Can Mandatory Arbitration Agreements Ever Be Stricken?

Judge Abraham J. Gafni (Ret.)
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ADR

Decisions of the U.S. Supreme Court have repeatedly reflected that arbitration must be accorded preferential treatment so that provisions waiving the right to litigate disputes (often involving class actions) and mandating arbitration may not be stricken lightly.

Thus, in 2011, the court held that state-law prohibitions on class action waivers in mandatory arbitration agreements are contrary to and pre-empted by the Federal Arbitration Act (FAA) and, accordingly, such waivers will not invalidate arbitration agreements unless grounds otherwise exist at law or in equity for their revocation (*AT&T Mobility LLC v. Concepcion*, 563 US 333 (2011)).

Similarly, last month, in *DirecTV v. Imburgia*, 577 U.S. ____ (December 14, 2015), the court reviewed an arbitration agreement that provided for class action waiver unless it was unenforceable under the "law of your state." When the agreement was originally executed such waivers were prohibited under California law. However, under *DirecTV*, following *Concepcion*, they could be enforced, as the state law was no longer valid. The court stated that it could "find nothing in that opinion (nor in any other California case) suggesting that California would generally interpret words such as 'law of your state' to

include state laws held invalid." To prohibit arbitration would not place the interpretation of arbitration contracts "on equal footing with all other contracts."

My article published Oct. 15, 2015, in The Legal, "Can Unconscionable Arbitration Provisions Be Waived and Severed?" discussed how one court had analyzed whether and when a multiplicity of unconscionable arbitration provisions might be severed or waived, thus allowing a mandatory arbitration provision to survive.

Coincidentally, a few days earlier, on Oct. 1, the U.S. Supreme Court granted certiorari in *MHN Government Services v. Zaborowski* (U.S.C.A. 9th Cir. No. 13-15671, 2014) to address this very issue of the impact of unconscionability on arbitration agreements.

The case has since been removed from the court's argument calendar due to a notice from the parties that they are in the settlement process, according to SCOTUSblog.

In *Zaborowski*, by a 2-1 vote, the U.S. Court of Appeals for the Ninth Circuit had affirmed that "multiple aspects of the arbitration provision [were] substantively unconscionable"; and, under generally applicable severance principles, "California courts refuse to sever when multiple provisions permeate the entire agreement with unconscionability." The court further rejected the claim of FAA pre-emption, as these general principles of California unconscionability law applied to the revocation of all contracts.

The dissent disagreed, contending that *Concepcion* should create a presumption in favor of a meaningful severance of the "relatively small number of unconscionable provisions," which would allow the enforcement of the remainder of the arbitration agreement.

The argument before the Supreme Court was to address more directly the circumstances under which an arbitration agreement containing unconscionable provisions may be revoked under state contract law.

In light of these cases, I started to consider what scenario, if any, might clearly warrant a finding that notwithstanding the preference for arbitration, revocation of the agreement rather than severance of its unconscionable provisions should result.

Here is one I came across, not from California and the Ninth Circuit where most of these cases have originated, but from the Fourth Circuit, *Lorenzo v. Prime Communications L.P.* (No. 14-17271622, November 24, 2015). (See similarly, *C.M. v. Maiden Re Insurance Services LLC* (Superior Court of New Jersey, Monmouth County, September 18, 2015).)

Rose Lorenzo had filed a claim under the North Carolina Wage and Hour Act against her former employer, Prime Communications, claiming that it had unlawfully failed to pay her overtime wages and had incorrectly calculated commissions. Prime filed a motion to compel Lorenzo to submit to arbitration based on an arbitration provision in its employee handbook.

It was undisputed that Lorenzo had received Prime's 2010 employee handbook when her employment began, and that it contained mandatory procedures for resolution of all employment issues including internal dispute resolution, mediation and, finally, arbitration. She had also signed a form acknowledging receipt and providing that, "I understand that I am responsible for reviewing the Prime Communications employee handbook." This form also acknowledged the opportunity to ask her manager questions about the handbook. Finally, it represented that she fully understood and/or would make sure that she did understand the contents of the handbook as it related to her employment.

However, the handbook also provided, "I understand that the Prime Communications' employee handbook is not a contract of employment and does not change the employment-at-will status of employees. Moreover, no provision should be construed to create any bindery (sic) promises or contractual obligations between the company and the employees (management or non-management)."

Another provision stated that, "I understand that the information contained in the handbook are guidelines and are in no way to be interpreted as a contract."

Prime contended that arbitration should be ordered because Lorenzo had agreed to arbitrate all disputes, the arbitration provision was binding and severable from the rest of the handbook, and any doubts must be resolved in favor of arbitration.

Lorenzo countered that the acknowledgment form did not exempt the "arbitration provision from the acknowledgments form's explicit statements disclaiming that the handbook established any binding obligations."

In agreeing with Lorenzo, the court noted that both parties realized the "resolution of this issue requires a determination of whether the parties entered into a contract to commit employment disputes to arbitration." Moreover, Section 2 of the FAA recognizes that written agreements to arbitrate are valid, irrevocable and enforceable, "save upon such grounds as exist at law or in equity for the revocation of any contract."

Therefore, notwithstanding a liberal policy favoring arbitration, "whether the parties agreed to arbitrate is resolved by application of state contract law."

The court agreed that Lorenzo's acknowledgement that she had continued working after receiving and reviewing the handbook would ordinarily create an implied assent. However, the acknowledgment form also provided that the terms of the handbook, including its arbitration provision were only "guidelines and are in no way to be - interpreted as a contract."

"Any implied assent that might have been created by Lorenzo's receipt and review of the handbook and by her continued employment was nullified by the express agreement of the parties not to be bound by any of the handbook's terms," the opinion said.

Understandably, Prime inserted the language in its handbook reflecting that no binding obligations or contractual commitments were created to avoid subsequent exposure to liability and to ensure that it would not be restrained in establishing new rules of conduct for its at-will employees. However, Prime could not be allowed to unilaterally alter any aspect of the relationship of the parties merely by changing the handbook, while retaining the right to demand arbitration under its provisions.

Not discussed in the *Lorenzo* opinion is the contra proferentem doctrine addressed in both the majority and dissenting opinions in *DirecTV*, i.e., that ambiguities, if any, should be construed against the drafter, here, Prime.

Consequently, in light of *Lorenzo*, employers that wish to retain flexibility in their employee relations should ensure that their handbooks state clearly that provisions relating to dispute resolution, unlike others, are unaffected by changes in employee handbooks and remain binding on both employer and employee.

Indeed, greater caution would suggest that dispute resolution provisions should be set out and executed in a separate agreement, independent of the employee handbook, so that it is clear that its provisions remain binding and enforceable upon all parties. •

Abraham J. Gafni is a retired judge and mediator/arbitrator with ADR Options and a professor at Villanova University School of Law.