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Russell Evans

Note

Engalla v. Permanente Medical Group, Inc.: Can Arbitration Clauses in Employment Contracts Survive a "Fairness" Analysis?

by
RUSSELL EVANS*

Introduction

On June 30, 1997, the California Supreme Court handed down its decision in *Engalla v. Permanente Medical Group, Inc.*[1] The *Engalla* Court refused to compel arbitration of a medical malpractice claim despite the presence of a binding arbitration clause in the terms of a medical insurance agreement.[2] The California Court indicated that defendant malfeasance appeared likely, and it remanded the case to the trial court for factual determinations on whether the defendant HMO, Kaiser Permanente Medical Group, induced the arbitration clause through fraud or waived its right to arbitration due to its dilatory conduct.[3]

The holding and eventual outcome of this case, however, are merely side issues for purposes of this Note. Rather, it is the Court's intriguing examination and careful scrutiny of Kaiser's arbitration process that raises key legal questions. Under the conventional review of arbitration clauses, courts limit their analysis to issues of creation and initial consent to such clauses. The *Engalla* Court, however, did not limit itself to the formation of the arbitration

* J.D. Candidate, Hastings College of the Law, 1999; B.A. University of California, Berkeley, 1995.

1. 938 P.2d 903 (Cal. 1997).
2. *See id.* at 908.
3. *Id.* at 924.

agreement. Instead, the Court conducted a sweeping examination into how the Kaiser arbitration process functioned and considered whether the process was an adequate system for resolving malpractice claims.[4] Using this mode of analysis, the majority found numerous flaws in Kaiser's arbitration process. The opinion is especially critical of the ways in which the arbitration process infringed upon the procedural rights of claimants. The Court's examination of the arbitral process, rather than agreement formation, and its focus on procedural deficiencies imply that minimum levels of "fairness" must be present in the operation of all arbitration systems.

This expansion in the judicial examination of arbitration clauses has important implications for employment law. Binding arbitration clauses have exploded in usage and popularity since the United States Supreme Court's 1991 decision in *Gilmer v. Interstate/Johnson Lane Corporation*.[5] Yet, the widespread use of such clauses has been matched step-by-step with widespread criticism. Many commentators assert that arbitration in the employment context is marred by procedural shortcomings, inappropriateness, and general unfairness.[6] The *Engalla* decision signals that the California Supreme Court has also grown weary of binding arbitration. *Engalla* surely does not herald the end of binding arbitration clauses in employment contracts. Nevertheless, in the wake of this decision, employees have a new point of attack in challenging arbitration clauses, while employers have the impetus to amend their arbitration practices to conform to the heightened requirements of a "fairness" standard.

Part I of this Note examines the *Engalla* decision in detail. Part II considers whether *Engalla* is part of a growing trend of dissatisfaction with arbitration in the non-commercial context or if the impact of the decision will be limited to cases with similarly distasteful facts. Part II will also consider whether *Engalla* represents a judicial reaction to the criticisms of employment dispute arbitration and, if so, what effect this development will have on employment contracts. Part III presents a case study of the securities industry and its experience using arbitration for employment matters. Finally, Parts IV and V suggest several courses of action in response to the fairness issues raised by the *Engalla* decision.

I. The *Engalla* Decision

The *Engalla* case originated from a malpractice claim in which

4. *See id.* at 909-14.
5. 500 U.S. 20 (1991).
6. *See infra* notes 60-74 and accompanying text.

Wilfredo Engalla asserted that Kaiser doctors negligently failed to diagnose his lung cancer.[7] Under the terms of Engalla's Service Agreement (SA) with Kaiser, the malpractice claim was subject to arbitration.[8] The SA required claimants to serve Kaiser with an arbitration claim and required each side to designate an arbitrator within thirty days after service.[9] The parties had an additional thirty days to choose a neutral third arbitrator for the arbitration panel.[10] In addition to these time requirements, the California Supreme Court found two related factors relevant. First, the arbitration program called for by the SA was designed, written, mandated, and administered by Kaiser.[11] No independent person or entity was employed to provide administrative services, oversight, or evaluation of the arbitration program and its performance.[12] Moreover, these facts were not disclosed to members of Kaiser's health plan.[13] Second, Kaiser disseminated various publications representing its arbitration program as quick, efficient, and fair.[14]

In practice, the Kaiser arbitration program was cumbersome and extremely slow.[15] An independent statistical analysis of data provided by Kaiser revealed that medical malpractice arbitrations were delayed in ninety-nine percent of the cases.[16] A neutral third arbitrator was selected within the sixty-day SA time requirement in only one percent of the cases and only three percent of the cases saw a neutral arbitrator appointed within 180 days.[17] The average time taken in selecting a neutral third arbitrator was 674 days.[18] Even after selection of the arbitrators, additional delays occurred as it took an average of 863 days to reach a hearing under Kaiser's arbitration program.[19]

In Wilfredo Engalla's case, Kaiser did not select its arbitrator until forty-seven days after the original claim was served.[20] Despite Mr. Engalla's deteriorating medical condition, Kaiser refused to begin

7. *See* 938 P.2d at 909.
8. *See id.*
9. *See id.*
10. *See id.*
11. *See id.*
12. *See id.*
13. *See id.*
14. *See id.* at 910.
15. *See id.* at 912-13.
16. *See id.* at 912.
17. *See id.* at 912-13.
18. *See id.* at 913.
19. *See id.*
20. *See id.* at 910.

discovery until after the appointment of a neutral third arbitrator.[21] However, Kaiser delayed the selection of the third arbitrator when it failed to formally retain the agreed-upon arbitrator and then failed to pay the deposit required for the arbitrator's services.[22] As administrator of the arbitration program, Kaiser was obligated to perform both of these duties.[23] The neutral arbitrator was finally accepted by Kaiser 144 days after service of Mr. Engalla's claim, one day before Mr. Engalla died.[24]

Claiming malpractice and fraud, Engalla's family and the representatives of his estate sued Kaiser in Superior Court.[25] The trial court denied Kaiser's motion to compel arbitration based on findings of fraud in the inducement and fraud in the application of the arbitration agreement.[26] The California Court of Appeal reversed.[27] On subsequent appeal, however, the California Supreme Court agreed with the trial court's finding that evidence of fraud existed to support a denial of Kaiser's petition to compel arbitration. The Court therefore remanded the case for factual determinations on the issues of fraud and waiver.[28]

The first basis relied on by the California Supreme Court in refusing to compel arbitration was fraud in the inducement of the arbitration clause.[29] The Court began by interpreting section 1281.2 (b) of the California Code of Civil Procedure to mean that petitions to compel arbitration will not be granted when grounds exist for rescinding the arbitration agreement.[30] Fraud constitutes such grounds.[31] In *Engalla*, the Court found facts to support the claim "that Kaiser entered into the arbitration agreement with knowledge that it would not comply with its own contractual timelines, or with at least reckless indifference as to whether its agents would use reasonable diligence and good faith to comply with them."[32] The

21. *See id.* at 911.
22. *See id.* at 912.
23. *See id.*
24. *See id.*
25. *See id.* at 914.
26. *See id.* at 915.
27. *See id.*
28. *See id.* at 908.
29. *See id.* at 922.
30. *See* 938 P.2d at 916 (interpreting CAL. CODE. CIV. PROC. §1281.2 (West 1997)). "[T]he court shall order the petitioner and respondent to arbitrate the controversy if it determines that an agreement to arbitrate the controversy exists, unless it determines that: (a) The right to compel arbitration has been waived by the petitioner; or (b) Grounds exist for the revocation of the agreement." *Id.*
31. *See* CAL. CIV. CODE § 1689(b)(1) (West 1997).
32. 938 P.2d at 917.

Court recognized that Kaiser was not strictly bound to a sixty day requirement since selecting the neutral third arbitrator was a bilateral decision dependent on agreement of both parties.[33] Nevertheless, Kaiser's contractual representations "at the very least commit[ted it] to exercise good faith and reasonable diligence" in meeting its established timelines.[34] This was especially true considering Kaiser contractually assumed responsibility for administering the arbitration program.[35] Therefore, the Court held that Kaiser's misrepresentations regarding the timeliness of its arbitration program, its knowledge of these falsities, Mr. Engalla's reliance upon the falsities, and his subsequent damage were sufficient to support a claim of fraud in the inducement of the SA arbitration clause.[36]

The Court then considered whether Kaiser's dilatory conduct constituted waiver of its right to compel arbitration.[37] Section 1281.2 (a) of the California Code of Civil Procedure provides that a petition to compel arbitration shall be refused if the "right to compel has been waived by the petitioner."[38] A variety of actions may constitute waiver, including unreasonable delay, bad faith, or willful misconduct.[39] According to the *Engalla* Court, delay must be substantial, unreasonable, and in spite of the claimant's own reasonable diligence.[40] The Court concluded that "Kaiser's course of delay,... which was arguably unreasonable or undertaken in bad faith, may provide sufficient grounds for a trier of fact to conclude that Kaiser has in fact waived its arbitration agreement."[41]

Finally, the *Engalla* Court examined Kaiser's arbitration clause for unconscionability, but it ultimately rejected this challenge.[42] Under California case law, "contractual arrangements for the non-judicial resolution of disputes 'must possess' minimum levels of integrity."[43] The *Engalla* Court cautioned that "HMO's are... especially obligated not to impose contracts on their subscribers that are one-sided and lacking in fundamental fairness."[44] Nonetheless, it held that Kaiser's arbitration agreement did not, on its face, lack

33. *See id.*
34. *Id.*
35. *See id.*
36. *See id.* at 922.
37. *See* 938 P.2d at 922-24.
38. CAL. CIV. PROC. CODE § 1281.2 (West 1997).
39. *See Engalla*, 938 P.2d at 923.
40. *See id.* at 924.
41. *Id.*
42. *Id.* at 924-25.
43. *Id.* (quoting Graham v. Scissor-Tail, Inc,. 623 P.2d 165, 176 (Cal. 1981)).
44. *Id.*

minimum levels of integrity and was thus not per se unconscionable.[45] The Court objected to the discrepancy between Kaiser's representations and the actual workings of the program, not the arbitration clause itself.[46]

The rejection of Wilfredo Engalla's unconscionability claim presents an important limit to the decision. The Court was unwilling to find that Kaiser's arbitration clause was unfair on its face. Yet, in its analysis of Mr. Engalla's fraud and waiver claims, the Court's conclusions were induced by the unfair operation of Kaiser's arbitration program. The Court apparently reached a line it was unwilling to cross and instead drew a distinction between the general fairness of arbitration and the fairness of particular arbitration programs. Thus, arbitration remains a legitimate alternative to judicial resolution, even in the non-commercial context, but only if the arbitration process satisfies an unspecified level of fairness. As Justice Mosk wrote for the majority: "[A]lthough we affirm the basic policy in favor of... arbitration agreements, the governing statutes place limits on the extent to which a party that has committed misfeasance in the performance of such an agreement may compel its enforcement."[47]

The *Engalla* decision is exceptional because it expressed a unique, expansive mode of analyzing arbitration clauses. The Court validated Engalla's fraud and waiver claims only after an extensive review of the operation of Kaiser's arbitration system.[48] Not only did the Court look to Mr. Engalla's experience with the program, but it also considered how the program performed in the past.[49] The fundamental problem with Kaiser's arbitration program was that systematic delays evinced a patently unfair arbitration process. The *Engalla* Court extended its scrutiny of arbitration beyond an analysis of the creation and inducement of an arbitration clause to a broad examination of Kaiser's entire arbitration process.

Justice Kennard, in concurrence, summed up the rationale behind the majority's scrutiny: "[T]his case illustrates yet again the essential role of the courts in ensuring that the arbitration system delivers not only speed and economy but also fundamental fairness."[50] Justice Kennard further explained how "[p]rocedural manipulations can be used by a party not only to delay and obstruct

45. *See id.* at 925.
46. *See id.*
47. *Id.* at 908.
48. *See id.* at 908-14.
49. *See id.* at 912-13.
50. *Id.* at 925 (Kennard, J., concurring).

the proceedings, thereby denying the other party the speed and efficiency that are the arbitration system's primary justification, but also to affect the possible outcome of the arbitration."[51] Moreover, the concurrence pointed out that unfairness in arbitration is a special risk outside of the commercial context because consumer banking terms, health insurance agreements, or employment contracts resemble adhesion contracts between parties of unequal bargaining power in which the institutional party can demand the arbitration process of its own choosing.[52] Although Justice Kennard's observations were not explicitly expressed in the majority opinion, the majority's careful scrutiny of Kaiser's arbitration process implies that it was motivated by similar concerns.

Justice Brown's dissenting opinion, however, strongly protested this new approach. According to the dissent, misfeasance in the arbitration process should first be resolved in arbitration.[53] Only after an arbitrator finds a specific arbitration clause unenforceable should the parties be permitted to seek relief from the courts.[54] The majority's approach to binding arbitration clauses, with its careful scrutiny of the fairness of the arbitration process, prompted a warning from the dissent: "However well-intentioned the majority and however deserving its intended target, today's holding pokes a hole in the barrier separating private arbitrations and the courts. Unfortunately, like any such breach, this hole will eventually cause the dam to burst."[55]

Does *Engalla* represent a growing trend for judicial review of arbitration clauses or merely an anomaly generated by unique facts? To answer this question, the factors that influenced the concurrence's misgivings regarding arbitration in the consumer and employment context must be examined alongside the precedent which motivated the dissent's reverence for a separate arbitral forum.

II. Is *Engalla* a Trendsetter or an Anomaly in the Employment Context?

Although the *Engalla* case involved mandatory arbitration in the medical malpractice context, the Court's "fairness" scrutiny could have an important impact in the field of employment law. Scrutiny of arbitration procedures for "fairness" is a particularly ominous

51. *Id.* at 926 (Kennard, J., concurring).
52. *See id.* at 926-27.
53. *See id.* at 928.
54. *See id.* at 930-31.
55. *Id.* at 932 (Brown, J., dissenting).

development for employment law in light of the exploding use of binding arbitration clauses in non-union employment contracts.[56] Eager to enjoy the purported advantages of arbitration[57] and avoid the uncertainties of a jury trial, employers are including arbitration clauses in standard employment contracts with increasing frequency.[58]

This growing practice, however, has not been universally endorsed by the legal community. Commentators have vigilantly examined the shortcomings of mandatory arbitration of employment disputes.[59] The *Engalla* decision itself may represent the acceptance of the scholarly criticism which argues that the problems associated with arbitrating employment disputes can only be countervailed by requiring stricter procedural safeguards for the arbitration of such claims. If this is a valid interpretation of *Engalla*, the most important question arising from the case is whether the Court's "fairness" analysis represents part of a growing judicial trend or merely an aberration produced from the egregious facts of a particular case. The following section examines the claimed deficiencies of arbitration for employment disputes and analyzes whether courts will increasingly probe arbitration processes or continue to apply traditional standards of arbitration review.

In the years following the United States Supreme Court's 1991 decision in *Gilmer v. Interstate/Johnson Lane Corporation*,[60] the use

56. *See* Martin H. Malin & Robert F. Ladenson, *Privatizing Justice: A Jurisprudential Perspective on Labor and Employment Arbitration from the* Steelworkers Trilogy *to* Gilmer, 44 HASTINGS L.J. 1187, 1188 & n.5 (1993).

57. In theory, arbitration advantages include speed and efficiency, lower cost, privacy, and finality. Also, "arbitrators are less likely than juries to award excessive damage awards." Michele M. Buse, Comment, *Contracting Employment Disputes Out of the Jury System: An Analysis of the Implementation of Binding Arbitration in the Non-union Workplace and Proposals to Reduce the Harsh Effects of a Non-appealable Award*, 22 PEPP. L. REV. 1485, 1496-99 (1995).

58. However, a survey of the use of mandatory arbitration suggests that the early enthusiasm for arbitration policies that was produced by the *Gilmer* decision may be slowing as the questions left unanswered by *Gilmer* become more evident and produce greater uncertainty. Some of the employers questioned in the survey indicated they expected to implement an arbitration policy, but were awaiting further judicial definition of the types of plans that would withstand legal scrutiny before going forward with their own policies. *See* Mei L. Bickner et al., *Developments in Employment Arbitration*, 52 JAN DISP. RESOL. J. 8, 78 (January 1997).

59. *See infra* notes 60-74 and accompanying text.

60. 500 U.S. 20 (1991). The narrow holding of *Gilmer* was that an agreement to arbitrate contained in a securities exchange registration form will be enforced with respect to claims under the Age Discrimination in Employment Act. Nonetheless, by reasoning that arbitration is appropriate where a statute does not expressly preclude waiver of statutory rights (such as the right to a court trial) *Gilmer* provided the foundation for lower federal courts to enforce arbitration agreements with respect to employment claims

of arbitration clauses in employment contracts has steadily increased. At the same time, critics have been equally steadfast in observing and commenting on the substantive problems posed by the arbitration of employment disputes.[61] Several commentators have also considered the procedural issues raised by employment dispute arbitration.[62] In particular, commentators have noted that widespread judicial approval of mandatory arbitration clauses in employment contracts may require courts to police the arbitration systems which are instituted by such clauses.[63] Meanwhile, a common criticism of employment dispute arbitration involves the arbitrators themselves. Many employment arbitration clauses call for an arbitration system in which the arbitrators are unfamiliar with and inexperienced in employment law.[64] This is particularly troublesome in the employment context since arbitrators are often called upon to interpret and expound discrimination statutes that were enacted to protect the public.[65] Moreover, in contrast to the equal opportunity goals of most employment statutes, some employment arbitration panels are dominated by older white males.[66] This stands in stark contrast to statutory safeguards which assure fairness and diversity in selecting petit jurors for federal trials; federal juries are intended to represent a broad cross-section of the community and, thus, potential jurors cannot be excluded due to race, color, religion, sex, national

under Title VII, the ADA and other statutes; some courts have declined to do so, but the majority have expanded the *Gilmer* rationale to various statutes. *See* Martin H. Malin, *Arbitrating Statutory Employment Claims in the Aftermath of* Gilmer, 40 ST. LOUIS U. L.J. 77, 92 (1996).

61. In particular, controversy surrounds whether or not it is appropriate for private arbitrators to decide issues of public law outside of the collective bargaining context. *See* Malin, *supra* note 60, at 99-102; Buse, *supra* note 57, at 1512-13. This controversy, however, exceeds the scope of this Note.

62. *See, e.g.*, Malin, *supra* note 60, at 95-99.

63. *See id.*

64. *See* HEALTH, EDUCATION, AND HUMAN SERVICES DIVISION, GENERAL ACCOUNTING OFFICE, EMPLOYMENT DISCRIMINATION: HOW REGISTERED REPRESENTATIVES FARE IN DISCRIMINATION DISPUTES 11 (1994) [hereinafter GAO REPORT]; Evan J. Spelfogel, *Legal and Practical Implications of ADR and Arbitration in Employment Disputes*, 11 HOFSTRA LAB. L.J. 247, 265 (1993); Megan L. Dunphy, Comment, *Mandatory Arbitration: Stripping Securities Industry Employees of their Civil Rights*, 44 CATH. U. L. REV. 1169, 1210-11 (1995).

65. For example, Title VII of the Civil Rights Act of 1964. *See* 42 U.S.C. § 2000e *et seq.* (West 1997).

66. The 1994 GAO report found that in December 1992 the New York Stock Exchange's arbitrator pool was 89% male, 97% white, and was an average age of 60; NASD officials predicted that their arbitrator pool generally resembled that of the NYSE. *See* GAO REPORT, *supra* note 64, at 8.

origin, or economic status.[67] The securities industry provides a useful example of these concerns and its experience with arbitrating employment disputes will be discussed in detail in Part III.

Another claimed deficiency of employment arbitration relates to the selection procedures instituted by some arbitration policies. Some systems give the employer sole power to choose the arbitrator.[68] Meanwhile, even where joint selection by the employer and the employee is provided, individual employees may be put at a disadvantage by a lack of familiarity with and information about the eligible arbitrators relative to the knowledge possessed by employers.[69] Also, the employer's continuous use of arbitration risks creating an institutional bias whereby an arbitrator who desires future work will be hesitant to render a decision that is contrary to the employer's expectations.[70] Various other procedural criticisms have been cited as proof of the flawed nature of employment dispute arbitration, including: charging of arbitration costs and fees to claimants;[71] limited discovery permitted in arbitration proceedings;[72] lack of written opinions;[73] and insufficient judicial review of arbitration decisions.[74] Despite these criticisms, courts have been reluctant to address the claimed shortcomings of arbitration procedures. In both the employment and non-employment contexts, the vast majority of courts have avoided scrutinizing the "fairness" of an arbitration process.

Nonetheless, several courts have taken a careful look at the appropriateness of specific arbitration procedures. For instance, in *United States Equal Employment Opportunity Commission v. River Oaks Imaging & Diagnostic*,[75] the United States District Court for the Southern District of Texas ordered a preliminary injunction preventing the operation of a mandatory arbitration program.[76] The

67. *See* William M. Howard, *Arbitrating Employment Discrimination Claims: Do You Really Have To? Do You Really Want To?*, 43 DRAKE L. REV. 255, 276 (1994) (*citing* 28 U.S.C. §§ 1861-1863; 18 U.S.C. §243).

68. *See* Bickner et al., *supra* note 58, at 80; Joseph R. Grodin, *Arbitration of Employment Discrimination Claims: Doctrine and Policy in the Wake of* Gilmer, 14 HOFSTRA LAB. L.J. 1, 43-44 (1996).

69. *See* Bickner et al., *supra* note 58, at 11; Grodin, *supra* note 68, at 43-44.

70. *See* Bickner et al., *supra* note 58; Grodin, *supra* note 68, at 43-44.

71. *See* Grodin, *supra* note 68, at 44-45.

72. *See* Ellwood F. Oakley, III & Donald O. Mayer, *Arbitration of Employment Discrimination Claims and the Challenge of Contemporary Federalism*, 47 S.C. L. REV. 475, 533 (1996); Buse, *supra* note 57, at 1521-22, 1534-35.

73. *See* Oakley & Mayer, *supra* note 72, at 533-34; Buse, *supra* note 57, at 1537.

74. *See* Malin, *supra* note 60, at 102-03; Buse, *supra* note 57, at 1537-38.

75. 67 Fair Empl. Prac. Cas. (BNA) 1243 (S.D. Tex. 1995) (*River Oaks*).

76. *See id.*

defendant in the case, River Oaks Imaging & Diagnostic ("ROID"), instituted an "ADR Policy" which required the arbitration of all employment controversies.[77] Chief Judge Black found ROID's policy "so misleading and against the principles of Title VII of the Civil Rights Act of 1964 that its use violate[d] such law."[78] Judge Black cited several flaws in the arbitration program as grounds for his decision: the program required complaining employees to pay half the costs of any ADR proceedings as well as employer attorney's fees if the employer prevailed; the filing requirements interfered with an employee's rights to file complaints with the EEOC; and the implementation of the policy, whereby employees who refused to agree with the new policy risked termination, possibly constituted retaliation.[79] The case was ultimately decided by a consent order which permanently revoked ROID's ADR policy.[80] This case is significant in that the court did not blindly uphold the challenged arbitration program. Rather, the Court scrutinized the policy and enjoined it on the basis of the unfair provisions it contained.[81]

A federal district court in Boston embarked on an even more ambitious examination of arbitration procedures. In *Rosenberg v. Merrill Lynch*,[82] a sex discrimination suit brought by a securities employee, the defendant sought a motion to compel arbitration pursuant to the mandatory arbitration clause found in the employee's securities dealer registration form.[83] The district judge initially deferred a decision on the motion and ordered the parties to submit information on whether the securities industry's mandatory arbitration system adequately protects the rights of workers who make discrimination claims.[84] In support of her order, Judge Gertner explained that the United States Supreme Court's decision in *Gilmer* had left "open the possibility that some arbitration procedures could be systematically challenged as biased."[85] The plaintiff's argument

77. *See* Sharona Hoffman, *Mandatory Arbitration: Alternative Dispute Resolution or Coercive Dispute Suppression?*, 17 BERKELEY J. EMP. & LAB. L. 131, 136 (1996).

78. 67 Fair Empl. Prac. Cas. (BNA) at 1243.

79. *See id.*; *see also* Hoffman, *supra* note 77, at 136-40.

80. United States Equal Employment Opportunity Comm'n v. River Oaks Imaging & Diagnostic, No. H-94-755 (S.D. Tex. June 23, 1995).

81. *See* Hoffman, *supra* note 77, at 140.

82. 965 F. Supp. 190 (D. Mass. 1997) (*Rosenberg* I).

83. *See id.* at 191.

84. *See id.* at 192. The order also called for briefings on issues that are beyond the scope of this Note: the applicability of *Gilmer* to Title VII in light of that statute's 1991 amendments; the applicability of *Gilmer* to the ADEA in light of that statute's 1990 amendments; and the legal standard for an employee's waiver of rights to an Article III judge and representative jury. *See id.* at 203.

85. *Id.* at 201. *See infra* text accompanying notes 134-41.

that her "arbitration panel may be biased or inappropriately selected [was], at least on the surface," found to have some merit, but the record was insufficient to make a final determination.[86] Therefore, Judge Gertner ordered discovery regarding plaintiff's signing of her securities registration form and the adequacy of the arbitration process desired by the defendant.[87] After submissions by both parties, the district court found that the NYSE arbitration system was "inadequate to vindicate Rosenberg's [statutory] rights."[88] According to the court, "Rosenberg ha[d] risen to the Supreme Court's challenge" and demonstrated that "structural bias" in the New York Stock Exchange (NYSE) procedures made the system inadequate for the fair adjudication of her claims.[89] This conclusion was based on two findings. First, the court found that Merrill Lynch was a member firm of the NYSE, and that the NYSE's member firms "govern the [NYSE] as part of [its] self-regulating scheme."[90] Second, the court found that "[f]rom the rules that govern arbitration procedure, through the selection of the arbitrators, to the details of discovery practice, the system is dominated by the NYSE itself."[91] The district court concluded that "[d]ominace of an arbitral system by one side in the dispute does not comport with any model of arbitral impartiality," regardless of the "competence or fairness of individual arbitrators who participate [in] the NYSE system."[92] In addition to these procedural problems, the court found Rosenberg's arbitration clause unenforceable under applicable discrimination statutes.[93] Consequently, the court refused to compel arbitration of Rosenberg's employment claims.[94]

86. *Rosenberg* I, 965 F. Supp. at 201.

87. *See id.* at 203.

88. Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 995 F. Supp. 190, 212 (D. Mass. 1998) (*Rosenberg* II).

89. *See id.* at 203, 206-07.

90. *Id.* at 207 (internal quotations omitted).

91. *Id.* at 210.

92. *Id.* at 211.

93. *See id.* at 204-06. The court held that the 1991 Amendments to Title VII (the Civil Rights Act of 1991) as well as the Older Workers Protection Act amendments to the Age Discrimination in Employment Act precluded the enforcement of pre-dispute agreements to arbitration claims under these statutes. *See id.* This conclusion was overruled by the First Circuit on appeal. *See* Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 163 F.3d 53, 56 (1st Cir. 1998) (*Rosenberg* III). *But see* Duffield v. Robertson Stevens & Co., 144 F.3d 1182, 1199 (9th Cir. 1998) (holding that the Civil Rights Act of 1991 establishes Congress' intention to preclude the enforcement of mandatory pre-dispute agreements to arbitrate Title VII claims).

94. *See* Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 995 F. Supp. 190, 204-06 (D. Mass. 1998) (*Rosenberg* II).

On appeal, however, the above findings of the Massachusetts district court were overturned because there was no conclusive evidence of actual bias in the NYSE arbitration system.[95] The First Circuit explained that the lower court misinterpreted the structure of the NYSE's system. Rather than being controlled by member firms like Merrill Lynch, the court found that the NYSE itself plays a significant role in monitoring and disciplining members for non-compliance with its rules.[96] The court also found errors in the lower court's description of the NYSE system's specific arbitration procedures.[97] The selection process for choosing NYSE arbitrators did not undermine employee rights and, since employees were not asked to bear fees for the arbitration of their claims, cost considerations did not impede employee claims.[98] Accordingly, the court concluded that "the evidence establishe[d] no basis to invalidate the NYSE arbitral scheme."[99] Once again, the actual outcome of the *Rosenberg* litigation is of only minor importance to this Note. As with *Engalla*, the significance of *Rosenberg* is that both the district and appellate court engaged in a careful examination of a particular arbitration process.

Cheng-Canindin v. Renaissance Hotel Associates[100] presents another employment case in which a court's holding was based on the procedural flaws of a particular arbitration system. In this decision, a California appellate court held that an employer's mandatory complaint review system, and the procedures it operated under, were unacceptably biased in favor of the employer hotel.[101] The procedures did not involve a third party decision maker. Instead, Hotel managers had final authority in deciding disputes brought before the review committee.[102] Likewise, the calling of witnesses and presentation of evidence was subject to the discretion of Hotel managers.[103] Meanwhile, the Employee Guide provided to employees explicitly discouraged the use of attorneys in the dispute proceedings.[104] According to the court, the dispute resolution system "totally lack[ed] impartiality."[105] Given its "strong view that a third

95. *See Rosenberg* III, 163 F.3d at 66-67.
96. *See id.* at 67.
97. *See id.* at 66-68.
98. *See id.*
99. *Id.* at 68.
100. 50 Cal. App. 4th 676 (1996).
101. *See id.* at 692-93.
102. *See id.* at 680, 688.
103. *See id.*
104. *See id.*
105. *Id.* at 692-93.

party decision maker and some degree of impartiality must exist for a dispute resolution mechanism to constitute arbitration," the court concluded that this system failed to constitute a valid arbitration system.[106] Procedural defects once again provided the grounds for a court's rejection of an "unfair" arbitration arrangement.

Careful scrutiny of arbitration has also been employed in the consumer arbitration context. In *Patterson v. ITT Consumer Financial Corp.*,[107] a California appellate court closely examined arbitration procedures and invalidated an arbitration clause on grounds of unconscionability.[108] *Patterson* involved a "guaranteed loan" financing document with a mandatory arbitration clause. According to the court, the clause established confusing arbitration procedures which created significant obstacles to a participatory hearing.[109] First, the location of the arbitration was unclear because neither the agreement itself nor the rules of the administering arbitration agency, the National Arbitration Forum (NAF), specified whether arbitration would be held in California, where the documents were signed, or in Minnesota, where the NAF was located.[110] Moreover, borrowers would remain uninformed of the location until after a claim was filed and a response entered.[111] Second, the arbitration clause acted to limit a borrower's rights to a hearing.[112] For example, borrowers had to prepay substantial fees in order to initiate a hearing and additional fees were required for discovery, written findings, and expedited hearings.[113] "The likely effect of these procedures," wrote the court, "is to deny a borrower against whom a claim has been brought any opportunity to a hearing, much less a hearing held where the contract was signed, unless the borrower has considerable legal expertise or the money to hire a lawyer and/or prepay substantial hearing fees."[114] The court concluded that such procedures "become oppressive when applied to unsophisticated borrowers of limited means in disputes over small claims" and therefore refused to enforce the arbitration clause.[115]

Meanwhile, some courts have inquired into arbitration procedures in the traditional domain of arbitration—commercial

106. *Id.* at 687, 692.
107. 18 Cal. Rptr. 2d 563 (Cal. Ct. App. 1993).
108. *See id.* at 567.
109. *See id.* at 566-67.
110. *See id.* at 566.
111. *See id.*
112. *See id.*
113. *See id.* at 566 n.3.
114. *Id.* at 566.
115. *Id.* at 567.

disputes. In *Graham v. Scissor-Tail*,[116] the California Supreme Court refused to enforce an arbitration provision in which the arbitrator was unilaterally designated by one party.[117] The Court found the contract to be one of adhesion and explained that an adhesion contract (or provision) will not be enforced against the adhering party if it does not fall within the reasonable expectations of that party.[118] Even if it meets the reasonable expectations test, a provision will not be enforced if it is unduly oppressive or unconscionable.[119] The Court concluded that the provision at issue failed the second test "because it designate[d] an arbitrator who, by reason of its status and identity, [was] presumptively biased in favor of one party...."[120] In such circumstances, the contract "must be scrutinized with particular care to insure that the party of lesser bargaining power... is not left in a position depriving him of any realistic and fair opportunity to prevail in a dispute under its terms."[121] Moreover, "[w]hen it can be demonstrated... that the clear effect of the established procedure of the arbitrator will be to deny the resisting party a fair opportunity to present his position, the court should refuse to compel arbitration."[122]

Likewise, in *Graham Oil Co. v. Arco Products Co.*,[123] the Ninth Circuit refused to compel arbitration based on several restrictions that were placed on the arbitration process.[124] The agreement established a shorter period of limitations than the applicable statute, the Petroleum Marketing Practices Act, and precluded the exemplary damages and attorney's fees authorized by that law.[125] The court characterized these provisions as an integrated scheme to circumvent public policy and held the entire arbitration clause invalid.[126]

In addition to the above cases, the very decision which legitimized the use of mandatory arbitration clauses in employment

116. 623 P.2d 165 (Cal. 1981).

117. *See* Grodin, *supra* note 68, at 21-22.

118. *See Scissor-Tail*, 623 P.2d at 172-73.

119. *See id.*

120. *Id.* at 173.

121. *Id.* at 176.

122. *Id.* at 176-77.

123. 43 F.3d 1244 (9th Cir. 1994); *see also* Grodin, *supra* note 68, at 41-42; Lucille M. Ponte, *In the Shadow of* Gilmer*: How Post-*Gilmer *Legal Challenges to Pre-Dispute Arbitration Agreements Point the Way Towards Greater Fairness in Employment Arbitration*, 12 OHIO ST. J. ON DISP. RESOL. 359, 378-79 (1997).

124. *See Arco Products*, 43 F.3d at 1246-47.

125. *See id.* at 1247-48.

126. *See id.* at 1249. Nonetheless, some courts have compelled arbitration of employment discrimination claims despite restrictions on damages, attorney's fees, and filing periods. *See* DeGaetano v. Smith Barney, Inc., 1996 WL 4426 (S.D.N.Y. 1996); Johnson v. Hubbard Board, Inc., 940 F. Supp. 1447 (D. Minn. 1996).

agreements, *Gilmer v. Interstate/Johnson Lane Corp.*, implied that fairness of process may be required for the enforcement of non-commercial arbitration decisions.[127] The plaintiff in this case signed an employment agreement which required the arbitration of any employment disputes.[128] The agreement also provided that arbitration would be conducted in accordance with the procedures and rules of the New York Stock Exchange ("NYSE") arbitration system.[129] In his appeal, Gilmer challenged the adequacy the NYSE arbitration procedures.[130] He asserted that arbitration panels would be biased and that arbitration discovery was too limited.[131] Gilmer also claimed that the lack of written opinions and the limited review of arbitration decisions would impede the purposes of antidiscrimination statutes and stifle the development of employment law.[132] Furthermore, Gilmer contended that the unequal bargaining power of employers and employees undermined the legitimacy of arbitration decisions.[133] The United States Supreme Court, however, rejected each of these claims. First, the Court noted that Gilmer's "generalized attacks on arbitration 'rest on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants,' and as such, they are 'far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes.'"[134] The Court then countered Gilmer's claims with examples of how the NYSE arbitration rules and procedures, which applied to the employment dispute at issue in the case, afforded sufficient safeguards to ensure Gilmer a fair opportunity to present his claims.[135]

127. 500 U.S. 20.
128. *See id.*
129. *See id.* at 30-33.
130. *See id.*
131. *See id.* at 30-31.
132. *See id.* at 32.
133. *See id.* at 32-33.
134. *Id.* at 30 (citing Rodriguez de Quijas v. Sherson/American Express, Inc., 490 U.S. 477, 481 (1989)).
135. In regards to arbitrator bias, the Court noted that the NYSE rules required that parties be informed of the employment histories of arbitrators, that they be allowed to make further inquires into arbitrator backgrounds, and that each party had one peremptory challenge and unlimited challenges for cause. Also, the rules required arbitrators to disclose any circumstances that might preclude their objectivity and impartiality. The NYSE rules also provided for detailed written opinions which would be available to the public and, since the rules did not restrict collective proceeding or the types of relief which could be awarded, they were consistent with statutory purposes. Finally, the Court explained that mere inequity of bargaining power did not render arbitration unenforceable in the employment context. *See Gilmer*, 500 U.S. at 30-33.

Nonetheless, by intricately detailing the features of an acceptable arbitration system, the United States Supreme Court implicitly suggested that arbitration processes that do not contain similar guarantees of fairness may be vulnerable to challenges in future cases.[136] The Court reminded lower courts to "remain attuned to well-supported claims that the agreement to arbitrate resulted from the sort of fraud or overwhelming economic power that would provide grounds 'for the revocation of any contract.'"[137] Moreover, the decision did not reject the suggestion that a minimum level of fairness is required for employment arbitration. Instead, the Court concluded its procedural analysis by noting that, "[a]s with the claimed procedural inadequacies discussed above, [a] claim of unequal bargaining power is best left for resolution in specific cases."[138]

The *Engalla* decision presents the sort of case-specific analysis of arbitration procedures that was alluded to in *Gilmer*. After a careful examination of the procedures established by Kaiser's arbitration clause, the California Court found the system to be so unfair that it amounted to fraud in inducing enrollees to agree to such a process as well as waiver of any right to arbitration that Kaiser may have originally possessed.[139] As detailed above, decisions from Texas, Massachusetts, and California suggest that the procedural-fairness approach of *Engalla* can also be applied to arbitration systems that are used to resolve employment disputes.[140] In combination with the *Engalla* decision, these cases reveal an evolving standard of heightened procedural scrutiny for arbitration in the employment context.

Nevertheless, the procedural analysis in *Gilmer* was only a small part of that decision. As explained above, it did not alter the Court's ultimate support for arbitration. Instead, the Court's narrow holding focused on the enforceability of arbitration decisions: the Court held that an agreement to arbitrate will be enforced with respect to claims under the Age Discrimination in Employment Act because Congress did not explicitly express, through either the text or legislative history of the Act, any intent to preclude arbitration of such claims.[141]

136. *See* Hoffman, *supra* note 77, at 154.

137. *Gilmer*, 500 U.S. at 33 (citing Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 627 (1985)).

138. *Id.*

139. *See Engalla*, 938 P.2d at 922, 924.

140. *See supra* notes 72, 75 and accompanying text.

141. *See Gilmer*, 500 U.S. at 35. "[H]aving made the bargain to arbitrate, the party should be held to it unless Congress itself has evinced an intention to preclude waiver of judicial remedies for the statutory rights at issue." *Id.* at 26 (quoting Mitsubishi Motors

Most courts similarly limit their review of arbitration issues to two narrow subjects: (1) the arbitrability of the dispute in question (for example, whether or not a statutory discrimination claim can be subject to arbitration) and (2) the enforcement of particular arbitration decisions.[142] The procedural aspects of arbitration arrangements are usually ignored in such decisions. This approach is consistent with the Federal Arbitration Act ("FAA") which contains minimal procedural safeguards. The FAA provides that arbitration awards will be vacated only where procured by fraud or corruption, for evident partiality in the arbitrator, or for arbitral misconduct in refusing to postpone a hearing upon sufficient cause or other misbehavior prejudicial to a party's rights.[143] In addition, courts will invalidate an arbitration award if the decision amounts to a manifest disregard for the law.[144] This principle is a narrow one. A manifest disregard for the law is shown only if "the majority of arbitrators deliberately disregarded what they knew to be the law in order to reach the result they did."[145]

Courts that restrict the review of arbitration to issues of enforcement and arbitrability are simply adhering to the broad deference to arbitration that was explicitly ordered by the United States Supreme Court in the "Steelworkers Trilogy."[146] Likewise, the California Supreme Court mandates a high level of deference to arbitration. In *Moncharsh v. Heily & Blase*,[147] the California Court went so far as to hold that a binding arbitration award is not appealable even when the decision is based on erroneous fact or law.[148] The rationale behind strict judicial respect for arbitration agreements and awards is the notion that if parties agree to arbitrate a particular dispute, then an arbitrator's decision was intended to

Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)).

142. *See* Malin, *supra* note 60, at 83.

143. *See* 9 U.S.C. § 10 (West 1997).

144. *See, e.g.*, Health Servs. Management Corp. v. Hughes, 975 F.2d 1253 (7th Cir. 1992); Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056 (9th Cir. 1991); Advest, Inc. v. McCarthy, 914 F.2d 6 (1st Cir. 1990). *See also* Malin, *supra* note 60, at 102 n.120 (citing various circuit courts' use of the manifest disregard standard).

145. *Hughes*, 975 F.3d at 1267. In 1995, the United States Supreme Court expressly adopted the manifest disregard standard for review of the merits of an arbitral decisions. *See* First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, —, 115 S. Ct. 1920, 1923-24 (1995).

146. *See* United Steelworkers of Am. v. American Mfg. Co., 363 U.S. 564 (1960); United Steelworkers of Am. v. Warrior & Gulf Navigation Co., 363 U.S. 574 (1960); United Steelworkers of Am. v. Enterprise Wheel & Car, Corp., 363 U.S. 593 (1960).

147. 832 P.2d 899 (Cal. 1992).

148. *See id.* at 915-16. See also Buse, *supra* note 57, at 1501 & nn.105-09, for a detailed discussion of the case.

resolve the dispute. Accordingly, courts should not interfere with the parties' original intent.

Nevertheless, arbitration decisions are overturned in limited circumstances. For example, California's arbitration statute, section 1281.2 of the Code of Civil Procedure, provides that an agreement to arbitrate is unenforceable if "[g]rounds exist for the revocation of the agreement."[149] Similarly, the FAA provides that an arbitration award is "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[150] Therefore, the *Engalla* court, and like-minded courts around the country, can avoid traditional modes of arbitral deference by concluding that flaws in the arbitration process rise to such an objectionable level that the initial agreement to arbitrate is subject to revocation. That is, where procedural unfairness is successfully linked to claims of fraud, waiver, or unconscionability, as alleged in *Engalla*, traditional deference to arbitration and the usual presumption of arbitrability may be overcome.

The fact that this approach may be used by courts does not mean it ought to become a common mode of analysis. The particular facts of the *Engalla* case may conceal the troublesome repercussions that would derive from a "fairness" approach to the enforcement of arbitration agreements. In *Engalla*, Kaiser drastically failed to implement its arbitration promises and, due to its systematic delays, Mr. Engalla died before having the opportunity to present his claims.[151] Kaiser's arbitration system may have been so egregious that it produced one of those dreaded opinions in which bad facts made bad law. Arguably, heightened scrutiny for procedural "fairness" is inappropriate for arbitration review. First, the concept of "fairness" is open-ended and highly elusive. How can courts adequately explain what differentiates a "fair" arbitration system from an "unfair" one, such that future parties can structure arbitration agreements in a non-offensive manner? A second problem concerns the contractual nature of arbitration. The parties agreed to a specific arbitration process. Why not hold them to their bargain as long as their consent satisfies traditional contract requirements? Furthermore, should review of fraud or waiver claims be limited to the circumstances surrounding the formation of an arbitration agreement or should review be extended to the actual operation of the arbitration process? Past arbitration cases favor the former approach. In those cases, review was generally limited to

149. CAL. CIV. PROC. CODE. § 1281.2(b) (West 1997).
150. 9 U.S.C. § 2 (West 1997).
151. *See Engalla*, 938 P.2d at 912.

inspecting for any inappropriate inducement of the arbitration agreement.[152] Finally, by associating fraud with "unfair" arbitration procedures, the *Engalla* decision threatens to undercut arbitration as a courtroom alternative. Under an extreme application of the *Engalla* analysis, whenever a court is convinced that an arbitration system contains some measure of "unfairness," the agreement to arbitrate is subject to nonenforcement because of fraud, waiver, unconscionability, or some other contract doctrine. Such an approach, as Justice Brown warned in her dissent, threatens to burst open the dam and nullify arbitration as a mode of dispute resolution.[153]

Any threat posed by *Engalla*, however, depends on whether the decision represents an anomaly or the start of a judicial trend. Unfortunately, it is too early to make this determination. Yet, in the shadow of *Engalla* and similar cases, employers and employees are now on notice that some courts will be critical of arbitration procedures. At the very least, the *Engalla* decision represents a warning to employers. If an employer wants to arbitrate workplace disputes it should ensure that its arbitration system satisfies a minimum level of procedural fairness. To do otherwise risks non-enforcement of the arbitration clause and a loss of arbitration's desired advantages.

III. Case Study: The Securities Industry

The arbitration experience of the securities industry exhibits the successes and deficiencies of using mandatory arbitration for employment disputes. As a condition of employment in the securities industry, all securities dealers are required to file a registration and disclosure agreement known as a U-4.[154] This registration form contains a mandatory arbitration clause requiring securities employees to arbitrate all employment disputes.[155] The resulting arbitration programs are administered by self-regulating organizations (SROs), such as the New York Stock Exchange (NYSE) or the National Associations of Securities Dealers (NASD), and must be approved by the Securities and Exchange Commission.[156] Although individual organizations such as the NASD can uniquely

152. *See, e.g.*, Prudential Ins. Co. v. Lai, 42 F.3d 1299, 1305 (9th Cir. 1994) (holding that arbitration must be knowingly accepted by an employee); *see also*, Howard, *supra* note 67, at 266-69.

153. *See Engalla*, 938 P.2d at 932.

154. *See* GAO REPORT, *supra* note 64, at 4.

155. *See id.*

156. *See id.* at 5.

tailor their arbitration procedures, most securities organizations model their arbitration systems on the Uniform Code of Arbitration that was developed by the Securities Industry Conference on Arbitration in 1977.[157]

As discussed above, the United States Supreme Court's *Gilmer* decision found this type of arbitration agreement binding for ADEA claims and expressly sanctioned the arbitration procedures used by the NYSE.[158] Several lower courts have extended the *Gilmer* decision and require securities employees to arbitrate a variety of other statutory employment claims.[159] Through these decisions, the securities industry has successfully attained many of the time and cost advantages provided by arbitration.[160]

The arbitration of employment disputes in the securities industry, however, has not been without its detractors. Notably, scholars point out that the securities industry arbitration process was not designed to resolve the range of claims it currently encompasses.[161] The initial purpose of securities arbitration was to resolve commercial disputes between the industry and public investors.[162] This historical origin, along with the continued prominence of investor-firm disputes, results in an arbitrator pool that lacks experience in employment law.[163] For instance, neither the NYSE nor the NASD assigns arbitrators to arbitration panels on the basis of their knowledge of the subject matter of the dispute.[164] Consequently, an employment claim will likely be heard by arbitrators whose expertise lies in complex securities matters, not employment law.[165] This problem becomes especially acute when discrimination claims are involved. The 1994 Government

157. *See id.*

158. *See supra* text accompanying notes 130-35.

159. *See, e.g.*, Alford v. Dean Witter Reynolds, Inc., 939 F.2d 229, 230 (5th Cir. 1991) ("Title VII claims can be subjected to compulsory arbitration."); Willis v. Dean Witter Reynolds, Inc., 948 F.2d 305, 312 (6th Cir. 1991); Bender v. A.G. Edwards & Sons, Inc., 971 F.2d 698, 700 (11th Cir. 1992); Prudential Ins. Co. of Am. v. Lai, 42 F.3d 1299, 1303 (9th Cir. 1994) ("Our circuit has extended *Gilmer* to employment discrimination claims brought under Title VII."); Metz v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 39 F.3d 1482, 1487 (10th Cir. 1994). *But see* Duffield v. Robertson Stevens & Co., 144 F.3d 1182, 1199 (9th Cir. 1998) (holding that the Civil Rights Act of 1991 establishes Congress' intention to preclude the enforcement of mandatory pre-dispute agreements to arbitrate Title VII claims).

160. *See* GAO REPORT, *supra* note 64, at 1.

161. *See* Dunphy, *supra* note 64, at 1172.

162. *See id.*

163. *See* GAO REPORT, *supra* note 64, at 11-12.

164. *See id.*

165. *See id.* at 9.

Accounting Office report recognized that "[d]iscrimination suits are inherently different from the usual types of employment disputes arbitrated by SROs because they involved issues in federal civil rights law that lie beyond the scope of securities law and industry practices."[166] Therefore, the report suggested that each arbitration panel include at least one arbitrator with experience in employment or discrimination law.[167] Another securities arbitration deficiency involves the lack of arbitrator diversity. In terms of race, gender, and age, securities arbitrators are far less diverse than the claimants who seek resolution of discrimination disputes.[168] Employment arbitration in the securities industry is further hindered by insufficient oversight. The Securities and Exchange Commission focuses its arbitration inspections on customer-firm disputes rather than employer-employee arbitrations.[169] Moreover, many of the general criticisms of mandatory employment arbitration apply with similar force to the securities context.[170]

Deficiencies in the securities arbitration process have led to a gradual dissatisfaction with securities employment arbitration in both the courts and in the industry itself. As noted in Part II, a district court in Massachusetts found that the NYSE's arbitration system inadequately protected the rights of employees.[171] Likewise, two sex discrimination suits were recently settled under terms which will alter the use of binding arbitration for some securities employees. In one case, the defendant securities firm, Smith Barney, Inc., agreed to allow sexual harassment and discrimination plaintiffs to use outside referees.[172] Under the proposed settlement, an outside mediator will attempt to resolve the disputes and forward unresolved cases to a three-member arbitration panel that includes at least one woman.[173] In a separate settlement, the brokerage firm Merrill Lynch abandoned its policy of requiring employees to arbitrate employment claims and will now allow claimants to bring suit in court regardless of the language found in the securities industry's U-4 form.[174]

166. *Id.* at 12.

167. *See id.*

168. *See id.*

169. *See id* at 12.

170. *See supra* notes 82-87 and accompanying text; *see also* Dunphy, *supra* note 64, at 1201-02.

171. *See supra* notes 69-74 and accompanying text.

172. *See Smith Barney Break With Wall St. in Settling Harassment Case*, WASH. POST, Nov. 19, 1997, at C12.

173. *See id.*

174. *See* Cremin v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 957 F. Supp. 1460 (N.D. Ill. 1997).

These judicial developments, in conjunction with criticism of employment arbitration, prompted the NASD to amend its U-4 arbitration provision.[175] In August 1997, the NASD eliminated the U-4 provision that required securities dealers to arbitrate statutorily based employment discrimination claims.[176] This change was approved by the Securities and Exchange Commission.[177] Similarly, the NYSE proposed a similar rule change in 1998.[178] However, these changes do not forbid individual securities firms from including mandatory arbitration agreements in their own employment contracts. Firms that continue to insist on employment dispute arbitration may become less attractive to potential employees, but the perceived benefits of arbitration may still prompt firms to use independent arbitration programs. Securities firms, like other employers seeking to arbitrate employment claims, will have to consider what substantive and procedural guarantees should be included in their arbitration programs. Moreover, securities firms also need to consider whether their arbitration system can withstand an *Engalla* "fairness" analysis.

IV. Responding to the *Engalla* Decision

The *Engalla* decision poses a dilemma for employers seeking to use arbitration for employment disputes: how should *Engalla* be interpreted and applied by employers? At one extreme, the decision is an indictment of the procedural problems associated with employment arbitration systems and a warning that such systems will not be upheld as a legitimate alternative to judicial resolution. However, the *Engalla* Court did not generally chastise arbitration as a form of dispute resolution. Rather, the Court found fault with the particular procedures used by Kaiser in its arbitration program. Therefore, the crucial question is not whether arbitration is viable, but what minimum set of procedural safeguards will enable a particular arbitration system to withstand the judicial scrutiny of an *Engalla* "fairness" analysis. Various alternatives are available to guarantee the fair resolution of employment-disputes. An extreme

175. *See* Deborah Lohse, *NASD Votes to End Arbitration Rules in Cases of Bias*, WALL ST. J., Aug. 8, 1997, at B14.

176. *See id.*

177. *See* Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Approval to Proposed Rule Change Relating to the Arbitration of Employment Discrimination Claims, 63 Fed. Reg. 35,299 (1998).

178. *See* Self-Regulatory Organizations; Notice of Filing of Proposed Rule Changes by the New York Stock Exchange, Inc. Relating to Arbitration Rules, 63 Fed. Reg. 52,782 (1998).

solution would prohibit employment dispute arbitration. At the opposite end of the spectrum, *Engalla* could be ignored as unhelpful and inapplicable to future cases. Most commentators, however, acknowledge the benefits of arbitration and therefore suggest various changes to arbitration procedures rather than wholesale abandonment. If implemented, such safeguards are likely to shield employers from the potentially negative repercussions of the *Engalla* decision.

As mentioned above, one possible response to the *Engalla* decision is to disregard it. According to this view, the Court's analysis was an interesting, but unimportant, aberration in arbitration jurisprudence. Moreover, the unconventional "fairness" analysis used by the California Court was prompted by the unique facts of the case, and it will not be generally applied in future challenges to mandatory arbitration agreements. Such a view is not outrageous. Kaiser's self-administered arbitration program involved disturbing patterns of delay and obstruction.[179] Moreover, Kaiser's practice of delay resulted in the death of the misdiagnosed claimant before he had an opportunity to challenge the treatment he received from Kaiser doctors. Even the *Engalla* dissent acknowledged that the "intended target of the majority's wrath... could not be more deserving."[180] The unique facts of Kaiser's arbitration program offended the justices to such a degree that their examination of the legal claims of waiver and fraud was guided by a factual condemnation of Kaiser's arbitration process. The Court may not have intended a "fairness" analysis of Kaiser's procedures; it may have been merely a byproduct of the factual circumstances involved in the case.

Nonetheless, even if this dismissive view controls, *Engalla* should not be totally ignored. At a minimum, the decision provides a specific example of how not to structure an arbitration system: (a) do not set unrealistic timelines for arbitration proceedings if the system will repeatedly fail to satisfy the time frames, and (b) do not make claims of speed and efficiency if the arbitration program is consistently unable to live up to such promises. These simple rules may be the narrow lesson of *Engalla*, and the unconventional procedural scrutiny employed in the decision might only be repeated when an arbitration program is similarly outrageous. Nevertheless, in view of the widespread criticism of employment dispute arbitration and the sparse, but seemingly growing, collection of judicial scrutiny of arbitration procedures, a passive response to the *Engalla* decision

179. *See Engalla*, 938 P.2d at 908-14.

180. 938 P.2d at 927 (Brown, J., dissenting).

would be a dangerous gamble for employers who wish to enjoy the benefits of arbitration.

In direct opposition to the view that *Engalla* maintains the status quo, some critics of employment arbitration contend that the *Engalla* decision does not go far enough. Instead, these critics advocate the complete prohibition of pre-dispute arbitration agreements in non-union employment contracts. This position has been taken up in both federal and state legislatures. In 1994, the Coercive Employment Agreements Act was proposed in the United States Senate.[181] This bill would prohibit employers from requiring employees to agree to arbitration as a condition of employment or job advancement.[182] Meanwhile, in the House of Representatives, the Civil Rights Procedures Protection Act of 1994 attempted to amend federal civil rights statutes.[183] The bill sought to add language providing that the statutes determined procedure for and retained exclusive power over employment claims.[184] In addition, the bill provided that arbitration agreements could only be entered into after a dispute had arisen.[185] Other proposals in the United States Senate and House have similarly called for amendments to federal civil rights statutes in order to prevent the involuntary arbitration of claims arising from unlawful employment discrimination.[186] However, none of the federal proposals have passed.

California has witnessed similar attempts to prohibit employment dispute arbitration.[187] Meanwhile, several states have gone beyond mere proposals and have enacted restrictions on arbitration in the employment context.[188] For instance, some states do not enforce agreements to arbitrate future disputes.[189] Other state

181. *See* S. 2012; *see also* Ponte, *supra* note 123, at 360 n.4 (citing Hope B. Eastman & David M. Rothenstein, *The Fate of Mandatory Employment Arbitration Amidst Growing Opposition: A Call for Common Ground*, 20 EMPLOYEE REL. L.J. 595, 601 (1995)).

182. *See* S. 2012.

183. H.R. 4981.

184. *See* Ponte, supra note 123, at 360 n.4.

185. *See id.*

186. *See* S. 63, 105th Congress (January 21, 1997); H.R. 3748, 104th Congress (1996); H.R. 983, 105th Congress (March 6, 1997).

187. *See* Cal. A.B. 574, Cal. Reg. Sess. (February 25, 1997) (intending to prohibit pre-dispute arbitration agreements between employees and employers); Cal. S.B. 19, Reg. Sess. (December 2, 1996) (proposing to amend the California Code of Civil Procedure to require that courts vacate arbitration awards if a standardized contract, drafted by a non-consumer party, contains a mandatory arbitration provision which binds a consumer party (a consumer is defined as an employee pursuing an employment dispute)).

188. *See* Grodin, *supra* note 68, at 18 nn.103-13 (listing the various state statutes which limit the enforceability of arbitration).

189. *See* ALA. CODE § 6-6-1 (Michie Supp. 1995); HAW. REV. STAT. § 658-2 (1993);

statutes specifically prohibit the enforcement of arbitration agreements in employment contracts.[190]

In the judicial realm, only the Court of Appeals for the Ninth Circuit has held that mandatory pre-dispute agreements to arbitrate employment disputes are unenforceable.[191] In *Duffield v. Robertson Stevens & Co.*, the Ninth Circuit found that the text, legislative history, and purposes of the Civil Rights Act of 1991, which amended Title VII, evinced the congressional intent to preclude the waiver of the judicial forum for Title VII discrimination claims.[192]

Prohibiting mandatory employment arbitration offers an appealing solution to critics of unfair arbitration procedures. An absolute prohibition immediately eliminates the unease associated with a private arbitrator applying public discrimination laws since an employee could pursue statutory claims in court. As illustrated by legislative proposals and the *Duffield* decision, some commentators feel that employment discrimination statutes were intended to be interpreted and applied by courts of law. Nonetheless, such an extreme response to the perceived flaws of arbitration reintroduces many of the problems arbitration was devised to avoid. For instance, the absence of arbitration would further clog the courts with employment dispute lawsuits. In addition, employees and employers would be saddled with the slow, cumbersome, and expensive attributes of the trial system.

In light of these concerns, many observers propose a compromise between the above described extremes. According to this view, mandatory arbitration of employment disputes should be permitted (or even favored) so long as procedural safeguards are included to

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MISS. CODE ANN. § 11-15-101 (Law Co-op 1972 & Supp. 1995); VA. CODE § 55-10-1 (1990).

190. *See* ARIZ. REV. STAT. ANN. § 12-1517 (West 1982); IOWA CODE ANN. § 679A.1(2)(b) (West 1987); KAN. STAT. ANN, sec. 5-401(c)(2) (1986); KY. REV. STAT. ANN. sec. 417.050 (Michie 1992); KY. REV. STAT. ANN. § 336.700 (Michie 1995); LA. REV. STAT. ANN. 9:4216 (West 1991); MD. ANN. CODE § 34-206(b) (Michie 1989 & Supp. 1995); S.C. CODE ANN. § 16-108-201 (Michie 1987); MO. ANN. STAT. § 435-350 (West 1992). Although these statutes are impressive as an indication of legislative trends, they have limited practical effect due to the preemptive force of the Federal Arbitration Act, which has been interpreted to cover general employment contracts. *See* Grodin, *supra* note 68, at 18. See also Grodin, *supra* note 68, at 15-20, for a discussion of the conflicting interpretations of the Federal Arbitration Act's § 1 exemption for "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." 9 U.S.C. §1 (West 1997). Most lower courts have found that §1 does not exempt the majority of employment contracts. *See* Malin, *supra* note 60, at 88-91; Buse, *supra* note 57, at 1503-05 & n.126.

191. *See* Duffield v. Robertson Stevens & Co., 144 F.3d 1182, 1199 (9th Cir. 1998).

192. *See id.*

ensure the fairness of such an arrangement. In the wake of the *Engalla* Court's careful scrutiny of Kaiser's arbitration procedures, adding procedural safeguards to mandatory arbitration systems appears to be the surest way to guarantee that a particular arbitration system will survive judicial review. The question that remains, however, is what minimum set of procedural safeguards will pass muster under a "fairness" analysis.[193]

The *Engalla* decision itself offers the first clue towards answering this question. Part of the Court's criticism of Kaiser's arbitration program was that Kaiser acted as administrator for its own program.[194] The majority noted that "many large institutional users of arbitration, including most health maintenance organizations (HMO's), avoid potential problems of delay in the selection of arbitrators by contracting with neutral third party organizations, such as the American Arbitration Association (AAA)."[195] The Court's statement indicates that contracting with an outside arbitration agency will counter a presumption of unfairness that is associated with an employer-administered arbitration processes. One reason neutral organizations counter any perceived unfairness is that many have adopted special arbitration rules that provide for claimant representation, discovery as deemed necessary by the arbitrator, and written opinions.[196] Moreover, users of the AAA are required to abide by these immutable procedural guidelines.[197]

Kaiser Permanente, meanwhile, has taken the *Engalla* Court's suggestions to heart. In January 1998, Kaiser announced that it was adopting a set of major changes to its malpractice arbitration system, as proposed by an independent panel.[198] The accepted recommendations included the creation of an independent administrator to manage Kaiser's system, procedures to speed up its

193. A 1997 study revealed that existing arbitration systems are remarkably diverse and contain varying levels of procedural safeguards. Meanwhile, several companies in the study have not yet instituted an arbitration system for employment disputes but remain interested in doing so; they are waiting to see what type and what level of safeguards will be required by the courts before proceeding. *See* Bickner et al., *supra* note 58, at 82.

194. *See Engalla*, 938 P.2d at 922.

195. *Id.* at 918.

196. *See id.* at n.9 (citing AMERICAN ARBITRATION ASSOCIATION, EMPLOYMENT DISPUTE RESOLUTION RULES (INCLUDING MEDIATION AND ARBITRATION RULES) (1993)). The AAA has also published a guide to assist employers in creating internal dispute resolution procedures: AMERICAN ARBITRATION ASSOCIATION, RESOLVING EMPLOYMENT DISPUTES: A MANUAL ON DRAFTING PROCEDURES (1993).

197. *See Engalla*, 938 P.2d at 918 n.9.

198. *See* Harriet Chiang, *Kaiser to Revamp Arbitration System*, S.F. CHRON., Jan. 7, 1998, at A15.

process, and regular audits and evaluations of the process.[199]

In addition, two organized efforts have attempted to outline the procedural protections required for a fair arbitration proceeding: the Dunlop Commission Report[200] issued by the United States Departments of Commerce and Labor and the Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship.[201] The Dunlop Commission encouraged the use of private arbitration for workplace disputes but also recognized the need for standards to govern such procedures.[202] The Commission identified several essential features of an acceptable plan, including: a neutral arbitrator who knows the law; employee access to information for presenting a claim; cost sharing; the right to representation; remedies equal to those available through litigation; reasoned, written opinions; and judicial review of decisions to ensure consistency with the law.[203] The Due Process Protocol, composed of representatives of the American Bar Association and several private ADR organizations, also recommended certain procedural safeguards.[204] The Protocol found that representation, adequate discovery, written decisions, and remedies equal to those available in court were essential standards for arbitration agreements.[205] Although these reports are merely advisory and not binding on courts, they provide insight into what experts consider to be the minimum procedural safeguards necessary for arbitration.

Scholarly examinations of employment arbitration also offer a plethora of suggested procedural requirements. One recurring demand is that employment disputes be heard by arbitrators who have sufficient experience with employment law.[206] Moreover, it is suggested that arbitrators be chosen from a pool of sexually and racial diverse individuals who reflect workplace demographics.[207] Many commentators also propose changes in how arbitrators are selected in

199. *See id.*

200. *See* Report AND RECOMMENDATIONS, COMMISSION ON THE FUTURE OF WORKER-MANAGEMENT RELATIONS (December 1994) [hereinafter REPORT AND RECOMMENDATIONS].

201. *See Task Force on Alternative Dispute Resolution in Employment, A Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship*, DISP. RESOL. J. Oct-Dec. 1995, at 37 [hereinafter *Task Force*].

202. *See* REPORT AND RECOMMENDATIONS, *supra* note 200, at 30-31.

203. *See id. See also* Bickner et al., *supra* note 58, at 12.

204. *See Task Force, supra* note 201.

205. *See id.*

206. *See* Buse, *supra* note 57, at 1532-33; Dunphy, *supra* note 64, at 1213-14; GAO REPORT, *supra* note 64, at 12.

207. *See* Ponte, *supra* note 123, at 385-86; Dunphy, *supra* note 64, at 1214. *See also* GAO REPORT, *supra* note 64, at 12.

specific disputes. For instance, fears regarding the fairness of an arbitration process are reduced where employees are given an equal voice in selecting an arbitrator.[208] A related suggestion would allow employees to challenge arbitrators through a "certain number of preemptory challenges and unlimited challenges for cause."[209] In 1997, the Chief of the National Labor Relations Board, William Gould, offered similar recommendations to ensure the impartiality of arbitration, including the use of diverse arbitrators who have expertise in employment discrimination, the sharing of arbitration costs between employers and employees, and giving employees a voice in selecting arbitrators.[210]

The fairness of employment arbitration would also be strengthened by taking several steps at the time when an employee initially agrees to an arbitration provision. For instance, employers should clearly and specifically explain what disputes are covered by their arbitration provision and what rights are waived by agreeing to arbitrate, such as the right to appeal, the right to extensive discovery, and the right to a jury.[211] Similarly, commentators advise that employees be adequately educated regarding the benefits and disadvantages of arbitration[212] and be provided with clear, understandable notice of the meaning and scope of arbitration, perhaps through a separate acknowledgment form.[213]

Adjustments to arbitration hearings themselves might also help guarantee the fairness of employment arbitration. Most importantly, employees should be given a right to representation by counsel.[214] Flexible discovery, as deemed necessary by the arbitrator in a particular dispute, could also reinforce the legitimacy of employment arbitration decisions.[215] Furthermore, in order to maintain the integrity of federal employment statutes, the procedures outlined in Title VII and other such statutes should be followed in arbitration proceedings.[216] The publication of reasoned, written opinions has

208. *See* Grodin, *supra* note 68, at 43-44; Malin, *supra* note 60, at 98; Ponte, *supra* note 123, at 385-86; Buse, *supra* note 57, at 1532; Dunphy, *supra* note 64, at 1214.

209. Ponte, *supra* note 123, at 386.

210. *See* Ilana DeBare, *NLRB Chief Backs Rules for Arbitration*, S.F. CHRON., Apr. 10, 1997, at C1.

211. *See* Buse, *supra* note 57, at 1519-22, and *cf.* Hoffman, *supra* note 77, at 156; Howard, *supra* note 67, at 283; Ponte, *supra* note 123, at 385.

212. *See* Ponte, *supra* note 123, at 385.

213. *See* Buse, *supra* note 57, at 1526.

214. *See* Grodin, *supra* note 68, at 45; Malin, *supra* note 60, at 98.

215. *See* Oakley & Mayer, *supra* note 72, at 532; Buse, *supra* note 57, at 1534-35; Dunphy, *supra* note 64, at 1215.

216. *See* Ponte, *supra* note 123, at 385. *See also* Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985) ("By agreeing to arbitrate a statutory

also been recommended in order to ensure the fairness of employment arbitration.[217] Finally, several writers propose enhanced judicial review of employment arbitration decisions.[218] This last proposal seeks to ensure that arbitrators will properly apply the substantive law of employment statutes.

Despite their commendable appeals to general notions of fairness, the above proposals raise several problems. Providing for increased discovery and heightened judicial review makes arbitration look more like the trial system that it is intended to replace. Such alterations may diminish the speed, efficiency, inexpensiveness, and finality that arbitration was designed to provide. Another problem with "fairness" proposals is that it will be extremely difficult for courts to police arbitration systems for "fairness." Unlike *Engalla*, where Kaiser's system was uniquely unsettling, a closer case may lead to decisions based on the subjective notions of fairness held by a particular judge. Employers would be helpless in trying to determine what type of arbitration system will pass judicial muster. Therefore, adopting meaningful and enforceable standards for arbitrator selection and discovery may be a task best left to legislatures or administrative agencies.[219]

Proponents of these procedural changes argue, however, that any negative effects will be negligible or will be outweighed by the benefits they create. For example, judicial review of employment arbitration decisions could be limited to ensuring arbitrator adherence to statutory prerogatives; courts would give broad deference to arbitrator fact findings while conducting *de novo* review of an arbitrator's legal conclusions.[220] Meanwhile, increased discovery rights may leave employees more amenable to the arbitration system and less distrustful of mandatory arbitration clauses.[221]

claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.").

217. *See* Grodin, *supra* note 68, at 47; Oakley & Mayer, *supra* note 72, at 533; Buse, *supra* note 57, at 1537; Dunphy, *supra* note 64, at 1215.

218. *See* Grodin, *supra* note 68, at 46-47; Malin, *supra* note 60, at 104-05; Malin & Ladenson, *supra* note 56, at 1237-38; Buse, *supra* note 57, at 1537-38; Dunphy, *supra* note 51, at 1215; Oakley & Mayer, *supra* note 72, at 533-34.

219. *See, e.g.*, Grodin, *supra* note 685, at 52-53.

220. *See* Malin & Ladenson, *supra* note 56, at 1238.

221. *See* Buse, *supra* note 57, at 1535.

V. Withstanding *Engalla's* Procedural "Fairness" Standard: A Proposal

Despite the difficulties that will accompany an increase in arbitration's procedural protections, some measure of procedural safeguards should be adopted in the employment arbitration context. Procedural protections will help reduce the unease that many commentators have with employment arbitrators deciding important questions of statutory law. Moreover, an increase in procedural safeguards represents a desirable compromise between the unfavorable extremes of either leaving arbitration alone, and thereby risking the nonenforcement of "unfair" systems, or outlawing employment dispute arbitration entirely. Finally, and most importantly, an employment arbitration system that includes procedural safeguards will withstand judicial scrutiny under a "fairness" standard and thus avoid the refusal to compel arbitration that occurred in *Engalla.*

Therefore, this Note proposes that all employment arbitration proceedings include the following features. First, employees should never be solely responsible for paying the costs and fees of an arbitration proceeding.[222] Instead, as suggested by JAMS/Endispute, a national arbitration services organization, arbitration procedures should allocate costs in a way that does not preclude access by the employee to the procedures.[223] In some situations, an employer should offer to pay all arbitration costs. This would be advisable where the employer unilaterally drafts the employment contract and offers it to employees on a take-it-or-leave-it basis. Nevertheless, since a perception of arbitrator partiality could arise where the employer alone pays all arbitration costs and fees, employees should always be given the opportunity to pay an equal share.[224] In situations where an arbitration agreement is the product of arms-length negotiations between the employer and employee, the equal sharing of arbitration costs and fees will be appropriate. Arbitration agreements are contractual arrangements; thus, if the parties to the contract agree to split the costs and fees of arbitration, their wishes should be respected. As long as costs and fees are shared equally, any procedural unfairness regarding arbitration costs and fees is

222. In *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1468 (D.C. Cir. 1997), the D.C. Circuit held that an employer cannot require an employee to pay all or part of an arbitrator's fee.

223. *See* JAMS/ENDISPUTE, MINIMUM STANDARDS OF PROCEDURAL FAIRNESS, POLICY ON EMPLOYMENT ARBITRATION (1998) (encouraging any company that implements mandatory arbitration to adopt various arbitration procedures).

224. *See id.*

sufficiently reduced.

Second, arbitration procedures should ensure a minimum level of discovery. Discovery ordinarily should not be as broad as it would be in litigation or else the advantages of speed and efficiency potentially available from arbitration will be destroyed. However, every arbitration must at least permit the discovery necessary for full and adequate consideration of the employment claims in a particular dispute. Thus, at a minimum, employees should have the right to document exchange and the deposition of the supervisor or other decision-maker responsible for the adverse employment action.[225] Likewise, employers should be entitled to documents and the deposition of the employee.[226] In many cases, an abbreviated level of discovery will sufficiently inform an arbitrator as to the parties contentions. However, complex or unusual cases may require extensive discovery and this should not be curtailed for the sake of rushing a dispute to conclusion.

Third, arbitration must be conducted by a neutral, impartial arbitrator who is mutually selected by both parties. A relatively straightforward way to ensure impartiality is to contract with an outside arbitration agency for the appointment of arbitrators. This will counter any presumption of unfairness that is naturally associated with an arbitration process administered exclusively by one party. Moreover, employment dispute arbitrators should have some experience or familiarity with employment law as well as the statutes that affect the workplace.

Fourth, employment arbitrators should not be restricted in the remedies they may award. Instead, arbitrators should have the authority to grant whatever relief is available in court under law or equity. Full access to remedies ensures that participants possess the same rights and opportunities to relief that they would have in court.

Fifth, arbitration decisions should be accompanied by well-reasoned, written opinions. This requirement may reduce the risk that an arbitration decision will be vacated by a reviewing court. In a recent Second Circuit case, *Halligan v. Piper Jaffey, Inc.*,[227] the court held that when arbitrators do not explain the rationale for their award, the arbitration decision may be vacated if it appears not to conform with the evidence presented at the arbitration proceeding.[228]

225. *See id.*

226. *See id.*

227. 148 F.3d 197 (2d Cir. 1998).

228. *See* Ruth V. Glick, *Write It Down: Lack of Reasoned Opinion Supports Vacating Award*, S.F. DAILY J., Oct. 28, 1998, at 5. Also, without a written award that explains the legal basis for the arbitrator's decision, a reviewing court will have nothing to counter the

Although the above suggestions require employment arbitration hearings to include various procedural protections, the suggestions, by their nature, also exclude certain safeguards. For example, a jury is not essential for arbitration proceedings. Agreeing to arbitrate carries with it the understanding that a dispute will be considered by an arbitrator (or arbitrators) and not by the judge and jury associated with courtroom proceedings. The relinquishment of a jury as decision-maker reflects a trade-off designed to ensure the efficiency and speed offered by arbitration. On average, the presence of a jury complicates and thereby prolongs a proceeding. Arbitration is intended to avoid this result. Consequently, a court will not find that the absence of a jury renders an arbitration proceeding "unfair."

Similarly, extensive discovery is not required. Although extensive discovery may sometimes be necessary in arbitration, arbitrators should attempt to limit discovery to levels that are minimally necessary for the arbitrator to reach an informed decision. Thus, material evidence must be discoverable and admissible. However, arbitration should not degenerate into the discovery gamesmanship that sometimes obstructs courtroom litigation.

Finally, judicial review of the merits of arbitration need not be expanded. As discussed earlier, most courts currently limit review of arbitration to issues of contract formation, the arbitrability of particular disputes, or outright arbitrator misconduct.[229] Great deference is given to an arbitrator's legal and factual conclusions regarding the merits of a dispute. This practice provides finality to arbitration participants because they know that the time-consuming appeals that often accompany courtroom litigation are rare in the arbitration context. The addition of procedural safeguards to the arbitration process should not alter the limited scope of judicial review. The examination of arbitration processes should be strictly limited to a review of arbitration procedures. Thus, when asked to review the merits of a decision, courts can continue to give great deference to arbitrator decisions.

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charge that the arbitrator manifestly disregarded the law. In contrast, when reviewing courts have a reasoned, written record to examine, they will be able to clearly see how an arbitrator applied the governing law and, more significantly, in most cases courts will confine their review to the limited grounds set forth in federal and state statutes. *See* 9 U.S.C. § 10 (West 1997); *see also* CAL. CIV. PROC. CODE § 1286.2 (West 1997) (providing grounds for vacating an arbitration award which are similar to those found in the federal statute); CAL. CIV. PROC. CODE § 1281.9 (West 1997) (vacation of arbitration award due to arbitrator's failure to make required disclosures); CAL. CIV. PROC. CODE § 1286.6 (West 1997) (correction of arbitration award). Under these narrow statutory grounds for review, courts are unlikely to vacate arbitral decisions except in unusual circumstances.

229. *See supra* notes 142-50 and accompanying text.

The above suggestions pose a risk that employment arbitration will become more like litigation. However, the importance of the statutory and common law rights at stake in employment disputes makes this risk worthwhile. Moreover, procedural protection may reduce the unease employees have in being subjected to arbitration and ensure both parties' willingness to submit employment disputes to arbitration. Most importantly, by adopting the procedural protections described above, an employment arbitration system will be able to survive the "fairness" analysis of *Engalla v. Kaiser Permanente.*

Conclusion

The California Supreme Court's *Engalla* decision portends a new direction in the judicial analysis of arbitration clauses. The arbitration procedures called for by mandatory arbitration clauses in the non-commercial context, particularly the employment context, may be subjected to a searching "fairness" scrutiny in future cases. Several other courts have taken a similar approach to arbitration systems and in combination with *Engalla* these decisions may represent a growing dissatisfaction with the alleged inequities of binding arbitration agreements. Nevertheless, the basic legitimacy of arbitration remains intact. Courts may continue to limit arbitration review to the contractual formation of arbitration agreements and the arbitrability of disputes under particular arbitration clauses. Moreover, particular courts may refuse to inquire into the procedures used by arbitration programs.

The question of whether *Engalla* represents the forefront of a new trend or a judicial anomaly, however, is of only secondary importance. The true significance of the decision is the risk it presents to employers who rely on arbitration clauses and the opportunity it offers to employees who seek to challenge binding arbitration. In the wake of *Engalla*, an employer who adopts or continues to apply an arbitration system which lacks minimum procedural protections may encounter intense judicial scrutiny of their arbitration process and risk a judicial finding that their arbitration procedures are "unfair." Like Kaiser, employers who use such a system will be deprived of arbitration's benefits. Meanwhile, employees who substantiate their unfairness claims will be able to successfully challenge binding arbitration clauses and thereby avoid arbitration's restraints.

The specific nature and amount of procedural protections required to withstand a "fairness" scrutiny remains unsettled. Courts and commentators suggest a wide variety of possible changes to

arbitration procedures, but no magic formula guarantees the enforceability of a particular system. Nonetheless, the *Engalla* decision has made it clear that some level of procedural safeguards should be included in arbitration programs. In the absence of procedural protections, employers take an unjustifiable risk that their arbitration system will be found unfair, and thus, unenforceable.