lawyers are incentivized by two features of litigation: (1) cost of defense and (2) unpredictable juries. In this discussion, we in no way disparage plaintiffs' lawyers. Unlike arbitrators who, by definition, are supposed to fair and impartial, plaintiffs' lawyers do not owe such a duty to be "just." Plaintiffs' lawyers are advocates who can take or refuse cases at will, and once they have accepted the case they will do their best to prevail. But a lawyer has no obligation to take a case that limits damages even when it has clear liability. As a practical matter, a series of such decisions will put the lawyer out of business. Moreover, judges have apparently grown increasingly frustrated with lawyers who bring "fees cases"—cases where the fees greatly outweigh the damages.

Another issue involves employers' view of potential employee suits. The costs of defending cases in court and employers' fear of runaway juries often convince employers to settle cases that they would otherwise adjudicate before an arbitrator.²⁵ The fact that arbitration for low- or medium-wage employees does not provide a financial windfall for plaintiffs' lawyers does not mean that the system is unjust or that employers should be vilified for choosing arbitration. Instead, employers can, and often do, use arbitration as the center piece of their labor relations program.

²⁴ See: Bingham (1997), *supra*.

²⁵ See: Sherwyn *et. al.* (2005), *supra*.

Class Actions

Arbitration is particularly popular among employers because of recent Supreme Court decisions allowing employers' arbitration policies to prohibit collective or class actions.²⁶ Unlike the litigation versus arbitration trade-off, this prohibition is not simply a forum or process change. Instead, it does take away a tool that could be used by plaintiffs. The question is whether this represents a problem for employees in terms of achieving a fair resolution of workplace disputes.

While the litany of publicized wage and hour class action settlements supports the view that class actions are an effective tool for employees who have been wronged by employers, a closer look shows that class action settlements are, in fact, a boon for plaintiffs' lawyers and tend to provide little compensatory relief to the employees themselves. Two questions arise in this context. First, are employees harmed by the lack of class actions?, and second, are class actions the optimal way to address systemic legal violations?

Let's begin with a look at the typical pattern of a class action. Seasoned class action lawyers on both sides know that there is a rhythm to employment class actions. The number one priority for plaintiffs' lawyers is the potential for a large damage award against a deep-pocketed employer. Next, the parties battle over the certification of the class. At this point, the plaintiffs' lawyers have a large investment in the case, which they typically have accepted on a contingent-fee basis. Defense lawyers shift to damage control at this point. They work to knock out certain aspects of the claim to make the settlement numbers manageable. This posturing increases the plaintiffs' lawyers' investments in their cases, increases their costs, and thus, increases the amount of fees they need to recoup.²⁷

When the parties finally settle, the employer is comfortable with the damage award and the plaintiffs' lawyers sell the settlement to the employees. Are the employees justly compensated for their lost wages? Are they happy with the award? We have never seen these empirical questions addressed by researchers. Instead, the contention that eliminating class actions is hurtful to employees is made in a vacuum and without comparison to potential relief through arbitration.²⁸

²⁶ See: *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011).

²⁷ Indeed, at Georgetown Law School's Hospitality Law Conference (10/25/13 Washington, DC) four seasoned management lawyers, all labor and employment department chairs, Gregg Gilman (Davis & Gilbert), Carolyn Richmond (Fox Rothschild), David Ritter (Barnes & Thornburg), and Paul Wagner (Stokes, Wagner) stated that in their extensive collective experience, class action settlements generally revolved around plaintiffs' lawyers' fees, and the amount of money that most employees would recover bordered on inconsequential.

²⁸ The National Football League recently settled a lawsuit in which players sought redress for concussions and other physical and mental injuries. The media reported the settlement as acceptable to the players, who did

Next, let's examine an alternative scenario, one that includes arbitration. In a workplace in which employees contracted away their right to file a class action, say that a plaintiff's lawyer invested the time and energy to discover a class-wide violation. At this point, the lawyer would file an arbitration demand and arbitrate the best claim first, perhaps, or depending upon the terms of the arbitration agreement, aggregate any other claims into a class-wide arbitration. If class-wide arbitration is not permitted, the plaintiffs' lawyer may elect to arbitrate the same claim over and over at the employer's expense. With genuine classes, this may be so inefficient that it may increase the odds that an employer agrees to treat the putative group of employees as a class.

In a situation like this, employers may not regard a class action ban as a true advantage if they have to arbitrate the same issue hundreds of times. If the first arbitration yielded a pro-employee decision the employer would not want to repeatedly arbitrate the same claim. The first case would not entail the class certification issue, would not result in huge amounts of attorney time, and could be adjudicated instead of settled. The employee would not have to use her award to pay for the lawyer's time. Instead, the lawyer would have her hourly fee (as determined by the court and paid by the employer) and maybe a small percentage of the award. Subsequent arbitration cases would likely be settled by focusing exclusively on the employee's lost wages because the legal issue would be settled. The employer would pay what it owes, the employee would get what she deserves, and the plaintiffs' lawyers would lose a boondoggle. In short, reduced transactional costs associated with arbitration actually make repeat arbitration of class-wide violations more likely to yield a greater percentage of available surplus funds to go to wronged employees as compared to attorneys and experts. Employees may thus be better off waiving their right to class actions in many cases, and using arbitration as a lever to gain *de facto* class status, but with a greater potential yield of available damages.

The Law of Arbitration

As we said, the simple answer to whether mandatory arbitration is lawful and can prevent class actions is yes. The evolution of the law is complex, however. Let's briefly examine the procedure under which the law developed, beginning about forty years ago. In almost all cases since then, the employer has had an arbitration policy but the employee's counsel filed a lawsuit in court despite the policy. The employer then would file a motion to compel arbitration and the court would have to decide whether to keep the case or defer it

not get health insurance, and as a pragmatic decision because it could take years to actually litigate the case. Although a judge suspended the agreement pending further information, the fact remains that the court had ordered mediation, and a hearing appeared to be the last resort.

to arbitration. This scenario is somewhat different than the first Supreme Court case that addressed the issue.

In *Alexander v. Gardner-Denver*, a 1973 case, the employee, who was a union member, was fired and arbitrated his grievance under his union contract.²⁹ At the arbitration the employee alleged that the employer terminated the employee because of his race. The arbitrator denied the grievance and held there was cause for termination. Subsequently, the employee filed a race case in federal court, where the employer argued that arbitration was the exclusive forum for the dispute and, regardless of that, the employee had chosen to go to arbitration and was not entitled to the proverbial second bite of the apple. The United States Supreme Court rejected the employer's argument and found that arbitration did not preclude the employee from a subsequent lawsuit.³⁰ The basis for the Court's decision was twofold. First, the Court held that while arbitration was fine for contract rights (that is, the just cause provision in the union contract), it was not appropriate for statutory rights (in this case, anti-discrimination law). Second, the Court held that union arbitration provisions were inappropriate for resolving discrimination lawsuits because the union "owned" the grievance, not the employee and, because the union by definition was supposed to focus on the good of the whole, the individual case could get lost. Most lawyers and scholars took the holding of *Gardner-Denver* to mean that pre-dispute mandatory arbitration would not prevent an employee from pursuing a statutory claim in court. This lasted until 1991, when the *Gilmer* case was decided.

In *Gilmer v. Johnson Interstate*, the employee had to sign an arbitration agreement as part of accepting a position that involved working on the New York Stock Exchange (NYSE).³¹ The NYSE agreement provided that all disputes arising out of employment would be adjudicated before an arbitrator and thus precluded the employees from filing cases in court. After two years of employment, the company fired Gilmer, who filed an age discrimination case in federal court. The employer filed a motion to compel arbitration and the issue was once again ripe, but this time the result was different.

The *Gilmer* court enforced the motion to compel arbitration and distinguished *Gilmer* from *Gardner-Denver* because Gilmer's contract was an individual contract and not a union contract.³² The fact that Gilmer's case was a statutory right did not affect the decision because, as the

Court held, there was Supreme Court precedent to enforce arbitration of statutory rights as long as the statute did not expressly prohibit arbitration.³³ It must be noted that *Gilmer* does not prevent an employee from filing a claim with the Equal Employment Opportunity Commission or any other administrative agency and it cannot prevent that agency from filing a claim on behalf of the employee.

Gilmer made two more arguments that the Court rejected. First, *Gilmer* argued that the arbitration was unfair because in some cases: (1) there are no written opinions; (2) the employee does not get to choose the arbitrator; (3) damages are less than that provided in court; (4) discovery is limited; (5) the employee's decision to sign the contract is not knowing and voluntary; and (6) the employment contract was not covered by the Federal Arbitration Act (FAA).

The Court rejected the first three of these arguments not because these "defects" would make a policy unfair and therefore unenforceable, but because the NYSE policies provided for written opinions, choice of arbitrator, and damages equal to that in court. The Court rejected the discovery argument because the point of arbitration is that it should be quicker and less expensive than litigation, so limited discovery was not only acceptable, it was part of the process. With regard to the "knowing and voluntary" contention, the Court held that a take it or leave it policy is effectively voluntary. The unequal bargaining power in this situation does not make signing the contract involuntary, since the employee could walk away from the employment offer. Last, the FAA does instruct courts to enforce arbitration agreements and does exclude employment contracts for employees engaged in industries affecting international or interstate commerce. *Gilmer* argued that the FAA's language excluded all employment contracts, while the employer argued that the exception was limited to employees in the transportation industry. The *Gilmer* Court did not rule on the issue because since the NYSE was not the employer the contract was not an employment contract, excluded from coverage under the FAA. Thus, after *Gilmer* there were two main issues—what is a fair agreement and what is the effect of the FAA.

In the next twenty years, the courts defined what is fair and the effect of the FAA. The effect of the FAA is easily described. In *Circuit City v. Adams*, the Supreme Court held that Congressional intent behind the phrase "seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce" was limited to the transportation industry and that commerce did not have the widespread meaning that is ascribed to it today.³⁴ Thus, any employer outside the transportation industry can implement an arbitration policy as long as it is fair.

²⁹ 415 U.S. 36.

³⁰ *Id.* at 50.

³¹ 500 U.S. 20.

³² After *Gilmer* it seemed that arbitrations in union contracts could not prevent litigation. This changed in *14 Penn Plaza LLC v. Pyett*, 556 U.S. 247 (2009).

³³ *Id.* at 34-5.

³⁴ *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 105, 115 (2001).

With regard to fairness, most jurisdictions simply examine the substance of the policy and determine whether it is fair. Because “what is fair” varies by jurisdiction, employers should not draft arbitration agreements without experienced employment law counsel.³⁵ Still, the threshold rules from *Gilmer* (i.e., written opinions, statutory damages, choice of arbitrator, some discovery, and knowing and voluntary) are essential. In drafting arbitration policies, other topics to consider include the claims subject to arbitration, mutuality, cost arrangements, opt-outs, statute of limitations, use of attorneys, pre-arbitration mediation and other dispute resolution steps, and all available remedies. All in all, for the last ten years, employers with experienced employment counsel have been able to draft policies that will ensure that their employment lawsuits will be resolved in arbitration not litigation.³⁶

Class Actions

At the time of the *Gilmer* decision, wage and hour issues were something that most management law firms funneled to one or two associates and most companies rarely thought about. In the last ten years wage and hour class actions have become “bet the company” lawsuits for restaurants and clubs, and a serious source of concern for hotels. As the wage and hour issues became more prevalent, employers with an arbitration policy faced the difficult decision as to whether to exclude class actions from the policy, allow class actions in the arbitration forum, or to try to use the policy to prohibit class actions.

Arbitrating class actions greatly concerned employers because the same features that make arbitration attractive in the single employee discrimination cases (i.e., limited discovery and appeals, and relaxed rules of evidence) made it terrifying in class actions. Under federal law, punitive damages in discrimination cases are limited to \$300,000 per

³⁵ The advisory board of the Cornell Institute for Hospitality Labor & Employment Relations features eleven labor and employment lawyers who are all experienced in drafting, implementing, litigating, and arbitrating these policies.

³⁶ California is different. In California, contracts are unenforceable if they are procedurally and substantively unconscionable. In *Circuit City Stores, Inc. v. Adams* (Adams III), 279 F.3d 889, 896 (9th Cir. 2002), the Ninth Circuit, applying California law, held that “take or leave it” clauses are procedurally unconscionable. Next, the court, still applying California law, held that policy was substantively unconscionable because it limited damages and did not require mutuality. In other words, employees were required to arbitrate, but employers could litigate. The court then refused to enforce Circuit City’s policy because it failed both tests. In *Circuit City Stores, Inc. v. Ahmed*, 283 F.3d 1198 (9th Cir. 2002), however, the Ninth Circuit held that an “opt-out” option (i.e., the employee was covered by the arbitration policy but had 30 days to opt out) was not unconscionable. Thus, in California employers can have “unfair” policies as long as there is an opt-out. This is a safe way to ensure enforcement. Employers who do not wish to have an opt-out clause need to make sure that experienced counsel analyzes their policy with regard to substantive unconscionability.

plaintiff.³⁷ Thus, while a rogue arbitration decision could certainly hurt a company, there was an order of magnitude difference between that and a wage and hour class action where tens of millions of dollars could be at stake. The safe bet for employers was to prohibit class actions and hope the courts enforced the policy. This is exactly what happened.

The major cases addressing whether arbitration provisions can prevent class actions are not in the employment context, but instead mostly involve consumer matters. In *AT&T v. Concepcion*, for instance, the service contract required arbitration of all disputes and prohibited class actions.³⁸ In overturning both provisions, the district court and the Ninth Circuit held that a party to an arbitration agreement cannot get around its agreement to arbitrate individually and instead demand a class action.³⁹ Likewise, in *American Express Co v. Italian Colors Restaurant*, the arbitration agreement again prohibited class actions.⁴⁰ The merchant argued that any monetary damages that a single merchant could obtain in an arbitration over credit card fees would not exceed the costs of the arbitration and thus, a class action should be allowed. The Supreme Court held that the fact that the amount an individual could recover was too low to warrant pursuing a claim does not invalidate a class action waiver in an arbitration agreement. The Court continued by holding that courts must “rigorously enforce” arbitration agreements according to their terms, even for claims that allege a violation of federal statute, unless the FAA’s mandate has been “overridden by a contrary congressional command.”⁴¹ This ruling is applicable to the hospitality industry, because in many cases the amount of an individual’s wage and hour claim is not worth the cost of arbitration. The *Italian Colors* holding legitimizes an employer’s policy in such cases. Thus, the law is clear—employers, with the help of counsel, can implement mandatory arbitration policies which will ensure that all individual cases will be arbitrated and that there will be no class actions. As a final point in this report, we examine whether employers should do this.

Should Employers Implement Mandatory Arbitration Policies?

As a starting point, we propose that an arbitration policy goes hand in hand with a good-conscience effort to follow all relevant employment laws. Thus, employers should

³⁷ 42 U.S.C. § 1981a (West).

³⁸ *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011).

³⁹ *Id.*

⁴⁰ 133 S.Ct. 2304 (2013).

⁴¹ *Id.* at 2306-8. The Supreme Court did state that an arbitration agreement would be unenforceable if it prohibited the assertion of certain statutory rights or had administrative or filing fees making the forum impractical. *Id.* at 2310.

implement mandatory arbitration policies only if they also work hard to comply with the various labor and employment laws. Contrary to the argument that arbitration is a method used by employers who wish to violate the law, the fact is that arbitration has fewer barriers to entry, which means that employees with good claims are more likely to pursue those claims.⁴² Moreover, with arbitration, employers cannot benefit from the delays inherent in the EEOC and state agency process. These delays often force wronged employees to settle for nuisance amounts or to simply walk away. Under arbitration, employees will get their “day in court” within six to nine months—less time than it takes the EEOC to assign an investigator in a litigation case.⁴³ Once there is a hearing, employers cannot “big firm” employees in arbitration because discovery and motions are limited.⁴⁴ The arbitrator will want to get the case heard and will not let the employer “process” the employee to exhaustion. Even class claims will be heard for the first individual and then, if the employer is liable, there will be an avalanche of arbitrations.

Our contention is that employers who work hard to comply with the seemingly endless labor and employment laws and regulations will greatly benefit. The cost of defense

⁴² Richard A. Bales, *Normative Consideration of Employment Arbitration at Gilmer’s Quinceanera*, 81 Tul. L. Rev. 331, 355-358 (2006) (citing Elizabeth Hill, *AAA Employment Arbitration: A Fair Forum at Low Cost*, Disp. Resol. J., May-July 2003, at 8, 9).

⁴³ *Id.* at 343. (“Disposition time unequivocally favors arbitration. Lewis Maltby has found that the average litigated employment discrimination case took 679.5 days—nearly two years—to resolve, while the average arbitration case took only 8.6 months.” (citing Lewis L. Maltby, *Private Justice: Employment Arbitration and Civil Rights*, 30 Colum. Hum. Rts. L. Rev. 29, 55 (1998)).

⁴⁴ Michael H. LeRoy & Peter Feuille, *When Is Cost an Unlawful Barrier to Alternative Dispute Resolution? The Ever Green Tree of Mandatory Employment Arbitration*, 50 UCLA L. Rev. 143, 161-63 (2002).

will no longer drive cases. Plaintiffs’ lawyers, who take cases based on the depth of the employer’s pockets and their susceptibility to negative publicity, do not pursue arbitration cases. Moreover, like many of the current arbitration users, employers can make arbitration a centerpiece of their employment relations programs. These employers can communicate to their employees that the company wishes to resolve disputes in a timely non-adversarial way by having a policy that has a several step grievance policy, provides for mediation, and ends in arbitration. We have already noted that some employers will not send counsel if the employee is *pro se*. Other employers provide funds to hire a lawyer (again, the cost is much lower). Still others trade employment-at-will for arbitration under the theory that they only discharge and discipline for cause, so why not implement arbitration?

In the end, well-meaning employees and employers are better off if they have an alternative dispute resolution program that corrects problems and resolves disputes. The research shows that these employers will not reduce the number of disputes and will not increase their win–loss records.⁴⁵ They will, however, greatly reduce outside counsel fees and greatly reduce the amount of time that a case lingers. The reduction in time reduces damages because the less time results in less back pay and, because the plaintiffs’ lawyers have less time invested, settlements are no longer driven by attorney’s fees. Most important, employers with arbitration policies find that employees with disputes work to resolve the dispute and stay employed—something that is almost unheard of in the world of litigation. This, of course, reduces turnover costs and has a positive effect on morale. Because of the class action waiver and the numerous other benefits, it is time for “good” employers to consider arbitration. ■

⁴⁵ See Sherwyn, *supra* note 4.