Federal and state legislation establish a public policy encouraging the use of arbitration agreements to resolve disputes. However, many employers have seen their agreements invalidated since the California Supreme Court's 2000 decision in Armendariz v. Foundation Health Psychcare, Inc. In that case, the Court imposed several procedural requirements for employment arbitration agreements. Recent appellate decisions have relied on those requirements to refuse to enforce employer's existing arbitration agreements.

Nevertheless, a recent California Court of Appeal decision breathed new life into the viability of employment arbitration agreements. In Roman v. Superior Court (Flo-Kem), the court upheld an employer's motion to compel arbitration against a former employee who sued the company for disability discrimination and wrongful termination.

Public Policy Favoring Arbitration

Congress enacted the Federal Arbitration Act (“FAA”) to ensure the validity and enforcement of contractual arbitration agreements. In general, the FAA evidences a national policy favoring arbitration. California's Arbitration Act (“CAA”) is virtually identical in purpose. The California Supreme Court has said that the CAA evinces a public policy favoring arbitration just like the FAA. However, although courts often say there is no “judicial hostility” to arbitration, they regularly invalidate employment arbitration agreements.

Procedural Safeguards in Employment Arbitration Agreements

In Armendariz v. Foundation Health Psychcare, Inc., the California Supreme Court set out five minimum requirements for the lawful arbitration of unwaiveable, statute-based lawsuits. An employment arbitration agreement is lawful only if it: (1) provides for neutral arbitrators; (2) provides for more than minimal discovery; (3) requires a written award; (4) provides for all of the types of relief that would otherwise be available in court; and (5) does not require employees to pay either unreasonable costs or any arbitrators' fees or expenses as a condition of access to the arbitration forum.

Unconscionability

However, even if an employment arbitration agreement meets the Armendariz requirements, it may still be unenforceable. Under the FAA and state law, arbitration agreements are contracts, subject to generally applicable contract defenses, such as unconscionability. Courts can therefore refuse to enforce any unconscionable provisions in an arbitration agreement.

In California, unconscionability has a procedural and substantive component. Both must be present to justify refusal to enforce a contract or clause as unconscionable. Procedural unconscionability focuses on oppression or surprise due to unequal bargaining power. In employment cases, a “take it or leave it” arbitration agreement – called an adhesion contract – nearly always provides sufficient procedural unconscionability to satisfy the defense. Substantive unconscionability deals with overly harsh or one-sided results.

The courts since Armendariz have found a number of arbitration provisions substantively unconscionable. These include limits on remedies, short statutes of limitations, provisions permitting the employer to go to court on certain claims while barring the employee from court access on any claims, impermissible cost-shifting, and other provisions.

The courts recently have begun invalidating arbitration agreements that prohibit employees from bringing class action claims in arbitration. The California Supreme Court held in Gentry v. Superior Court (Circuit City) that class action waivers in arbitration agreements usually are substantively unconscionable. Even an agreement that is perfectly “conscionable” regarding an employee’s individual lawsuit is subject to attack when an employee cannot sue on behalf of others. The Gentry court left open the theoretical possibility that such waivers could be enforced. But the
gauntlet the court set up for enforcing class waivers is nearly impossible to run.

**Arbitration Agreements with Class Waivers**

On March 10, 2009, in *Franco v. Athens Disposal Company, Inc.*, the Second District Court of Appeal held an employee arbitration agreement was unenforceable. The agreement contained a provision waiving class-wide arbitrations. It also precluded an employee from acting in “a private attorney general capacity.” Specifically, the agreement barred the employee’s prosecution of civil remedies for alleged wage and hour violations under the Private Attorney General Act (“PAGA”).

Applying the Gentry test, the court found the class waiver was unconscionable. The size of the potential individual recovery was small, there was the possibility of retaliation against employees who filed individual suits, and absent members of the class were potentially ill informed about their rights. Moreover, by prohibiting enforcement of the PAGA, the arbitration agreement impeded enforcement of a statutory scheme with statutory sanctions and fines. The prohibition of private attorneys general in arbitration was also unconscionable.

On March 18, 2009, shortly after issuing its *Franco* decision, the Second District Court of Appeal invalidated another employment arbitration agreement. In *Sanchez v. Western Pizza Enterprises, Inc.*, the court once again held that an employment arbitration agreement containing a class arbitration waiver was invalid. The court also held the arbitration agreement was unenforceable because it permitted the use of an arbitration service with just one arbitrator signed up as a member. In the court’s view, the limited pool of arbitrators created the risk of financial interdependence between Western Pizza and the arbitrator. It also gave Western Pizza an unfair advantage through its knowledge and experience with the arbitrator.

**Roman v. Superior Court**

In *Roman*, Gabriela Roman, a former employee, sued Flo-Kem for disability discrimination in violation of California’s Fair Employment and Housing Act (“FEHA”) and wrongful termination in violation of public policy. The “arbitration agreement” consisted of a single paragraph at the end of her employment application, which stated:

I hereby agree to submit to binding arbitration all disputes and claims arising out of the submission of this application. I further agree, in the event that I am hired by the company, that all disputes . . . which might arise out of my employment with the company, whether during or after that employment, will be submitted to binding arbitration. I agree that such arbitration shall be conducted under the rules of the American Arbitration Association. . . .

On appeal, Roman claimed the arbitration clause was procedurally unconscionable because it was presented as a “take it or leave it” condition of employment. She claimed the agreement was substantively unconscionable because the statement “I agree” did not mutually bind the employer to arbitrate all claims against her.

The court disagreed with Roman that the clause was procedurally unconscionable. The court explained Roman made a voluntary decision to sign the application and the arbitration clause was clearly marked and not hidden in any way.

The court also disagreed with Roman’s assertion the clause was substantively unconscionable. The court explained the “I agree” language did not mean the clause applied only to Roman. In stating that “all disputes and claims” were covered, the arbitration clause impliedly applied to both parties.

Roman also argued the arbitration clause was unenforceable because it did not expressly satisfy the Armendariz requirements. Specifically, she claimed it limited discovery; (2) barred her from filing an administrative complaint with the Department of Fair Employment and Housing (“DFEH”); and (3) forced her to split the arbitration costs with Flo-Kem.

The court rejected Roman’s first two arguments, explaining that arbitration does not need to provide for all discovery available in a civil court and Armendariz approved of arbitrator determined discovery. The court also determined the clause did not preclude Roman from filing a complaint with the DFEH.

The court agreed with Roman that Armendariz requires the employer to pay for the costs of arbitration. However, rather than voiding the entire arbitration clause, the court instead severed only that portion, thereby leaving the remainder of it enforceable.

Lastly, Roman argued Flo-Kem waived its right to enforce the arbitration clause. Roman based on her argument on the fact that Flo-Kem conducted initial written discovery and filed a motion to compel during the two months after Roman filed the complaint, but
before the Company filed a motion to compel arbitration. The court listed six factors in determining whether the right to seek arbitration was waived:

(1) whether the party’s actions are inconsistent with the right to arbitrate; (2) whether ‘the litigation machinery has been substantially invoked’ and the parties ‘were well into preparation of a lawsuit’ before the party notified the opposing party of an intent to arbitrate; (3) whether a party either requested arbitration enforcement close to the trial date or delayed for a long period before seeking a stay; (4) whether a defendant seeking arbitration filed a counterclaim without asking for a stay of the proceedings; (5) ‘whether important intervening steps [e.g., taking advantage of judicial discovery procedures not available in arbitration] had taken place’; and (6) whether the delay ‘affected, misled, or prejudiced’ the opposing party.

While Flo-Kem responded to Roman’s complaint and conducted some discovery, the court determined Roman was not otherwise sufficiently prejudiced by arbitration to waive the company’s right to arbitration.

**Conclusion**

Roman goes against the grain of recent California court decisions closely scrutinizing and refusing to enforce employment arbitration agreements. But is Roman just a fluke, or a sign of things to come?

On April 1, 2009, the United States Supreme Court, in 14 Penn Plaza LLC v. Pyett, held that a provision in a collective-bargaining agreement clearly and unmistakably requiring union members to arbitrate Age Discrimination in Employment Act claims is enforceable as a matter of federal law. The Pyett decision is significant, because it clarifies a series of earlier U.S. Supreme Court decisions that appeared to disfavor arbitration agreements in the employment context.

California employers should not see Roman or Pyett as a green light to implement arbitration agreements or to enforce existing arbitration agreements. The burdens Armendariz and its progeny impose, and the significant administrative costs of arbitration – most of which must be borne by the employer – may offset any benefits employers perceive by avoiding a jury trial. Additionally, litigation over the enforceability of arbitration agreements itself is costly and time consuming. Employers desiring arbitration must frequently update their agreements to conform with the latest case law developments.

Whatever future decisions may hold, employers should be cautious in deciding whether to create and implement employment arbitration agreements for their employees. Likewise, employers with existing arbitration agreements should consult with counsel regarding their validity before undertaking the time and expense of trying to enforce agreements that may not be enforceable.