Session 402

Role of the In-house Attorney in Mediation and Arbitration

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Alternative Dispute Resolution Process

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Impetuous For TRW's Implementation of ADR

- Increase in employment litigation.
- Increase in litigation costs
- Jury awards driving settlement costs
- Length of litigation process
- Lack of accountability
- Gilmer decision
- Implemented prospectively 1/1/95

Process of Adoption

- Law Department initiative
- Involved Human Resources
- Surveyed employees

Communication To Employees

- Management training
- Employee video
- In-house publications
- Brochures
- Individual mailings with acknowledgment of receipt and agreement to abide by policy
- New hires sign agreement

Coverage

- **All domestic employees except:**
  - Employees covered by collective bargaining agreement
- **Mandatory coverage for employment disputes which state a legal claim and which involve:**
  - Involuntary separation
  - Discrimination or harassment based on protected status
  - Constructive discharge

Coverage

- Unit option to include other employment disputes
- Excluded:
  - Benefit disputes
  - Workers' Compensation
  - Unemployment relief
  - Injunctive relief
  - Establishment or modification of policy

Usage

- Mandatory for all covered disputes before resort to court
- No impact on individual's ability to file administrative complaint
- External Mediation - unit option

Results

- Binding on TRW if accepted by employee as complete resolution of dispute
- Employee can reject and go to court

Due Process Protections

- Right to representation
- Limited discovery
- Statute of Limitations - longer of:
  - 180 days
  - Limitations period provided by law

Arbitrator

- Joint selection
- Usually through AAA
- Arbitrator controls discovery
- Subpoenas through AAA
- Can award any remedies available in court for that cause of action
- Written decision

Costs

- Mediation - TRW pays all
- Arbitration
  - Employee pays $100 to initiate process
  - TRW pays all remaining costs (Cole decision)
  - Arbitrator can assess costs against either side.

TRW ADR Experience

- One Hundred Eleven ADR claims filed
  -Types of claims
  - 15 Sexual harassment/retaliatory discharge
  - 34 Layoff/discrimination
  - 7 Denial of promotion or demotion
  - 1 Equal Pay Act/Wages
  - 3 ADA/failure to accommodate
  - 2 Failure to rehire (pension)
  - 27 Discharge
  - 6 Policy/discipline
  - 12 Discrimination
  - 4 Rejected

TRW DRP Experience

- **ADR Results**
  - **Resolved**
    - 48 Resolved at mediation
    - 13 Resolved prior to arbitration
    - 12 Failed at mediation - failed to pursue
    - 3 Peer Review
    - 4 Not covered - rejected claim
    - 3 Litigation
      - Challenged ADR - 2
      - Post ADR - 1
    - 4 Arbitration Hearings Held
      - Company prevailed - 4
  - **Pending**
    - 11 Pending at mediation
    - 16 Pending at arbitration

Litigation Avoidance

- 16 Lawsuits filed and deflected into ADR
- 21 EEOC or state agency charges filed and deflected into ADR

ADR -- A COMPETITIVE IMPERATIVE FOR BUSINESS

By Todd B. Carver

The "verdict" -- or more appropriately for this topic, the "consensus" -- is in. Alternative Dispute Resolution ("ADR") is objectively a more efficient, economical and effective way to resolve disputes than litigation. Efficient dispute avoidance and resolution cannot be just a theory or buzz word any more. It is a competitive imperative! To be competitive in a world economy, or for that matter in a local economy, businesses and their lawyers can ill afford not to implement effective dispute avoidance and ADR methods.

This article discusses why ADR is imperative and how to implement it effectively. Most importantly, though, it identifies ways for businesses and business attorneys to optimize the benefits that ADR can offer.

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An Effective Alternative to Litigation is Imperative.

Law firms bill their clients, most of them businesses, more than $100 billion a year. This formidable figure does not include such other direct costs of litigation as the cost of in-house counsel or the costs of paying judgments and settlements.

The number of lawyers in America has grown to over 700,000; this is over 300 lawyers for every 100,000 in population. Japan, on the other hand, has only twelve lawyers per 100,000 people and Germany only 82. Over 18 million lawsuits are filed annually in the state court systems of the United States, and this number is growing at a rate of a million cases a year. In the last three decades there has been a 300% increase in the number of federal lawsuits filed. The courts are overwhelmed and backlogged. In some states, it takes five years just to get on a trial docket. Business people, lawyers, judges and public policy makers must now consider and address the impact that the high resource consumption of litigation inflicts upon American business' ability to compete.

According to polls, two-thirds of top U. S. corporate executives believe the U. S. civil justice system significantly hampers the ability of American companies to compete with Japanese and European rivals. A striking 83% of those executives say the fear of lawsuits has more impact on decision-making within their company today than it did ten years ago.
Businesses, large and small, multinational and local, all feel the economic and competitive impact of litigation and the threat of litigation.

About 80% of the money American businesses pay to outside counsel is for discovery. But, in Japan discovery, as American businesses and lawyers know it, doesn't even exist. American companies increasingly face claims for punitive damages. Jury trials tend to result in larger and larger and less and less predictable awards against what are perceived to be deep-pocketed, faceless corporations. Typical outside counsel fees for a company to defend even a "minor" product liability claim is $250,000. Thus, even if you "win," you don't really win. Damage awards in a typical American products liability case are $1.5 million on average, where in

Japan such awards rarely exceed $150,000.

The indirect disadvantages of litigation have as much impact as the direct ones. Litigation results in destruction of relationships with the so-called adversary, even if they are otherwise employees, suppliers, customers or potential customers. Again, even if you are right -- if you "win" -- you often don't really win when the relationship is destroyed. Litigation also occurs in the public eye. Even if the results of the case are not adverse, the publicity may prompt others to pursue similar claims or may nevertheless leave a misimpression of the business or its brands' reputation. The time of executives, sales people, service providers and product developers is diverted from their normal responsibilities which should be creating revenue and enhancing competitiveness to rehashing the past. Again, even if you "win," you often don't really win.

"Great," you say, "here's another article professing that things will be the way they are until the government overhauls the entire American justice system . . . WRONG. American business cannot afford to wait on government or others. Businesses are in significant part in control of their own destiny regarding most disputes -- if they want to control it; if they decide to control it; if they act to control it, they can. Indeed, given the "competitive imperative." evidenced above, American businesses must take control over such disputes.

Businesses Can Take Control of Disputes.

The vast majority of business relationships are contractual -- relationships with employees, suppliers, dealers, distributors, creditors, debtors, insurers, contractors, subcontractors, customers and many others. These relationships are all generally governed by some form of contract. Thus, the contract is the primary place where businesses can gain control over disputes.

Control must start with (1) solid contract clauses such as clearly defined duties and remedies, expressed parameters to damages and precise indemnities; (2) improved product/service quality; and (3) truthfulness in business dealings. But, those alone have been insufficient to curb the tide and high cost of litigation. To avoid the high cost of litigation and the competitive disadvantages that result from it, commercial contracts must specifically contemplate and provide

for efficient dispute avoidance and resolution processes, and they must include optimal ADR clauses.

Businesses Must Adopt Dispute Avoidance and Resolution As A Business "Philosophy."

> A respected attorney once admonished other lawyers as follows:
>
> Discourage litigation. Persuade your neighbors to compromise whenever you can. Point out to them how the nominal winner is often a real loser --in fees, expenses and waste of time. As peacemaker the lawyer has a superior opportunity of being a good man. There will be business enough.

The lawyer who gave this advice was Abraham Lincoln and although his words are nearly 140 years old, they are more true now than ever.

Thus, along with taking control of disputes by implementing dispute avoidance processes and ADR clauses, businesses must also fundamentally change their philosophy. To become less litigious, businesses must be less litigious, and must convince others, for example their lawyers, to act less litigious, as well. Businesses must embrace a non-adversarial dispute avoidance and resolution philosophy, which simply put is: "It may cost us money to avoid or settle disputes, but the ideal is to coexist and win that money back on future deals."

Businesses must re-define success not by the cases fought or won, but by the disputes avoided, the costs saved and the business relationships preserved to long-term competitive advantages. To achieve this philosophical change American businesses must view ADR not as the "alternative" method of resolving disputes, but as the primary and preferred method.

In-house counsel, business attorneys and business executives must lead the charge. They must be advocates for fundamental change. Attorneys must assist their business clients in organizing for dispute avoidance and ADR, and counsel their business clients to include ADR clauses in most if not all of their contracts. This presents an exciting, challenging and unique opportunity for true leadership by business executives, business consultants and business attorneys. We can have a direct and significant impact on the way America does business, on business' "bottom line," on American competitiveness, on American business philosophy, and on business relationships with employees, suppliers and, most importantly, customers.

ADR Is The Best Alternative.

Dispute avoidance and ADR are no longer and should no longer be mere buzz words or the Total Quality Management Process of the month. They are being implemented and must be implemented to overcome the competitive disadvantages of litigation. Over 600 major corporations, including Aetna, AT&T, Apple, Chevron, DuPont, Hewlett-Packard, ITT, Ford, Mead, NCR, Norwest, RJR Nabisco, Safeway, Sears, Textron, Union Pacific, U.S. West, Wal-Mart, Whirlpool, Xerox and Zenith to name just a few, have adopted the Center for Public Resources' Policy Statement pledging to implement ADR. The American Arbitration Association has a well-established infrastructure that enables businesses to rather easily and inexpensively implement ADR. A variety of other ADR-facilitating organizations have been established, ranging from court and community sponsored programs, to firms of private judges, to mediation firms.

Litigation attorneys are being trained in ADR, and some firms now have ADR specialists who attempt to resolve disputes while the litigators pound away, or better yet before the litigators even get involved. Bar associations across the nation have endorsed ADR. Some have gone so far as to say that a lawyer's failure to counsel a client on ADR is a breach of professional duty. Accounting and consulting firms have recognized the value of ADR, are promoting it as an effective way to conduct business, and are providing consulting on implementation of ADR and dispute avoidance processes. Articles and seminars on ADR abound. Somewhat ironically in name, even the National Institute for Trial Advocacy now sponsors an ADR program. Law schools and universities have established journals, curricula, certificate programs and even graduate degrees in ADR and dispute/conflict resolution.

Federal and state law has emerged to liberally uphold the enforceability of arbitration and other out-of-court dispute resolution procedures. For example, the Federal Arbitration Act requires courts to compel arbitration and suspend court proceedings where parties to a contract involving any form of interstate commerce have included an arbitration clause in the contract. Some 45 states have enacted versions of the Uniform Arbitration Act, which likewise requires

enforcement of agreements to arbitrate. Both the federal and state Arbitration Acts include provisions that strictly limit the grounds upon which arbitration awards can be challenged, thus limiting the likelihood and wasted time and resource consumption of appeals.

ADR's time has come. American business is beginning to use it in volume, should use it, and in view of the competitive imperative must use it. But, despite the increased need for ADR, the increased infrastructure to enable ADR and the increased use of ADR, few businesses fully realize the optimal degree of benefits and competitive enhancement ADR has to offer.

In taking control over disputes, businesses must do so thoroughly and effectively. The remainder of this article provides suggestions on how to do so.

ADR Must Be Implemented More Effectively Than Currently Practiced.

In many instances ADR is implemented as a privatized judicial system that perpetuates many of the disadvantages of litigation. ADR often includes an over abundance of lawyering; discovery; depositions; judges; court reporters; motions; briefs; publicity; damage awards inconsistent with contractual language; excessive adversarial-ness; punitive damages; expert witnesses; counter-experts; and, in some instances, arbitrators or neutrals who are unqualified or who fail to implement ADR in optimal ways consistent with ADR's philosophical underpinnings. While occasionally litigation burdens may be necessary and worth their cost, rarely are they necessary or worth their cost in a typical, garden-variety dispute. To be a truly effective alternative to litigation, ADR must eliminate or limit these burdens.

For example, as mentioned above, discovery comprises about 80% of outside legal fees. If discovery is limited in the ADR process, then significant cost savings can be achieved. If in-house attorneys or business people handle disputes without significant involvement of outside counsel, further cost reductions can be achieved. If the ADR clause requires the parties to meet and attempt to negotiate solutions before relations are severed or before adversarial positions are entrenched, further savings can be achieved and better mutual solutions can be found. Likewise, requiring mediation before arbitration can result in more effective and efficient dispute resolutions. If effective "dispute avoidance" systems are adopted and implemented, then the

parties will be able to avoid the costs not only of litigation, but the costs of structured ADR as well.

If the "baggage" of litigation is brought "aboard the ADR train," then the ADR train will be as slow and expensive as litigation or, at best, only marginal benefits will be achieved over litigation. In order to maximize the benefits of ADR, businesses using it and attorneys practicing it for them need to rid it of the excess baggage of litigation. Businesses must take affirmative steps to enhance the cost-effectiveness of ADR, as well as the effectiveness of the resulting solutions. The places to start to gain control over and enhance ADR are in internal processes and in written contracts.

How to Maximize the Benefits of ADR.

1. Develop and Implement Systematic Dispute Avoidance and Resolution Processes.

The first step to maximizing the benefits of ADR is organizing and implementing internal processes to avoid disputes in the first place, and to see that they are addressed quickly, efficiently and effectively when they do arise.

· **Make Disnute Avoidance and Resolution a Kev Part of Someone's Job.**

Businesses should develop and implement Dispute Avoidance and Resolution Processes ("DARPs"). These processes should require all claims by or against the company be recorded and monitored by a person or single group of people whose job it is to resolve disputes in ways consistent with the philosophies discussed above. These people --be they contract managers, human resources managers, in-house lawyers or others (referred to collectively as "ombuds" or "case managers" throughout the remainder of this article) -- should be trained in problem-solving, dispute avoidance, negotiation and dispute resolution, not just in litigation or risk management. Their performance should be measured by the number of matters resolved, the number resolved without escalation to litigation, the quality of the solutions *(i.e.,* do they include win/win opportunities?), the permanence of the solutions *(i.e.,* was a settlement release signed?), whether they have identified ways to avoid other similar disputes from arising *(i.e.,* have they conducted an effective root cause analysis?), costs saved and how quickly they resolve disputes. Thus, dispute avoidance, not just dispute resolution, is made an important element in the process.

Disputes must be systematically managed by ombuds chartered and empowered to resolve them. Dispute resolution should not be assigned to people whose primary responsibilities and performance measurements are inconsistent with dedicating time and effort toward avoiding and resolving disputes. For example, sales people who are measured and compensated by the business they generate and the sales they make, generally should not be given primary dispute avoidance and resolution responsibilities with respect to the customer they serve -- often they are less able and motivated to effectively avoid and resolve disputes and, given that dispute avoidance and resolution takes time away from sales, they typically have disincentives to spend time and energy on dispute avoidance and resolution. (Separating the dispute avoidance and resolution responsibilities from other general business responsibilities may

also help establish that ombuds' records will be legally recognized as "work product" or "privileged" documents that will not be subject to discovery or admissibility in the event of litigation.)

This is not to say that those responsible for causing disputes in the first place should not be held accountable. Nor is this to say that normal contact person, for example the sales representative, should not play a key role in the dispute avoidance and resolution process. While the case managers should be responsible for the Dispute Avoidance and Resolution Process, they should enlist the most effective and efficient resources available, which may include people who have other responsibilities, such as the sales representative in a customer dispute or the human resources manager or supervisor in an employment dispute.

· **Define the Process with Particularity**. Disputes should not be allowed to fester, go unreported, be unaccounted for or go unmeasured. The DARP should be in writing, and should define time parameters within which the steps of dispute avoidance and resolution should occur and establish objective measurement criteria to evaluate effectiveness. For example, the DARP should require that all disputes be reported to the case managers within a short time *(e.g.,* one day within receipt of any form notice of a dispute or potential dispute). Case managers should record the dispute, such as in a computerized dispute database. They should alert all who should know of the dispute or who might help avoid or resolve it (*e.g.,* management, the account representatives, lawyers). The case manager should contact the other party quickly *(e.g.,* within three days of the ombud's receipt), identify the case manager as the contact point, and inform them that the problem is being investigated and will be addressed quickly in a problem-solving oriented way. This initial contact may help set a constructive solution-oriented tone and allow the ombud to discover the true underlying interests of the other party.

Case managers should conduct objective investigations, including good and bad, within a designated time frame *(e.g.,* 30 days). They should analyze the problems, assess the risks, brainstorm for solution alternatives and conduct root cause analyses (sharing the results with those empowered to resolve the root cause). Upon completion of the investigation and assessment, he or she should review the matter with management, recommend approaches, obtain

appropriate authority and develop a plan to achieve resolution.

Case managers and those they select as the most effective and efficient dispute resolution resources, should then proceed with discussions and negotiations with the other party in efforts to quickly and affordably resolve the problem to the best possible mutually satisfactory result. Often times responsiveness and communication go a long way toward effective dispute resolution. Where the parties agree on a solution, ombuds should see that the solution is documented. For example, if legal claims are involved a written settlement release normally should be obtained; or if one party is to do certain things, those things should be detailed in writing along with completion dates and mechanisms by which completion will be deemed fulfilled.

Given American culture (some will not have adopted the philosophical change discussed above), some cases will not be resolvable through negotiation. Ombuds should therefore introduce and pursue ADR early in the process. Even if the dispute proceeds to structured ADR or litigation, ombuds should continuously pursue negotiated, problem-solving solutions early, often and on many fronts.

A parallel process should be followed where the business is the claimant or dissatisfied party. Ombuds should serve as the focal point for gathering, recording, evaluating and communicating with the other party concerning the problem or potential problem and for effective solutions without litigation. By implementing such a process where the business is the dissatisfied party, the parties might resolve or avoid problems that would otherwise escalate or destroy relationships. It also lends some degree of objectivity in evaluating potential claims and adds fresh input from a trained problem-solver.

The DARP should be continuously evaluated, measured and improved. "Post- mortem" reviews of all disputes are effective and essential tools in continuously improving the process.

2. Include ADR Clauses in Contracts.

To assure that others adopt the dispute avoidance and resolution philosophy and practices discussed above, businesses should include ADR provisions in most if not all of their

written contracts. Inclusion of dispute avoidance/ADR clauses should be the rule rather than the exception. Businesses should make ADR the preferred and systematic way of doing business, not the "alternative" way.

To be truly effective and efficient, ADR clauses should not designate binding adjudication by a third party, such as arbitration, as the first step in the process. Before requiring the parties to resort to decision-making by someone else, the dispute resolution clause should require the parties to first negotiate, have representatives for each meet face-to-face and attempt to resolve differences between themselves, or submit the dispute to non-binding mediation or evaluation by a neutral. These initial steps are speedier, more cost-effective, more likely to result in solutions that meet all parties' needs, less likely to focus on legal damages, less likely to require involvement by outside attorneys and more likely to preserve relationships than forms of more structured ADR like arbitration and mini-trial.

The ADR clause must, however, provide for some form of final and binding resolution process. Thus, third-party adjudication is an essential step of any effective ADR clause; but, for the effectiveness and efficiency of dispute avoidance and ADR to be more fully realized, it should be a secondary step -- not the first one.

3. Propose ADR in Existing Litigation Matters.

It is never too late to resort to ADR. Even where litigation has been filed or appeals of court decisions are pending, ADR can be used effectively. The Dispute Avoidance and Resolution Process should require that ADR be sought continuously in every dispute. Thus, even if the parties have not entered a pre-dispute ADR agreement they can resort to ADR by agreement.

Some court or agency annexed ADR programs require parties to resort to ADR absent a pre-dispute ADR agreement. However, more often than not in court/agency annexed ADR programs, unless the parties have agreed to participate in ADR they cannot be compelled to do

so or the results of the ADR process are treated as non-binding. This demonstrates the importance of including ADR clauses in the contract before a dispute has arisen. Part of the challenge in getting disputes to ADR in the absence of a pre-dispute ADR agreement is convincing the other party that they stand to benefit from the process. Often this can be accomplished by referring them to ADR articles, ADR facilitating organizations, others who have engaged in the ADR process, the list of signatories to CPR's ADR policy and by offering them tangible benefits for participating in ADR *(e.g.,* reducing or capping the amount of the claim; agreeing to pay the initial ADR filing fees [these may be far cheaper concessions than the cost of litigating and "winning" -- remember, as discussed above, even if you nominally "win," often you don't really "win"]).

4. Improve the Quality of ADR Clauses.

Many businesses that adopt the dispute avoidance and resolution philosophy and practices discussed above still do not achieve optimal results from ADR. Often optimal results are not achieved because too much litigation "baggage" persists in structured ADR. Businesses and their lawyers can take control of this too by expressly limiting or eliminating the disadvantages of litigation in the dispute resolution clause itself.

For optimal effectiveness and efficiency, the dispute resolution clause can address such issues as:

- whether non-contract claims are to be resolved by ADR (which typically they should);
- whether the clause applies to associated individuals and entities (which typically they should);
- where the formal hearing will be held (designation of the hearing location to be in the non-claimant's home city may help avoid or create a disincentive for escalation of the dispute);
- what the neutral's or arbitrator's qualifications will be;
- whether the proceeding will be treated with confidentiality (which typically it should);
- whether the arbitrator will have the power to grant injunctive relief;
- whether challenges to arbitrability will be governed by federal arbitration law (the clause can also include a disincentive for court challenge of arbitrability by requiring the challenger to pay costs and attorney fees if he loses the challenge);
- whether the arbitrator shall be bound by the substantive law of a particular state;
- whether the parties will bear their own costs;
- whether and to what extent discovery will be permitted (which typically should be limited, but may provide for some pre-hearing exhibit exchanges to limit "trial by ambush" concerns);
- setting time parameters and limitations;
- whether the arbitrator has the power to award damages beyond the express limitations in the contract or award punitive damages (which typically he should not in commercial contracts where the parties are attempting to allocate economic risk with some degree of contractual certainty); and,
- satisfying due process protocol criteria for employment related disputes.

The model commercial dispute resolution clause recited in the appendix to this article includes provisions for most of these points. Not only does inclusion of these provisions help limit or eliminate many of the disadvantages of litigation, it leaves less room for legal challenges to

ADR and resource-wasting self-serving maneuvers. More importantly, it sets the philosophical tone of how disputes and ADR will be handled before a dispute arises, and it provides some degree of certainty to the parties.

5. Improve the Effectiveness and Efficiency of ADR Practices and Procedures.

Where the ADR clause does not address the points discussed in the preceding section, the participants in ADR should attempt to have the parties agree to similar provisions or even ask the arbitrator to order their implementation during the ADR process. Conduct during ADR, post-dispute ADR agreements and supplemental ADR stipulations thus can all help optimize the benefits of ADR.

Additionally, the parties should act consciously to streamline the ADR process and avoid bad habits developed from litigation. Parties should stipulate to undisputed facts and law, and not repetitiously present them to the neutral or arbitrator. Where the relevant facts are undisputed and where legal issues may be dispositive of the case or certain issues in the case, the parties should request of the arbitrator (and the arbitrator should agree) to rule on those issues in summary form, without evidentiary hearing. If the arbitrator is predisposed to hear the evidence first irrespective of potentially dispositive legal issues, then the arbitrator should clearly say so and generally the parties should not waste the time and resources to submit preheating motions on those issues. In short, motion practice should be used in ADR only where it will likely enhance the effectiveness and efficiency of the procedure not just as a normal step as is customary in litigation.

In some instances, briefs might not be necessary at all in ADR. Businesses should not spend the time and resources on them if they are unnecessary. Even when briefs are appropriate, not every factual and legal tidbit needs to be fully briefed. Again, stipulations can avoid many pages of briefs. The parties should ask the arbitrator what issues he would like the parties to brief. Not only will this give the parties an idea of the areas of interest and concern to the arbitrator, it will reduce the time and expense of briefing issues that the arbitrator does not need or want to hear more about. Arbitrators should be asked to set page limits on briefs; this too will help save costs and focus all participants on the key issues in controversy.

Prehearing exhibit and witness list exchanges enable and sometimes force the parties and the arbitrator to be better prepared. This results in more effective and efficient proceedings,

without the waste and burden of full-blown discovery. Many peripheral witnesses can submit testimony by affidavit or telephone. This, too, can streamline the ADR process.

Often, because of well drafted damage limitations that are expressly incorporated into the ADR clause or because there is no legitimate argument concerning amounts in dispute, there is no need to go into extensive damages proof. The parties can stipulate to the amount of damages or remedies or the arbitrator can rule on the effectiveness of damage limitations before hearing damages evidence. Even where damages cannot be agreed upon, damage "floors" and "ceilings" might be agreed upon by the parties or they can agree to "baseball" arbitration as a means of keeping damage/remedy claims and issues at a more realistic level than typically found in litigation. Also, if the damages evidence is voluminous, the parties and arbitrators should consider bifurcating the hearing into two separate proceedings -- one to determine liability; the other to determine damages/remedies. This can eliminate the wasted time and expense of damage proofs, damage witnesses and damage experts in cases where the claimant does not prevail, on the liability claim. Moreover, once the liability issue is resolved, the parties may be more likely to negotiate settlement on damages among themselves.

With respect to damages, the parties might agree to a single neutral damages expert to evaluate damages, rather than each party retaining their own expert that may be pre-disposed to support their client and which almost invariably results in conflicting testimony. Not only does a single neutral expert result in greater objectivity, the use of one expert is far more economical than each party employing its own. The neutral expert's report is more likely to result in the parties negotiating a solution to damages issues than is the case with extremely divergent reports from various experts with client relationships at stake. Also, where the arbitrator is specialized in the industry from which the dispute arises *(e.g.,* architecture, computers, construction, textiles, etc.), is a lawyer or is otherwise not well versed in economics, accounting, and financial analysis, the use of a supplemental neutral damages expert can provide better informed and reasoned damages assessments.

The parties may likewise agree to additional types of neutral experts *(e.g.,* accident investigation/reconstruction; fire origin; audits/accountings; technical issues) to lend more

objectivity and economy to the ADR process than is typically found in litigation. The parties themselves can help enhance the effectiveness of the neutral expert's evaluation by providing information to him and by submitting key questions that should be answered by the expert. Neutral expert evaluations may even address issues not directly in controversy. For example, the neutral expert may also be used to recommend improvements to products and practices, or for root-cause-analysis purposes. Thus, the money spent on technical experts might result in something more valuable than a self-serving litigation opinion, it might be used as an instrument for positive change and avoidance of future disputes.

6. Improve ADR Infrastructure.

ADR can be maximized only to the extent that ADR-facilitating organizations and the law permit the parties to limit or eliminate the disadvantages of litigation. ADR-facilitating organizations therefore need -- and businesses and lawyers that use ADR-facilitating organizations need to influence ADR-facilitating organizations to incorporate effective and efficient ADR practices and procedures, such as those outlined above, as part of the ADR-facilitating organization's standard rules, practices and procedures.

Arbitrators should be trained to routinely implement and require such practices and procedures. They should not permit broad discovery and should order proceedings to be confidential, unless all parties agree otherwise. Arbitrators should honor both the express terms and philosophical spirit of the ADR clause. They should consciously resolve to rid the ADR process of the burdens of litigation. They should not award damages outside of those permitted by the contract or the dispute resolution clause. The arbitrator training process must foster change in arbitrators' philosophy toward dispute resolution -- many arbitrators are lawyers and litigators who bring or allow the parties' attorneys to bring the bad habits of litigation into the

ADR process. In short, ADR-facilitating organizations must act to achieve fundamental philosophical consistency among arbitrators.

Courts should rigorously enforce arbitration agreements and impose sanctions upon those who refuse to honor their pre-dispute ADR agreements without first being ordered by a court to do so. Courts should also normally vigorously uphold arbitrators' awards, but should not hesitate to vacate or modify them in extraordinary circumstances such as where the arbitrator clearly acts beyond the authority granted by the contract from which his powers arise, such as in awarding more damages than the contract permits.

Conclusion

A competitive imperative requires American businesses to effectively use ADR. American businesses are increasingly using ADR, but have tended to transport many of the disadvantages of litigation into the ADR process. Because of this litigation "baggage," businesses rarely maximize the potential benefits ADR has to offer. Businesses can respond to the competitive imperative and take control. They can enhance the effectiveness of ADR through philosophical changes to the way they approach disputes, through improved and innovative internal Dispute Avoidance and Resolution Processes, and through improved dispute resolution clauses. ADR infrastructure-providers and policy-makers can enhance the benefits to be achieved from ADR through adopting policies, practices and procedures that better foster elimination of litigation "baggage" from the ADR process, through training and requiring arbitrators to reduce to practice the philosophies which underlie ADR, and through penalizing those who resist ADR after they have entered binding contracts that include ADR clauses.

If your business/client doesn't already use dispute avoidance processes and ADR, it should. If it already uses ADR occasionally, it should systematize its use of into an overall dispute avoidance and resolution philosophy and process, and should systematically include ADR clauses in its contracts. If it systematically uses dispute avoidance and ADR, it should improve its ADR clauses and practices so as to optimize the benefits ADR has to offer. We must

all encourage ADR-facilitating organizations and policy-makers to adhere to and enforce policies, practices and procedures that maximize the efficiency and effectiveness of ADR and that limit or eliminate the burdens of litigation. Even with some shortcomings, irrespective of imperfect implementation, and regardless of the criticisms of the dispute avoidance and resolution philosophy and of ADR, they sure beat the "alternative." TAKE CONTROL OF YOUR DISPUTES NOW; IT'S IMPERATIVE.

Todd B. Carver

Sample 3-Step Commercial Alternative Dispute Resolution Clauses

Short Version:

Any controversy or claim between the parties to this Agreement, including but not limited to those arising out of or related to this Agreement and regardless of the causes of action alleged, shall be resolved by arbitration before a sole arbitrator in -- pursuant to the then-current Commercial Rules of the American Arbitration Association. Before the filing of any arbitration demand, however, the parties shall attempt in good faith m negotiate a solution to their differences and, if negotiation does not resolve their differences, the parties agree to attempt in good faith to resolve their differences through participating in mediation as administered by the American Arbitration Association. If the matter proceeds to arbitration, the arbitrator's award will be final and binding, and may be entered in any court having jurisdiction thereof, but in no event can an award exceed the amount of direct compensatory damages actually incurred by the claiming party as is consistent with the damages limitations in this Agreement. Each party will bear its own attorney's fees and costs related to the arbitration. Any claim or action must be brought within one year after the cause of action accrues.

Longer Version

Section _____: Alternative Dispute Resolution

[a] Any controversy or claim arising between the parties to this Agreement, including but not limited to those arising out of or related to this Agreement, which cannot be settled by negotiation or mediation, whether based on contract, tort, statute, or other legal theory and any claim of infringement, fraud or misrepresentation, shall be resolved by arbitration pursuant to this section and the then-current Commercial Rules and supervision of the American Arbitration Association. Other than as expressly set forth below with respect to claims of irreparable harm, before the filing of any arbitration demand, the parties shall attempt in good faith to negotiate a solution to their differences and, if negotiation does not resolve their differences, the parties agree to attempt in good faith to resolve their differences through participating in mediation as administered by the American Arbitration Association. The duty to arbitrate shall extend to any employee, officer, shareholder, agent, or affiliate of a party hereto making or defending a claim which would be subject to arbitration if brought by a party hereto. If any part of this section is held to be unenforceable, it shall be severed and shall not affect either the duty to arbitrate hereunder or any other part of this section.

[b] The arbitration shall be held in [**alternate A - other party has US presence:** the US headquarters city of the party not initiating the claim [**alternate B** - other party has no US presence: New York, New York] before a sole arbitrator who is knowledgeable in business information and electronic data processing systems. The arbitrator's award shall be final and binding and may be entered in any court having jurisdiction thereof. The arbitrator shall not have the power to award punitive or exemplary damages, or any damages excluded by, or in excess of, any damage limitations expressed in this Agreement. Issues of arbitrability shall be determined in

accordance solely with the federal substantive and procedural laws relating to arbitration; otherwise, the arbitrator shall be obligated to apply and follow the substantive law of the choice of law state/nation specified in this Agreement, and if no choice of law state/nation is specified, then the arbitrator shall be obligated to apply and follow the substantive law of the State of New York. Each party shall bear its own attorney's fees associated with the arbitration and other costs and expenses of the arbitration shall be borne as provided by the rules of the American Arbitration Association.

[c] No party may bring a claim or action regardless of form, arising out of or related to this Agreement, including any claim or fraud or misrepresentation, more than one year after the delivery of any goods or services at issue or more than one year after the cause of action accrues, whichever is later.

[d] If court proceedings to stay litigation or compel arbitration are necessary, the party who unsuccessfully opposes such proceedings shall pay all associated costs, expenses and attorney's fees which are reasonably incurred by the other party.

[e] The arbitrator may order the parties to exchange copies of non-rebuttal exhibits and copies of witness lists in advance of the arbitration hearing. However, the arbitrator shall have no other power to order discovery or depositions unless and then only to the extent that all parties otherwise agree in writing.

[f] Neither a party, a witness, nor the arbitrator may disclose the contents or results of any arbitration hereunder without prior written consent of all parties, unless and then only to the extent required to enforce or challenge the award, as required by law, or as necessary for financial and tax reports and audits.

[g] In order to prevent irreparable harm, a party may elect not to first participate in negotiate or mediate the dispute in advance of filing an arbitration demand and the arbitrator may grant temporary or permanent injunctive or other equitable relief for the protection of intellectual property rights. Notwithstanding anything to the contrary in this Section, in the event of alleged violation of a party's intellectual property rights (including but not limited to unauthorized disclosure of confidential information), that party may seek temporary injunctive relief from any court of competent jurisdiction pending appointment of an arbitrator. The party requesting such relief shall simultaneously file a demand for arbitration of the dispute, and shall request the American Arbitration Association to proceed under its rules for expedited hearing. In no event shall any such temporary injunctive relief continue for more than 30 days.

CURRENT ISSUES IN EMPLOYMENT ARBITRATION

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In 1991, the Supreme Court ruled in *Gilmer v. Interstate/Johnson Lane Corp.,* 500 U.S. 20, 111 S.Ct. 1647, 114 L.Ed.2d 26 (1991) that an employee could be required to arbitrate a claim under the Age Discrimination in Employment Act. This ruling was foreshadowed by a series of decisions in which the Court held that the pro-arbitration policy embodied in the Federal Arbitration Act, 9 U.S.C. §1 *et seq.* (FAA), supported the conclusion that arbitration provides an appropriate forum to determine statutory claims.[1] The Court has also held that state statutes that require litigation of statutory claims are preempted by the FAA.[2]

Despite *Gilmer*, the Equal Employment Opportunity Commission and counsel representing employees have continued to object to mandatory arbitration of statutory claims such as Title VII, ADA, and ADEA. In recent years, they have been most successful in advancing these views before the Ninth Circuit. This paper will discuss the following issues:

- Whether the FAA is applicable to arbitration provisions in employment agreements
- Whether the FAA requires arbitration of Title VII and other employment discrimination claims
- Whether there is a requirement that the waiver of a judicial forum must be "knowing" and whether the arbitration agreement must contain explicit reference to specific statutory claims
- Whether an arbitration agreement must be "fair" in order to be enforceable
- Whether an employee is required to pursue arbitration instead of a complaint before the EEOC or a state civil rights commission
- Whether the existence of an arbitration agreement between the claimant and the employer bars the EEOC from seeking damages for the employee
- Whether state statutes may bar employers from including mandatory arbitration provisions in employment agreements

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[1] *Mitsubishi v. Soler Chrysler-Plymouth,* 473 U.S. 614, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985) Sherman Act, 15 U.S.C. §1 *et seq.*; *Shearson/American Express, Inc*. v. *McMahon,* 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987) (§10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b); and *Rodriguez de Quijas v. Shearson-American Express, Inc.*, 490 U.S. 477, 109 S.Ct. 1917, 104 L.Ed.2d 444 (1989) §12(2) of the Securities Act of 1933, 15 U.S.C. §77(2) and the civil provisions of the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §1961 *et seq.*

[2] See, e.g., in the employment context, *Perry v. Thomas,* 482 U.S. 483, 107 S.Ct. 1520, 96 L.Ed.2d 426 (1987)

Whether the FAA is applicable to arbitration provisions in employment agreements

Section 1 of the FAA, 9 U.S.C. §1 provides in part that "nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." Employees seeking to avoid arbitration have argued that this exception to the applicability of the FAA should be broadly construed to apply to employees of all types. The issue was not decided in *Gilmer*, both because the issue was not raised by the employee in the lower courts and because the arbitration agreement was contained in the "U-4" securities registration application. 500 U.S. at 25, fn. 2 Justice Stevens in dissent, joined by Justice Marshall, concluded, based on the Congressional Record, that "the FAA was specifically intended to exclude arbitration agreements between employers and employees" and that "the exclusion in § 1 should be interpreted to cover any agreements by the employee to arbitrate disputes with the employer arising out of the employment relationship, particularly when such agreements to arbitrate are conditions of employment." 500 U.S. at 40.

Both before and after *Gilmer*, this argument has been generally rejected. Instead, the exception has been narrowly construed to apply only to workers actually engaged in the *movement* of goods in commerce.[3] However, this issue has never been ruled on by the Supreme Court and the argument in favor of a broad exception for employment agreements continues to be asserted, and on occasion accepted. The most significant example of this is the Ninth Circuit's 2-1 decision in *Craft v. Campbell Soup Co.,* 161 F.3d 1199 (9h Cir. 1998).

The majority in Craft fashioned a second argument against the applicability of the FAA to arbitration provisions in employment agreements, based on § 2 of the FAA, 9 U.S.C. §2. That section makes enforceable agreements to arbitrate which are contained in a "written provision in any *maritime transaction or a contract evidencing a*

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[3] See, e.g., *McWilliams* v. *Logicon, Inc.,* 143 F.3d 573 (10th Cir. 1998); *Miller v. Public Storage Management, Inc.,* 121 F.3d 215 (5th Cir. 1997); *O'Neil v. Hilton Head Hospital,* 115 F.3d 272, 274 (4th Cir. 1997); *Patterson v. Tenet Healthcare, Inc.,* 113 F.3d 832, 835-37 (8th Cir. 1997) (overruling the pre-*Gilmer* decision in *Swenson v. Management Recruiters Int'l, Inc.,* 858 F.2d 1304 (8th Cir. 1988); *Cole v. Burns Int'l Sec. Servs.,* 105 F.3d 1465, 1470-71 (D.C. Cir. 1997); *Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222, 227 (3d Cir.). cert. denied, 118 S. Ct. 299 (1997); *Rojas v. TK Communications, Inc.,* 87 F.3d 745, 747-48 (5th Cir. 1996); *Asplundh Tree Expert Co. v. Bates*, 71 F.3d 592, 600 (6th Cir. 1995); *Miller Brewing Co. v. Brewery Workers Local Union No. 9, AFL-CIO,* 739 F.2d 1159, 1162 (7th Cir. 1984), cert. denied, 469 U.S. 1160 (1985); *Erving v. Virginia Squires Basketball Club,* 468 F.2d 1064, 1069 (2d Cir. 1972); *Dickstein v. duPont*, 443 F.2d 783, 785 (1st Cir. 1971); *Tenney Engineering, Inc. v. United Elec. Radio & Machine Workers, Local 437,* 207 F.2d 450, 453 (3rd Cir. 1953 (en banc); see also *Paladino v. Avnet Computer Tech., Inc.,* 134 F.3d 1054, 1069-61 (11th Cir. 1998) (Cox, J., for the majority of the Court). See also, *Grohn v. Sisters of Charity Health Services Colorado,* 960 P.2d 722, 726-27 (Colo.App. 1998)

transaction involving commerce…." (So emphasized in *Craft,* 161 F.3d at 1201) After a lengthy discussion of the meaning of "commerce" and "transaction", the understanding of Congress of "interstate commerce" in 1925, when it enacted the FAA, and the legislative history of the Act, the majority concluded that the FAA was intended to be applicable only to disputes between merchants and not to disputes involving employees. It further concluded that an employment agreement could not be a "transaction involving commerce" and held that:

> "Based on the wording of § 2, the pre-New Deal understanding of the Commerce Clause, the legislative history of the FAA, and the suggestions gleaned from *Lincoln Mills, Gilmer,* and *Terminix,* we hold that the FAA does not apply to labor or employment contracts."[4]

161 F.3d at 1206 *Craft* was criticized in *Koveleskie, supra,* 167 F.3d at 363.

As a result, in the Federal courts of the Ninth Circuit, the FAA will not be applied to employment agreements.

Whether the FAA requires arbitration of Title VII and other employment discrimination claims

In the years after *Gilmer*, the courts generally held that a pre-dispute arbitration agreement would be enforced to require arbitration of claims of employment discrimination under Title VII of the Civil Rights Act of 1964 and other Federal and state civil rights statutes, including ADEA, ADA, and FMLA.[5]

The EEOC has continued to oppose the use of arbitration provisions in employment agreements as a basis for requiring arbitration of Title VII claims. Since the Court has held that statutory claims are not subject to the FAA when Congress has clearly evinced its intent that such claims may only be litigated, the EEOC has argued that Congress has evinced such an intent in its passage of the Civil Rights Act of 1991, Pub. L. No. 102-166, 105 Stat. 1071. The Ninth Circuit accepted this argument last year *Duffield* v. *Robertson Stephens & Co.,* 144 F.3d 1182, 1189-1200 (9th Cir. 1998), *cert. denied,* __ U.S. __, 119 S.Ct. 465, 142 L.Ed.2d 418 (1998), __ U.S. __, 119 S.Ct. 445, 142 L.Ed.2d 319 (1998)..

However, most courts have rejected the EEOC's argument and held that Title VII claims are subject to arbitration under pre-dispute agreements. The Fourth Circuit, while

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[4] *Textile Workers Union v. Lincoln Mills,* 353 U.S. 448, 77 S.Ct. 912, 1 L.Ed.2d 972 (1957); *Gilmer, supra*; and *Allied-Bruce Terminix Cos. v. Dobson,* 513 U.S. 265, 115 S.Ct. 834, 130 L.Ed.2d 753 (1995)

[5] See, e.g., *Michalski v. Circuit City Stores, Inc.,* 177 F.3d 634, 637 (7th Cir. 1999) *Seus v. John Nuveen & Co., Inc.,* 146 F.3d 175, 182 (3rd Cir. 1998), cert. Denied __U.S. --, 119 S.Ct. 1028, 146 L.Ed.2d 38 (1998); *Gibson v. Neighborhood Health Clinics, Inc.,* 121 F.3d 1126, 1130 (7th Cir. 1997); *Metz v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 39 F.3d 1482, 1487 (10th Cir. 1994); *Bender v. A.G. Edwards & Sons, Inc.,* 971 F.2d 698, 700 (11th Cir. 1992); *Mago v. Shearson Lehman Hutton, Inc.,* 956 F.2d 932, 935 (9th Cir. 1992); *Willis v. Dean Witter Reynolds, Inc., 948 F.2d 305, 307* (6th Cir. 1991); *Alford v. Dean Witter Reynolds, Inc.,* 939 F.2d 229, 230 (5th Cir. 1991).

noting the *Duffield* decision, concluded that Congress *endorsed* arbitration in the Civil Rights Act of 1991, since it states that "Where appropriate and to the extent authorized by law, the use of alternative means of dispute resolution, including … arbitration is encouraged to resolve disputes arising under [Title VII]." Pub. L. No. 102-166, § 118, 105 Stat. at 1081. *Hooters of America, Inc. v. Phillips,* 173 F.3d 933, __ (4th Cir., 1999). Other Circuits have expressly declined to follow *Duffield*, on the same basis, and have instead found such disputes to be arbitrable under the FAA. The Third Circuit, in *Seus v. John Nuveen & Co.,* 146 F.3d 175, 183 (3d Cir. 1998). that "[o]n its face, the text of sec. 118 evinces a clear Congressional intent to encourage arbitration of Title VII and ADEA claims, not to preclude such arbitration," and that, with regard to the "authorized by law" language of the 1991 CRA, "it seems most reasonable to read this case as a reference to the FAA." The Fifth Circuit found this reasoning persuasive and chose to follow the Third Circuit instead of the Ninth, in *Koveleskie v. SBC Capital Markets, Inc.,* 167 F.3d 361, 365 (5th Cir. 1999). The First Circuit, in *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith Inc.,* 163 F.3d 53, 63 (1st Cir. 1999), also declined to follow *Duffield,* after an extensive discussion of the legislative history and applicable law.

The *Duffield* decision has been rejected by California appellate courts in *24 Hour Fitness, Inc. v. Superior Court,* 78 Cal.Rptr.2d 533, 539 n. 9 (Cal.App.1st Dist. 1998) and *Lee v. Technology Integration Group,* 79 FEP Cases 221, 222-23 (Cal.App. 6th Dist. 1999). This creates the anomalous situation in California that a Title VII claim brought in Federal Court will be tried even if there is an arbitration agreement, while the same claim brought in a state court will be stayed pending arbitration or even dismissed.[6]

The Third Circuit in *Seus* also considered the requirement of the Older Workers Benefit Protection Act of 1990 that rights and claims under ADEA may not be waived unless they are knowing and voluntary. 29 U.S.C. § 626(f)(1). The Court concluded that this requirement applied only to substantive rights and not to an agreement to arbitrate ADEA claims.

This issue remains open only as to arbitration agreements between the employer and the employee, and not as to arbitration provisions in collective bargaining agreements. In *Wright v. Universal Maritime Service Corp.,* __ U.S. __, 119 S.Ct. 391, 142 L.Ed.2d 361 (1998), the Supreme Court held that "a union-negotiated waiver of employees' statutory right to a judicial forum for claims of employment discrimination" must be "clear and unmistakable." 119 S.Ct. at 396. Although the Court discussed the tension between *Gilmer,* which involved an individual agreement to arbitrate, and *Alexander v. Gardner-Denver Co.,* 415 U.S. 36, 94 S.Ct. 1011, 39 L.Ed.2d 147 (1974) and its progeny, involving CBA arbitration, the Court declined to resolve the issue whether *Gilmer* has so undercut *Gardner-Denver* as to make a CBA arbitration agreement enforceable, if it contains a waiver that complies with the standard of "clear

[6] In *24 Hour Fitness, supra,* the court held that it was appropriate to grant summary judgment against the plaintiff employee when all of the issues were referable to arbitration. 78 Cal.Rptr.2d at 537, relying on C*harles J. Rounds v. Joint Council of Teamsters No. 42,* 4 Cal.3d 888, 484 P.2d 1397 (1971).

and unmistakable.[7] Nor did the Court indicate that non-CBA arbitration agreements should be held to the same high standard.

Whether there is a requirement that the waiver of a judicial forum must be "knowing" and whether the arbitration agreement must contain explicit reference to specific statutory claims

In *Prudential Insurance Co. v. Lai,* 42 F.3d 1299 (9th Cir. 1994), the majority of the Ninth Circuit panel held "that a Title VII plaintiff may only be forced to forego her statutory rights and arbitrate her claims if she has knowingly greed to submit such disputes to arbitration." 42 F.3d at 1305. This conclusion was based in part on the 1991 Civil Rights Act's endorsement in §118 of arbitration of Title VII disputes "where appropriate" and in part on a statement by Senator Dole that this section "encourages arbitration only 'where the parties knowingly and voluntarily elect to use these methods.'" *Ibid.* The majority then concluded that the plaintiff could not have known that she was agreeing to arbitrate her future Title VII claims because the U-4 form did not refer to such claims.[8] *Lai* was followed in *Renteria v. Prudential Ins. Co. of America,* 113 F.3d 1104, 1105-06 (9th Cir. 1997), describing the "knowing" requirement as a heightened standard.

Here too there is a split in the Circuits. In *Paladino, supra,* one judge stated that "To fall within the FAA's ambit, however, an arbitration agreement that purports to cover statutory claims must contain terms that generally and fairly inform the signatories that it covers statutory claims." 134 F.3d at 1059. The majority, following the Circuit's earlier decision in *Bender v. A.G. Edwards & Sons, Inc.,* 971 F.2d 698 (11th Cir. 1992), held that the broad form arbitration clause in the contract covered Title VII claims. 134 F.3d at 1061

The Third Circuit has rejected such an additional standard for enforceability of an arbitration agreement in the civil rights context, stating that it "would be inconsistent with the FAA and *Gilmer*. Nothing short of a showing of fraud, duress, mistake or some other ground recognized by the law applicable to contracts generally would have excused the district court from enforcing [the employee's] agreement. *Seus, supra,* 146 F.3d at 184-5.[9]

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[7] An example of a CBA in which the arbitration meets this standard is found in *Austin v. Owens-Brockway Container, Inc.,* 78 F.3d 875 (4th Cir. 1996). The majority of the Court concluded that "[w]hether the dispute arises under a contract of employment growing out of securities registration application, a simple employment contract, or a collective bargaining agreement, an agreement has yet been made to arbitrate the dispute. So long as the agreement is voluntary, it is valid, and we are of opinion it should be enforced." 78 F.3d at 885.

[8] The same U-4 form was before the Supreme Court in *Gilmer*, yet its omission of a reference to statutory claims created no obstacle to its enforcement.

[9] The plaintiff in *Seus* argued that a determination of whether the agreement was "knowing" and "voluntary" "requires an inquiry into such matters as the specificity of the language of the agreement, the plaintiff's education and experience, plaintiff's

The Fifth Circuit has held that that an arbitration agreement need not refer to statutory claims for them to be subject to arbitration. *Mouton v. Metropolitan Life Ins. Co.,* 147 F.3d 453 (5th Cir. 1998), following *Rojas, supra.*

The issue was discussed, but not decided, by the Seventh Circuit in *Gibson, supra,* 121 F.3d at 1129, and by the First Circuit in *Rosenberg, supra,* 170 F.3d at 17-18. The opinion in *Rosenberg* suggests that the Eighth Circuit in *Patterson, supra,* apparently rejects the requirement of a "knowing" waiver.

The California state courts also reject a requirement of a knowing waiver of claims for sexual harassment under the state's Fair Employment and Housing Act. *Lee, supra,* and cases cited at 79 FEP Cases at 224.

Further, a substantial number of decisions upholding arbitration have involved broad arbitration clauses that did not specifically refer to statutory claims.

Whether an arbitration agreement must be "fair" in order to be enforceable

The battle over arbitration does not stop with the determination by the court that Title VII and other statutory claims are covered by the FAA. Employees resisting arbitration will ask the court to scrutinize the arbitration agreement and to hold it unenforceable if it is procedurally or substantively unfair or if it limits the remedies provided by the applicable statute. As stated in *Rosenberg, supra,* 170 F.3d at 16, "*Gilmer* does not mandate enforcement of all arbitration agreements. Plaintiffs are not required to take their claims to biased panels or through biased procedures.

In *Martens v. Smith Barney, Inc.,* 181 F.R.D. 243. 255-56 (S.D.N.Y. 1998), the District Court concluded that arbitration had to meet the following minimum requirements in order to "effectively … vindicate … statutory cause[s] of action":

> "First, the arbitration must meet certain standards of procedural fairness. *See, e.g., Cole,* 105 F.3d at 1468-69 (D.C. Cir. 1997) (requiring 'reasonable right of access to a neutral forum' and meaningful review for Title VII claims);
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> "Second, the arbitration agreement cannot impose financial burdens on plaintiff access to the arbitral forum. Requiring plaintiffs to pay for access 'would surely deter the bringing of arbitration,' running counter to congressional intent underlying Title VII. *Cole,* 105 F.3d at 1468. This principle bars not only 'steep filing fees," but also 'fee-shifting' agreements in which plaintiffs pay part of the arbitrators fee. *Paladino* [*supra*].
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> "Third, the arbitration must allow remedies central to the statutory scheme. Arbitration need not provided exactly the same remedies as adjudication, but must provided remedies sufficient to satisfy statutory purposes."

In *Hooters, supra,* the Court found that there was a lack of procedural fairness. After concluding that the plaintiff's sexual harassment claim was arbitrable under the FAA, the Court reviewed the rules and regulations prescribed by the employer and found them to be so procedurally unfair as to constitute a breach by the employer of its

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opportunity for deliberation and negotiation, and whether plaintiff was encouraged to consult counsel." 146 F.3d at 183

obligations under the arbitration agreement. The Court found the provisions relating to the selection of the panel of arbitrators to be particularly egregious. While each party selected one of the three arbitrators and the two party-selected arbitrators chose the third, the third arbitrator could only be selected from a list prepared by the employer. This effectively gave the employer control over selection of the majority of the panel. Among the witnesses testifying to the unfairness of the rules were a senior vice president of the American Arbitration Association and a former president of the National Academy of Arbitrators!

Arbitration provisions have also been attacked because of contractually-imposed restrictions on remedies. Some courts have held that such restrictions render the agreement to arbitrate unenforceable. *Stirlen v. Supercuts, Inc.,* 51 Cal.App.4th 1519 (1st Dist. 1997) A different approach was taken by another California court in *Armendariz v. Foundation Health Psychcare Services, Inc.,* 98 C.D.O.S. 8919 (1st Dist. 1998). It held that the plaintiff's state discrimination claim was required to be arbitrated but struck the contract's prohibition against the arbitrator awarding punitive damages.

Further, the fairness of both the arbitration and the award itself may be subject to judicial review post-award. *Rosenberg, supra,* 170 F.3d at 16, based on a statement in a footnote to *Gilmer,* 500 U.S. at 32, n. 4.

Whether an employee is required to pursue arbitration instead of a complaint before the EEOC or a state civil rights commission

In *Gilmer,* it was argued that compelling arbitration would "undermine the role of the EEOC in enforcing the ADEA." In rejecting that argument, Justice White noted: "An individual ADEA claimant will still be free to file a charge with the EEOC, even though the claimant is not able to institute a private judicial action." 500 U.S. at 28.

Despite this *dicta*, a Minnesota appellate court has recently ruled that a claimant under the state civil rights statute can be compelled to arbitrate his claim of discrimination, even thought the Minnesota Human Rights Act, Minn. Stat. 363.11, confers exclusive jurisdiction on the Minnesota Department of Human Rights while a claim is pending before it. *Correll v. Distinctive Dental Services, P.A.,* 594 N.W.2d 222 (Minn. App. 1999), petition for review granted, July 28, 1999. The issue of whether the employment contract involved commerce was not determined by the trial court. Accordingly, the Court of Appeals assumed for purpose of its decision that it did not involve commerce and therefore the policy of the Minnesota Uniform Arbitration Act, and not the FAA, was at issue. The Court concluded that, if the FAA were applicable, arbitration would be ordered under the FAA and concluded that the same result should be reach under the Minnesota arbitration statute, particularly since the Minnesota Supreme Court had previously ruled that Title VII claims are subject to arbitration under the FAA.[10]

[10] *Johnson v. Piper Jaffray, Inc.,* 530 N.W.2d 790, 800 (Minn. 1995)

Whether the existence of an arbitration agreement between the claimant and the employer bars the EEOC from seeking damages for the employee

In *EEOC v. Kidder, Peabody & Co.,* 74 FEP Cases 1833 (S.D.N.Y. 1997), the EEOC brought an action under ADEA, seeking back pay and liquidated damages on behalf of 17 former employees of the defendant brokerage firm. All of the employees had signed securities registration arbitration agreements. The District Court dismissed the action, holding that the EEOC could not seek damages on behalf of employees who had agreed to arbitrate. (The EEOC had dropped its demand for reinstatement, so no equitable relief was being sought.) The Second Circuit affirmed, in *EEOC v. Kidder, Peabody & Co.,* 156 F.3d 298 (2nd Cir. 1998)

In *EEOC v. Frank's Nursery & Crafts, Inc.,* 966 F.Supp. 500 (E.D.Mich. 1997), the District Court dismissed an action brought by the EEOC on behalf of a former employee who complained of racial discrimination by her employer. The EEOC sought both injunctive relief and damages on her behalf and on behalf of a class of employees. The Sixth Circuit reversed in a 2-1 decision, declining to follow *Kidder, Peabody*. *EEOC v. Frank's Nursery & Crafts, Inc.,* 177 F.3d 448 (6th Cir. 1999), holding that the EEOC was not a party to the arbitration agreement and therefore was not bound by it. Even more significant to the court was the separate role given to the EEOC to enforce Title VII. Judge Nelson concurred in the holding that the EEOC retained the right to seek equitable relief against claimed discrimination, but dissented from the conclusion that the EEOC could seek monetary damages for a complainant who had agreed to arbitrate her claim. Instead, he would have followed the Second Circuit's lead.

Whether state statutes may bar employers from including mandatory arbitration provisions in employment agreements

At first blush, this would seem to be a non-issue. The FAA preempts such attempts to restrict the use of arbitration. As stated by the Supreme Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.,* 460 U.S. 1, 103 S.Ct. 927, 74 L.Ed.2d 488 (1983):

> "Section 2 [of the FAA] is a congressional declaration of a liberal federal policy favoring arbitration agreements **notwithstanding any state substantive or procedural policies to the contrary. The effect of the section is to create** a body of federal substantive law of arbitrability, applicable to <u>any</u> arbitration agreement within the coverage of the Act."

Perry v. Thomas, supra, held that the FAA preempted a California statute requiring that wage claims be resolved in a judicial forum. California Labor Code § 229.

Despite this well-settled law, the California House has passed a bill that would invalidate pre-dispute arbitration provisions contained in individual employment agreements, with a few limited exceptions.[11] It would amend the California Arbitration

[11] One exception is for employee-owned companies with at least 5,000 employees located in a "class 3 county," obviously tailored to meet the request of a particular California employer. The second applies to employment agreements where the compensation is

Act, Civil Code, §1670.1 *et seq.,* to preclude employers from requiring, or even requesting, as a condition of continued employment, an employee to agree to waive the right to a jury trial, the right to certain privileges under the Evidence Code, the right to protections under Title VII and the California Civil Rights laws, and the "right of access to a judicial forum." California Assembly Bill 858. The bill provides that "[a]ny waiver obtained in violation of this section is void and shall be deemed involuntary, beyond the reasonable expectations of the employee, and unconscionable." Further, it would impose a civil penalty of $5,000 **per violation.** Note that the bill is not limited to civil rights claims. Rather, it would be applicable to any dispute between an employer and an employee, such as enforcement of a trade secret agreement.

The bill contains no exception for contracts that would be subject to the FAA. It would seem that the FAA would preempt this bill, should it become law, as to employment agreements within its scope, under *Perry v. Thomas, supra*, unless the recent Ninth Circuit decisions discussed in this paper prove to be and remain good law. It should be noted that the Supreme Court has held, in other contexts, that statutory restrictions on how arbitration agreements must be worded violate the provisions of §2 of the FAA and are preempted. In *Doctor's Associates, Inc. v. Casarotto,* 517 U.S. 681, 1116 S.Ct. 1652, 134 L.Ed.2d 902 (1996), the Court struck down a Montana statute which required that "a notice that a contract is subject to arbitration" be "typed in underlined capital letters on the first page of the contract." In doing so, the Court quoted its opinion in *Allied-Bruce Terminix, supra,* 513 U.S. at 281, 115 S.Ct. at 843, 130 L.Ed.2d at 769:

> "States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause 'upon such grounds as exist at law or in equity for the revocation of *any* contract.' 9 U.S.C. §2 (emphasis added). What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal 'footing,' directly contrary to the Act's language and Congress's intent."

If A.B. 858 becomes law, one obvious choice is for employers to omit predispute arbitration agreements from their employment agreements. A second alternative is to include them, but to make them truly optional with the employee, with no adverse consequences as to employment or continued employment if the employee chooses not to enter into the agreement. Under such a program, the employer would have to rely on selling the benefits of arbitration in order to obtain the consent of the employee or

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over $150,000, the arbitration agreement is contained in the employment agreement and contains the title "Arbitration of Disputes" in bold or red and in at least an 8-point font, and the agreement contains a prescribed warning and acknowledgement in a prescribed appearance and is initialed by the employee. In addition, these restrictions would not be applicable to collective bargaining agreements.

applicant. The jeopardy of such an approach is that it would likely give rise to litigation over the issue of voluntariness.[12]

A third alternative would be to require arbitration which is not binding on the employee (although an employer may choose to make the result binding on itself). In this way, none of the rights sought to be safeguarded by the bill would be waived and therefore there should be no violation.[13]

A fourth alternative would be to condition the arbitration provision's effectiveness upon its being enforceable under the FAA, notwithstanding any contrary state statute. Especially if this last alternative is chosen, particular care must be given to any choice of law provision, particularly as to the choice of the arbitration act that will be applicable. As the Supreme Court held in *Volt Information Sciences v. Board of Trustees,* 498 U.S. 468, 109 S.Ct. 1248, 103 L.Ed.2d 488 (1989), a party will be held to the provisions of an arbitration act chosen to control the arbitration proceedings, even if such provisions are more restrictive than the FAA.

On September 10, 1999, the Bill was amended by the California Senate. All references to arbitration were removed and the Senate substituted a provision relating to partnership taxation and another substituting the State Treasurer for the State Controller on the Franchise Tax Board. The Assembly refused to concur in the Senate's amendments and the bill has been sent to conference.

CONCLUSION

Given the clear split in the Circuits on several of these issues and the EEOC's and the employee bar's continuing campaign against the enforcement of pre-dispute arbitration agreements, many of the issues discussed will continue to be raised until they are resolved by the Supreme Court or by Congress. However, many of the issues can be avoided by thoughtful and careful drafting. Counsel should review their company's arbitration agreements to make sure that they are procedurally and substantively fair and that they do not deprive the employee of substantive rights. Explicit and clear references to statutory claims will avoid the assertion that the agreement to arbitrate was not "knowing."

Further, proponents of arbitration should make their views heard in their state legislatures as well as in Congress, so that legislation such as California A.B. 858 does not become a pattern that would reverse the Supreme Court's endorsement of arbitration in the employment setting.

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[12] Ironically, one of the justifications contained in the bill is that the policy of the state "to encourage voluntary submission of employee claims to appropriate alternative dispute resolution mechanisms after a dispute arises" would "best be implemented with a minimum of conflict and judicial oversight…" by precluding involuntary pre-dispute agreements.

[13] See, e.g., *Michalski, supra,* where the employment agreement gave the employee the option to opt out of arbitration.

ARBITRATION AGREEMENT

THIS AGREEMENT is entered into in Cleveland, Ohio, on _____between _____ a _____ corporation (the "Company") and _____ (the "Employee");

NOW, THEREFORE, in consideration of the mutual covenants of the parties set forth in this Agreement, the parties agree as follows.

1. All controversies, claims, disputes and matters in question arising out of, or relating to, the employment of the Employee by the Company or the termination of such employment, or the Employee's Employment Agreement, or the breach thereof, or the relations between the parties, arising either during or after the employment relationship, shall be decided by arbitration in accordance with the Employment Arbitration Rules of the American Arbitration Association. This agreement covers claims based on statutory rights, including Federal and state laws against discrimination in employment.

2. The arbitration shall take place in _____, _____, shall be governed by the laws of the State of _____, and the arbitrator shall apply _____ law (without regard to conflict of law rules), except as otherwise provided by any written agreement between the parties.

3. The award rendered by the arbitrator shall be final and judgment may be entered upon it in accordance with applicable law in any court having jurisdiction thereof, including a Federal District Court, pursuant to the Federal Arbitration Act. The arbitrator may grant the Company injunctive relief, including temporary, preliminary, permanent and mandatory injunctive relief, but shall not be limited to such relief. In determining any award of the costs of arbitration, including the arbitrator's compensation, the arbitrator shall consider the ability of the Employee to pay such costs. If it would be a financial hardship for the Employee to make any deposit for costs or pay the initial filing fee, the Employer will advance such costs and fees.

4. This Arbitration Agreement shall not preclude the Company from seeking injunctive relief in a court in order to protect its rights until such time as judgment is entered upon an arbitration award, nor shall the filing of such an action constitute waiver by the Company of its right to seek arbitration hereunder.

5. In preparation for the arbitration hearing, each party may utilize all methods of discovery authorized by the _____ Rules of Civil Procedure, and may enforce the right to discovery in the manner provided by said Rules and/or by the _____ Arbitration Law.

6. The parties acknowledge that this is not a contract of employment.

IN WITNESS WHEREOF, the parties have executed this Arbitration Agreement. The Employee hereby acknowledges receipt of an executed copy of this Arbitration Agreement.

_____ Initialed EMPLOYEE

_____ Initialed COMPANY

The Employee, by his or her signature hereto, acknowledges that he or she has had adequate opportunity to review the foregoing Arbitration Agreement and that he or she is signing this Arbitration Agreement of his or her own free will without any duress or coercion.

_____
Employee - Signature

THE COMPANY:

_____
By: Duly Authorized Agent of the Company

PLEASE PRINT OR TYPE THE FOLLOWING:

_____
Employees's full name

_____
Home Address

_____
City State Zip

_____
Residence Telephone

_____ _____
Initialed Initialed
EMPLOYEE COMPANY