A STANDARD OF REASONABLENESS: CONSTRAINING MANDATORY ARBITRATION CLAUSES IN EMPLOYMENT AGREEMENTS

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I. INTRODUCTION

The Supreme Court recently reaffirmed its commitment to honoring arbitration clauses found in employment agreements. In Rent-A-Center v. Jackson, the Court reiterated its belief that arbitration agreements in the employment context should not be treated differently than similar agreements found in any commercial contract. The Rent-A-Center result was not surprising. In recent years, the Supreme Court has faced the issue of mandatory arbitration agreements numerous times, and in virtually every case, favored arbitration.

The Rent-A-Center plaintiff, Antonio Jackson, originally filed suit in federal court, claiming racial discrimination and retaliation. Jackson’s employer moved to dismiss the action and compel arbitration, citing the arbitration clause found within Jackson’s employment agreement. The agreement provided for arbitration of all disputes arising out of Jackson's employment with Rent-A-Center, including claims for discrimination. The agreement also provided that:

[T]he Arbitrator, and not any federal, state, or local court or agency, shall have exclusive authority to resolve any dispute relating to the interpretation, applicability, enforceability or formation of this Agreement including, but not limited to any claim that all or any part of this Agreement is void or voidable.

Jackson opposed the motion on the ground that the arbitration agreement was unconscionable and therefore not enforceable. Rent-A-Center responded that the court could not hear Jackson's unconscionability claim because Jackson had expressly agreed that the arbitrator would have exclusive authority to resolve any dispute about the enforceability of the

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2 Id. at 2775.
3 Id.
agreement. In the end, the Supreme Court sided with Rent-A-Center. The Court found that, to have a court hear a claim of unconscionability, a plaintiff must establish that the provision delegating questions of arbitrability to an arbitrator is unconscionable.4

Following Rent-A-Center, it seems certain that all challenges to the fairness of mandatory arbitration clause terms will be decided not by courts, but by arbitrators. The arbitrators themselves will decide whether the arbitration process is flawed.5 The Rent-A-Center decision means that the law places virtually no constraints on employers in their use of mandatory arbitration clauses in standard employment agreements. Within a few years, most employment agreements will contain broad arbitration provisions.

These arbitration clauses will reach all statutory claims. As seen below, statutes govern numerous aspects of employment. These statutes, defining the duties and responsibilities of the employer, resulted from public concern. Thus, before consigning all employment claims to private processes, we should ask whether relegating the resolution of employment claims to arbitration is a good idea. Are the public interests being satisfied “when public laws are enforced in the private fora?”6

In favoring arbitration clauses in employment agreements, the Supreme Court has relied on general contract principles.7 Essentially, the Court has found that if an employee has agreed to have his statutory discrimination heard in a private forum, then that employee should stick with the deal.8

However, relying on general contract principles to decide a matter involving the employment relationship is disingenuous. In fact, referring to the standard employment agreement as a traditional contract requires some imagination. Numerous areas of the employment relationship are not subject to contract. The employment relationship is heavily constrained by public law. The majority of the duties and obligations of an employment relationship are furnished by statute. An employment agreement, for the most part, only memorializes the employment relationship. The most important aspects of the employment relationship—occupational safety and health, minimum wage, overtime pay, discrimination—exist independently and cannot be waived in contract.

In essence, the employment relationship exists on a continuum. At one end of the spectrum lie those areas that are solely governed by contract. At the other end of the spectrum lie those rights that are granted by statute. The

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4 Id. at 2780.
5 Id. at 2778.
7 Rent-A-Center, 130 S. Ct. at 2776.
8 Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991) (“[H]aving made the bargain to arbitrate, the party should be held to it.”).
current judicial approach is to treat arbitration agreements as if they were a topic to be governed solely by contract principles. In contrast, many would argue that mandatory arbitration agreements should be banned outright, i.e., placed outside the scope of contract.9

In this paper, I argue that one option does not have to exist to the exclusion of the other. In fact, under my approach, arbitration agreements should fall somewhere along the middle of this continuum. There is precedent for my approach. There is a particular aspect of the employment relationship that, while open to contract, is still subject to constraints imposed by the law. A noncompete agreement permits an employee to contract with his employer to not work for a competitor following the termination of the employment relationship. This right to contract away the right to compete is, however, narrowly construed by the court system. A court may not enforce a noncompete agreement unless the agreement meets a standard of reasonableness. I propose that this same analysis be applied to arbitration agreements. It is my position that a pre-dispute, mandatory arbitration agreement should not be enforced unless it meets certain requirements that together make the agreement reasonable.

In Part II of this paper, I discuss the problems created by the use of mandatory arbitration clauses in employment agreements. Part III examines the fallacy behind applying general contract principles to arbitration agreements in the employment context. In Part IV, I outline a legislative proposal to constrain the use of arbitration as a means of resolving employment disputes. My proposed legislative solution is designed to address the concerns raised by the continued use of mandatory arbitration clauses in employment agreements.

II. THERE ARE PROBLEMS WITH ARBITRATION CLAUSES IN EMPLOYMENT AGREEMENTS

A. Tension Exists Between the Employment Relationship and Arbitration

A tension exists between mandatory arbitration agreements and employment relationships. The source of the tension lies in the nature of the disputes heard in arbitration. In an ordinary commercial arbitration proceeding, the issues addressed stem from the contract itself. In the arbitration of employment disputes, it is much more likely that the dispute stems from alleged violation of a right granted by statute. Courts have

struggled with this tension. In fact, the Supreme Court, when first facing the question of arbitration of employment rights found that an employee’s agreement to an arbitration process did not waive any rights to pursue statutory claims in court.\textsuperscript{10}

Courts struggled with similar issues in addressing mandatory arbitration in the commercial contracts. Over the years, the mandatory arbitration agreement has gone from pariah to favored status. Prior to passage of the Federal Arbitration Act (FAA) in 1925, the judicial system often exhibited resentment toward arbitration.\textsuperscript{11} The idea of a private court system seemed wrong – how could a judicial system work if the parties were able to contract their way out of it?\textsuperscript{12} In an effort to combat judges’ hostility to arbitration agreements and the resulting privatization of disputes, Congress created a statutory scheme designed to overcome judicial resistance to arbitration.\textsuperscript{13}

The FAA required courts to enforce arbitration agreements—to compel parties to arbitration, where an arbitration agreement existed, and to enforce arbitral awards. The FAA represented the first step to a national policy favoring arbitration.\textsuperscript{14} The drafters of the FAA intended the legislation to put arbitration agreements on the same footing as other contracts.\textsuperscript{15} To that end, section 2 of the FAA, the “primary substantive provision of the Act,”\textsuperscript{16} states that arbitration agreements in contracts involving commerce are “valid, irrevocable, and enforceable.”\textsuperscript{17} Section 2 further requires courts to enforce them according to their terms,\textsuperscript{18} “save upon such grounds as exist under law or in equity for the revocation of any contract.”\textsuperscript{19}

The FAA also made suitable provisions for judicial enforcement of arbitral awards. The FAA permits a party to seek enforcement of arbitration agreements in federal court. The FAA provides that petitions to compel arbitration may be brought before “any United States district court which, save for such agreement, would have jurisdiction under title 28 . . . of the

\textsuperscript{13} Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440, 126 S. Ct. 1204 (2006).
\textsuperscript{15} Marcantel, supra note 12, at 602.
\textsuperscript{17} Validity, Irrevocability, and Enforcement of Agreements to Arbitrate, 9 U.S.C. § 2 (2006).
\textsuperscript{19} 9 U.S.C. § 2.
subject matter of a suit arising out of the controversy between the parties.”

The FAA provided a method for prevailing parties to file a motion for confirmation of the award by a federal court, and an opportunity for judicial review to confirm, vacate, or modify arbitration awards. The FAA forms, for the most part, a single federal law of arbitration and preempts state arbitration laws to the extent those laws conflict with the FAA.

**B. The Attitude Toward Arbitration in Employment Has Changed**

The FAA does not refer to employment agreements or to arbitration in the employment context. Arbitration first entered the employment relationship through the collective bargaining process. The Supreme Court, in *Textile Workers Union v. Lincoln Mills*, stated that federal courts could enforce arbitration clauses contained in collective bargaining agreements. The *Lincoln Mills* decision was not based on interpretation of the FAA. Instead, the Court based its holding on Section 301 of the Labor-Management Relations Act of 1947. The *Lincoln Mills* decision left open the question as to what courts would say about the use of mandatory arbitration agreements in non-union employment relationships.

In 1964, Congress enacted Title VII, which prohibited employment discrimination on the basis of race, color, religion, sex, and national origin. Later federal statutes extended legal protection to age, pregnancy, and disability. These employment rights were gained not through the collective bargaining process, but instead through statute. At the same time state courts proved willing to test the edges of the employment-at-will doctrine. Employers reacted to this new wave of litigation by including in their employment agreements arbitration clauses prescribing mandatory arbitration in the event of a statutory claim.

Initially, the Supreme Court indicated that, outside of collective bargaining, it would not favor waiver of employment rights in an arbitration agreement. In *Alexander v. Gardner-Denver Co.*, the Court found that an employee’s arbitration of a just-cause claim under a labor agreement did not

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20 Id.
23 Id. at 458.
prevent subsequent litigation of the employee’s statutory discrimination claim. In Alexander, the same facts underlay both the plaintiff’s statutory and common law claims. The Court stated that by agreeing to arbitration of contract rights, a party could not waive her right to a judicial forum to hear her statutory claims. “Mere resort to the arbitral forum to enforce contractual rights constitutes no such waiver.”

The Alexander court disagreed with the notion of an arbitration proceeding as a substitute forum for the resolution of statutory employment claims. “We are also unable to accept the proposition that the petitioner waived his cause of action under Title VII . . . we think it clear that there can be no prospective waiver of an employee’s rights under Title VII.” The Court went on to note, “waiver of these rights would defeat the paramount congressional purpose behind Title VII.” The Court distrusted the arbitration process to handle such weighty claims, as it cited “the informality of arbitral procedures, the lack of labor arbitrators’ expertise on issues of substantive law, and the absence of written opinions.”

Thus, in the first test of the arbitration clause in a non-union employment agreement, the Supreme Court found that an arbitration provision could not prevent a plaintiff from asserting his statutory rights. In declining to support the use of the arbitration clause, the Alexander court recognized that an employee making a claim under Title VII has asserted a statutory right separate from the arbitration process. If a decision in arbitration is “based solely upon the arbitrator’s view of the requirements of enacted legislation, rather than on an interpretation of the collective-bargaining agreement, the arbitrator has exceeded the scope of the submission, and the award will not be enforced. Thus the arbitrator has authority to resolve only questions of contractual rights.”

Over time, the Supreme Court’s opinion regarding arbitration changed. In a series of cases the Court altered its opinion of arbitration and “reversed a longstanding presumption that employment claims were exempt from the FAA.” In these cases, referred to now as the Mitsubishi Trilogy, the Court enforced arbitration agreements that extended to antitrust, securities,
and racketeering laws. The Court stated, “we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution.”

But the biggest question remained whether the rights granted under Title VII and other anti-discrimination statutes could be consigned to arbitration. In *Gilmer v. Interstate/Johnson Lane Corp.*, the Court reversed its stance and found that employment disputes arising out of statutory claims were an appropriate area for arbitration. In *Gilmer*, the Supreme Court held that the FAA permitted an employer to require a non-union employee to arbitrate, rather than litigate, a federal age discrimination claim. “By agreeing to arbitrate a statutory 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.” According to the Court, objections of unconscionability and procedural unfairness could be addressed on a case-by-case basis. The Court decided that employment arbitration agreements would be enforced absent “the sort of fraud or overwhelming economic power that would provide grounds for the revocation of any contract.”

Nevertheless, despite the *Gilmer* decision, at least some doubt remained regarding the applicability of the FAA to employment agreements. An argument existed that the text of the FAA itself precluded the application of the statute to employment disputes. The FAA specifically excludes from the Act’s coverage “contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.” Given the historic broad interpretation of ‘interstate commerce,’ presumably most workers would be excluded from the Act’s coverage, if this statement were applied literally.

The Supreme Court confronted this issue in *Circuit City Stores, Inc. v. Adams*, and found that the FAA’s proscription of the Act’s application should be read narrowly. In *Circuit City*, the plaintiff signed an employment agreement containing a mandatory arbitration clause. When an employment dispute arose, the trial court compelled arbitration. The Ninth Circuit overturned, stating that the FAA did not apply to employment disputes. The Supreme Court disagreed. In *Circuit City*, the Court held that the limiting text of the FAA was directed only to transportation workers. For all other employees, claims arising out of statutory violations could be consigned to

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37 *Mitsubishi Motors*, 473 U.S. at 626-27.
39 Id. at 26.
40 Id. at 33
42 Id. at 109 (“We now decide that the better interpretation is to construe the statute, as most of the Courts of Appeals have done, to confine the exemption to transportation workers.”).
arbitration. Following Circuit City, employers could routinely include arbitration clauses in employment agreements subject only to general contract defenses.

C. Arbitration in the Employment Context Must be Carefully Monitored

At this point, one may question why mandatory arbitration in the employment context is a problem. Employees retain their right to general contract defenses—most importantly the defense of unconscionability. Nevertheless, there are a number of policy reasons that support the notion that mandatory arbitration clauses in the employment agreement be limited. Any of these practical issues would justify the decision to limit arbitration of employment disputes.

First, the decision to arbitrate employment disputes is often made on a unilateral basis. No opportunity exists for employees to provide input regarding the functioning of the arbitration process. Instead, employers create arbitration systems “with no employee input, often in secret, and then spring the procedure on employees.”43 Employees are not provided with guidance on arbitration, either the concept or the actual procedure.44 It is highly likely that employees are unfamiliar with the judicial process and are therefore uncertain as to the meaning of selecting arbitration as the final means of dispute resolution.45 Because of this lack of knowledge, the employee “is in no position to bargain or shop for a better term.”46

Agreement to any arbitration proceeding should be knowing and voluntary.47 Voluntariness, however, will likely mean something different in the employment context than in a commercial setting. Some courts have noted that agreements to employment arbitration may often be considered involuntary, because arbitration clauses are included in standard form employment agreements.48 Employees are presented with the agreement on “a take it or leave it, and be fired/not hired, basis.”49 Employees “must either

44 Id. at 174.
46 Id. at 56.
49 Marcantel, supra note 12 at 613.
‘agree’ to waive their right to litigate and use the ... arbitration procedure or lose their jobs.”

Finally, there is a question as to whether private arbitration schemes are equipped to deal with statutory claims. Employment discrimination remains a problem—laws aimed at eliminating employment discrimination have not solved America’s discrimination problems. White women and minorities of both sexes remain not only behind white males, “but have regressed recently in wages, representation in management, and representation in jobs in line for promotion to management.” While equal opportunity in employment may have improved since passage of Title VII, underlying problems remain and the statistics are clear. These statistics cannot simply be explained by facially neutral factors.

Whatever the cause of the continued lag in employment statistics, whether the problem lies with the statute or its enforcement model, mandatory private arbitration, as it is currently practiced, is not the answer. The process of shunting employment discrimination claims off to private arbitration panels, with non-standardized procedures, questions of fairness, questions of due process, and a complete lack of transparency, seems certain to perpetuate the problem of employment discrimination.

III. THE SUPREME COURT ERRED IN RELYING ON CONTRACT PRINCIPLES

A. The Employment Relationship is Unique

The employment relationship represents “one of the most complex and important relationships in modern society.” The employment relationship,

50 Halvordson, supra note 43, at 174.
51 Marcia L. McCormick, The Truth Is Out There: Revamping Federal Antidiscrimination Enforcement for the Twenty-First Century, 30 BERKELEY J. EMP. & LAB. L. 193 (2009). “Black women, for example, earn sixty-three percent of what white men earn, and Latina women earn only fifty-two percent of what white men earn. . . . Additionally, the number of women of all colors in corporate officer posts and in the pipeline for those posts at Fortune 500 companies has fallen in the past two years. Women of color make up just two percent of those corporate officer posts.” Id. at 194.
52 Id. at 194.
53 The continuing problem may be a result of ineffectual enforcement by the Equal Employment Opportunity Commission. Many have criticized the effectiveness of the agency. Perhaps, as some claim, the problem lies with the ability of the EEOC to create accountability on the part of those making employment decisions. “The current model, with the EEOC writing compliance guidelines, encouraging mediation and occasionally acting as prosecutor, is not working.” Id. at 194-95.
like the employment agreement that memorializes it, is almost inherently asymmetrical. The agreement is not the result of a bargain struck between equals. The majority of employees are not able to change any terms of the employment agreement, including the arbitration clause. The employer need not pay any additional consideration for the arbitration agreement; courts routinely construe continued employment as adequate consideration. Employers have sole control of all documents, agreements, policies and other terms of the employment relationship.

In a commercial contract, the parties may agree to arbitrate disputes arising out of the subject matter of the contract. The contract will contain the rights and obligations of the parties, and the arbitration agreement provides the forum that will adjudicate disputes related to those rights and obligations. The employment agreement is different. In the employment agreement, the arbitration clause is “immaterial to the core of the transaction.” While the employment agreement may contain provisions regarding salary and benefits, the employer has likely not insisted on a mandatory arbitration agreement to resolve disputes about salary and benefits. Instead, the employer intends to obtain the employee’s consent to submit future statutory claims to an arbitration proceeding.

Historically, courts have viewed the employment relationship as a matter of contract, a “private economic relationship.” The modern employment agreement is, however, a contract only in the broadest sense of the word. The employment agreement may contain terms and conditions of employment, but those terms and conditions are subject to, and constrained by, external law. The rights and duties of the parties to the employment agreement are much more likely to be defined by statute, or by the common law, than by the employment agreement.

For instance, Title VII and similar antidiscrimination statutes impose severe limitations on employers not only in the making of employment agreements, but in all aspects of employment and employment decisions. But discrimination laws are only one aspect of the extensive regulation of employment by legislation. There are numerous other examples of state

55 Id. at 370.
56 Id.
57 See, e.g., McNaughton v. United Healthcare Servs., Inc., 728 So.2d 592 (Ala. 1998) (“an employer’s providing continued at-will employment is sufficient consideration to make an employee’s promise to his employer binding.”); See also Mattison v. Johnston, 152 Ariz. 109, 112 (Ct. App. 1986) (“the continuation of employment for a substantial period of time establishes consideration”).
58 Fineman, supra note 54, at 380.
59 Schwartz, supra note 45, at 56.
60 McCormick, supra note 51, at 194.
61 Id.
62 Id.
control over the employment relationship. Hours and wages, two of the key elements of any employment relationship, are restricted by statute. An employee may not contract to work for less than the minimum wage, or agree to work overtime without the statutorily mandated pay addendum. The workers’ compensation scheme prohibits negligence suits against one’s employer. Occupational health and safety is a matter of government regulation, not of individual contractual choice. Social Security and federal income tax withholding are matters governed by statute, not by contract. The time and manner of wage payments is subject to state statute, not contract.

B. Arbitration of Employment Disputes Creates Unique Issues

To a large extent, “employment law consists of the competing paradigms of rights and contract.” This conflict between the aspects of employment that are governed by contract and those governed by public law is a constant source of tension. The employment relationship is, in one sense, based in contract: an individual agrees to work for an employer, and certain terms of that work, e.g., salary or benefits, will be dictated by the agreement, whether implicit or express. But the contract relationship occurs within boundaries. Numerous external laws limit the contract relationship. These external laws acknowledge rights and grant entitlements. These laws limiting contract rights within the employment relationship are present for public policy purposes, designed to serve the public interest and values.

In Gilmer, the Court noted that the purpose of the FAA “was to place arbitration agreements on the same footing as other contracts.” In favoring arbitration agreements, the Supreme Court has relied on general contract principles, i.e., because the parties made an agreement to arbitrate, they “should be held to it.” According to this line of thought, parties must arbitrate their employment-related claims because they agreed to arbitrate

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64 See e.g., Ward v. Bechtel Corp., 102 F.3d 199, 203 (5th Cir. 1997) (The Texas Worker’s Compensation Act “provides the exclusive remedy for injuries sustained by an employee in the course of his employment as a result of his employer’s negligence.”).
67 See, e.g., California Labor Code § 207 (2010).
69 Id.
70 Id.
72 Id. at 26 (quoting Mitsubishi Motor Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)).
their claims. But citing traditional contract principles to support arbitration is a disingenuous. As we have seen, the modern employment agreement is only tangentially related to traditional notions of contract. Common law traditions, as well as numerous state and federal statutes bind up the employment agreement. Although employment may be construed as a contractual relationship, the ability of the parties to contract is severely constricted in the employment relationship.

The employment relationship is a hybrid entity, in that current employment law is dictated as much by statute as it is by the terms of the employment agreement. The employment-at-will doctrine provides the foundation for modern employment law. Overlaying the employment-at-will doctrine with rights created a system that is neither contractual nor rights-based.

IV. THE EMPLOYMENT ARBITRATION AGREEMENT SHOULD BE CONSTRAINED

A. Precedent Exists for Limiting the Ability of the Parties to Contract to Arbitration Terms

I propose that the ability of the parties to enter into an arbitration agreement be limited. This is not a revolutionary position, for limiting the ability of the parties to contract to arbitration terms has already occurred. Arbitration terms are currently constrained in three ways: the language of the FAA, state contract law, and by the language of the statute underlying the dispute.

First, the FAA itself limits the effect of the arbitration agreement. While the FAA expressly states that arbitration agreements “shall be valid, irrevocable, and enforceable,” the Act permits courts to modify or vacate arbitration awards. Sections 10 and 11 provide the grounds for vacatur and modification.

Section 10 of the Act permits a court to vacate an arbitration award under certain conditions:

(a) Where the award was procured by corruption, fraud, or undue means;
(b) Where there was evident partiality or corruption by the arbitrators;
(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the
controversy, or of another misbehavior by which the rights of any party have been prejudiced or;

(d) Where the arbitrators exceeded their power or so imperfectly executed them that a mutual, final, and definite award upon the subject matter was not made.73

Under section 11, the grounds for modifying or correcting an award include “evident material miscalculation,” “evident material mistake,” and “imperfect[ions] in [a] matter of form not affecting the merits.”74 Together these provisions protect the parties and provide base line requirements of fairness.75

As noted previously, the FAA also permits arbitration agreements to be challenged upon any basis that would permit a contract to be challenged. Thus, the Act preserves the right of the parties to challenge the arbitration agreement “upon grounds as exist at law or in equity for the revocation of any contract.”76

Finally, there is another limitation on the rights of parties to agree to arbitration terms. The Supreme Court has, indirectly at least, indicated that arbitration terms must meet a certain standard of fairness. In Gilmer, the Court held that a valid arbitration agreement, an agreement that was to decide statutory claims, must permit the plaintiff to “effectively vindicate” his substantive statutory rights.77 Effective vindication would seem to mean that the agreement must maintain the same rights and remedies that substantive law would provide to the plaintiff.78 The parties may waive the forum in which to hear the dispute; they may not waive the substantive law applying to the dispute.79

The changes that I propose are therefore consistent with established law. It is not a question of changing the law regarding the unlimited freedom of employers to demand that their employees agree to arbitrate disputes based on any possible term. Instead, all I suggest is altering the extent to which the law will restrain the parties.

75 See 9 USC §10(a) (containing the grounds for vacatur of arbitration awards).
76 9 USC § 2. Thus, parties may still bring claims based on any ground that would allow a party to challenge a contract. In the arbitration sense, this ground is unconscionability. Parties have often challenged arbitration clauses on the basis of unconscionability, and this was the basis that the plaintiff in Rent-A-Center used.
78 Id.
79 Id.
B. Mandatory Arbitration Does Not Have to be Banned

While I argue for constraint, I do not suggest that arbitration agreements be banned outright. Others would disagree. Many have proposed the absolute elimination of pre-dispute, mandatory arbitration in the employment context.80

[Banning arbitration] rescues public law that has been put at risk by the unchecked growth of mandatory arbitration. It regulates the “wild west” processes creative counsel are designing to manage risk on behalf of their clients. It brings us back from almost two decades of a laissez faire, failed approach to balancing the great value of binding arbitration with the potential for its abuse in the hands of the economically powerful.81

Nor is the movement to prohibit arbitration agreements in the employment relationship merely academic. The proposed federal Arbitration Fairness Act, which first surfaced in 2007, was defeated, and again considered in 2009, prohibited most pre-dispute arbitration agreements between companies and individuals.82 The proposed statute was sweeping, prohibiting the use of arbitration agreements in “employment, consumer or franchise disputes, as well as disputes arising under statutes intended to protect civil rights or to regulate contracts or transactions between parties of unequal bargaining power.”83 In such matters, the parties would be limited to post-dispute arbitration agreements.

Broad proposals that would eliminate all mandatory arbitration agreements are not the solution.84 There is no need to ignore the potential benefits of arbitration. Arbitration has its advantages. Arbitration is meant to remedy a system weighed down with cost and delay, and it may lead to the resolution of claims at lower cost and with greater speed. Litigating a typical employment case can range from $5,000 to more than $200,000, while the average cost of arbitrating an employment dispute is $20,000, including

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80 Bingham, supra note 9.
81 Id. at 2-3.
84 The proposed legislation would invalidate arbitration in many contexts, including presumably disputes in the securities industry. The new law would apply not only prospectively, to end the use of such agreements, following its enactment, but also to "any dispute or claim that arises on or after" the enactment date. Presumably arbitration agreements that have been in place for years, and may have been fairly negotiated, would be rendered unenforceable by the bill. Id.
attorneys’ fees. Furthermore, a typical case that goes to trial lasts for months, and may even go on for years if appealed, while arbitrations can take as little as a few days.\[^85\] The private nature of the arbitration forum might also appeal to employees as well as employers. An employee reluctant to air his grievances in public may prefer a forum that provides protection from public embarrassment. Potential plaintiffs may see some comfort in the privacy protections of the arbitration process.\[^86\]

**C. The Noncompete Agreement is an Example of a Contractual Right that is Limited**

Rather than eliminating pre-dispute arbitration agreements, I propose that the ability of the parties to enter into arbitration agreements be constrained. The law would continue to permit employers to insist on arbitration agreements, but subject to certain limitations. We must develop the means to constrain arbitration agreements in a way that permits the continued use of such agreements, while at the same time addressing the problems caused by the agreements.

These reforms must take place on the federal level. Putting such constraints into law will require Congress to act. It is clear from recent precedent that the Supreme Court is “enamored with arbitration”\[^87\] and is unlikely to tolerate any restriction on the use of arbitration agreements. The Supreme Court has consistently ruled that the FAA preempts state laws that are aimed at arbitration agreements.\[^88\] State legislatures may not act in a way that limits or otherwise restrain agreements to arbitrate. Federal courts have routinely construed the FAA so as to prevent encroachment by state law.\[^89\] Without Congressional action, there is simply no way to change the law of arbitration. It has become clear that “the FAA, as the Supreme Court has interpreted it lately, is the problem and not the solution.”\[^90\]

Fortunately, precedent exists for how the law could address the constraint of contractual rights. Arbitration agreements resemble—in effect if not in form—another type of clause often found in employment agreements. The covenant not to compete, known more familiarly as the noncompete agreement, inhabits a shadow area in the employment

\[^85\] Halvordson, supra note 43, at 178.
\[^86\] See Rutledge, supra note 83, at 267.
\[^87\] Bales, supra note 28, at 1086.
\[^89\] Bales, supra note 28, at 1085; see also Doctor’s Assocs. v. Cassorotto, 517 U.S. 681, 687 (1996) ("Congress precluded states from singling out arbitration provisions for suspect status.").
\[^90\] Bingham, supra note 9, at 1.
relationship, a middle ground between areas governed by contract terms and those areas subject to rights granted by the law. 91

A noncompete agreement is “an agreement, generally part of a contract of employment or a contract to sell a business, in which the covenanntor agrees for a specific period of time and within a particular area to refrain from competition with the covenantee.” 92 The noncompete agreement is known by other names, most notably as a “covenant not-to-compete,” a “restrictive covenant,” or a “non-compete clause.” 93 These terms are interchangeable and all refer to an employment contract or provision purporting to limit an employee’s power upon leaving his or her employment, to compete in the market in which the former employer does business.94

Like arbitration agreements, noncompete agreements are not meant to punish the employee.95 Instead, they are meant to protect the employer from unfair competition.96 Non-compete agreements arguably protect an employer’s customer base, trade secrets, and other information vital to its success. From this perspective, noncompete agreements encourage employers to invest in their employees. An employer does not wish to invest in an employee only to see the employee take the skills acquired, or the company’s customers, to another employer. Logically, the employer will invest more in the employee if measures are in place to guard against the employee’s movement to a competitor.

The non-compete agreement is an example of an agreement that falls somewhere between right and contract. The noncompete agreement resembles a contract—terms dictated by agreement, supported by consideration. But, in fact, the language of the noncompete agreement does not necessarily bind parties. Unless the agreement meets a standard of reasonableness, and is constrained in several important areas, courts will refuse to enforce this “contractual” agreement. The law restricts the scope of the noncompete agreement because society has decided that fundamental issues of fairness are at stake. The issues surrounding the noncompete agreement are so important that it may only be waived under certain conditions.

As with arbitration agreements, Courts traditionally viewed noncompete agreements with disfavor, believing that the agreements contravened public

91 Estlund, supra note 68, at 379.
93 As no substantive difference exists among the names, this article refers to such covenants as “noncompete agreements.”
policy. In time, just as with arbitration agreements, courts grew more accepting of the agreement. Nevertheless, the court system did not embrace the noncompete agreement with the same fervor as it has attached to the mandatory arbitration agreement. Instead, the law continues to restrict the use of noncompete agreements for any purpose other than for legitimate business purposes. To ensure the purpose is legitimate, the law requires that a valid noncompete agreement meet a reasonableness requirement.

The reasonableness requirement for noncompete agreements is designed to balance the interests of all entities affected by the: the employer, the employee, and society as a whole. Each entity has an interest to be protected. The employee wishes to preserve his mobility; the employer wishes to protect itself from unfair competition; and society wishes to balance its interest in employed workers with a system that provides incentives for the development and training of employees. With such varied interests at hand, a noncompete agreement must be drafted in such a way as to satisfy all interested parties.

To satisfy the reasonableness requirement, the law requires that the employer establish a reason for the noncompete agreement other than preventing the employee from competing with his former employer. Moreover, establishing the existence of a legitimate business interest to be protected is merely the threshold step that an employer must meet to create an enforceable agreement. The scope of the noncompete agreement must not be greater than the business interest at stake. Almost all courts apply a similar standard of reasonableness in deciding whether to enforce a noncompete agreement.

98 Id. at 114.
99 See, e.g., Allen, Gibbs, & Houlik v. Ristow, 94 P.3d 724 (Kan. Ct. App. 2004); See also M. Scott McDonald, *Noncompete Contracts: Understanding the Cost of Unpredictability*, 10 TEX. WESLEYAN L. REV. 137 (2003). McDonald notes that among the recognized protectable interests for employers are:

(1) to protect trade secrets and confidential information of the company;
(2) to protect customer goodwill developed for the company (customer relationships);
(3) to protect overall business goodwill and assets that have been sold (noncompetes used in the sale of a business);
(4) to protect unique and specialized training;
(5) for situations in which the employer has contracted for the services of an individual of unique value because of who they are (e.g., performers, professional athletes); and
(6) for pinnacle employees in charge of an organization.
100 McDonald, supra note 99, at 143.
101 Garrison, supra note 97, at 115.
102 Id.
103 Id. at 118.
104 Garrison, supra note 97, at 117-18; Reddy, 298 S.E.2d at 910-11.
A noncompete agreement will be enforceable only “if the restraint imposed is not unreasonable, is founded on a valuable consideration, and is reasonably necessary to protect the interest of the party in whose favor it is imposed, and does not unduly prejudice the interests of the public.”\(^\text{105}\) Many states follow the test set forth in the Restatement (Second) of Contracts, which takes into consideration the following factors: (1) whether the restriction is greater than necessary to protect the business and goodwill of the employer; (2) whether the employer’s need for protection outweighs the economic hardship which the covenant imposes on the departing party; and (3) whether the restriction adversely affects the interests of the public.\(^\text{106}\)

Once a court determines that the noncompete agreement protects a legitimate business interest, it will then examine the agreement to ensure that it does not exceed the minimum restraint necessary to protect that interest.\(^\text{107}\) Courts will enforce agreements only where they are “strictly limited in time and territorial effect and . . . [are] otherwise reasonable considering the business interest of the employer sought to be protected and the effect on the employee.”\(^\text{108}\) To be enforceable, agreements must be reasonable in three ways: scope (referring to the subject matter of the agreement), duration, and geography.\(^\text{109}\)

**D. Arbitration Agreements Should be Restrained by a Reasonableness Standard**

The law restricts contractual freedom for noncompete agreements. Society tolerates contractual restrictions because it recognizes the competing interests involved and attempts to balance them with the reasonableness standard. In a similar vein, the law should recognize competing interests in the use of mandatory arbitration clauses in the employment relationship. Because of the special nature of the employment relationship, society should not permit unlimited contractual freedom in regard to mandatory arbitration.

Currently, the law supports mandatory arbitration agreements. These agreements permit a waiver of rights provided by external law. Following *Rent-A-Center*, the court system has indicated that it is unwilling to examine questions regarding possible unconscionable aspects of the arbitration process, provided that the arbitration agreement assigns those questions to

\(^{105}\) W.R. Grace & Co. v. Mouyal, 422 S.E.2d 529, 531 (Ga. 1992) (quoting Rakestraw v. Lanier, 30 S.E. 735, 738 (Ga. 1898)).

\(^{106}\) Restatement (Second) of Contracts § 188 cmt. a (1979).

\(^{107}\) Garrison, *supra* note 97, at 117.


the arbitrator. Arbitration agreements waive the right to litigate employment claims in court, and it is easy to visualize a process so unfair that it amounts to waiver of the underlying claims.

The solution is to introduce oversight to the arbitration agreement. Oversight could be accomplished by the use of a reasonableness standard. Under my proposal, courts should enforce mandatory arbitration clauses to the extent that the arbitration process is reasonable. Of course, “reasonableness” will require debate and forethought, but I would propose that the reasonableness standard should include the following.

1. The Arbitration Agreement Should Provide for Voluntariness

Arbitration of statutory demands without voluntary consent is not proper. Courts have described voluntariness the “bedrock justification” for the willingness to enforce mandatory arbitration agreements.\(^\text{110}\) Therefore, the proposed reasonableness standard should provide some guarantee that the employee entered into the agreement voluntarily. The voluntariness requirement should not be difficult to meet.

I propose that the arbitration agreement be contained in a separate agreement, or at a minimum, require a separate signature line. This idea of separateness would establish that the arbitration clause that the employee is agreeing to is different from the normal terms and conditions found in an employment agreement. By separating the arbitration clause from the rest of the agreement, employees would have notice that the arbitration agreement should be considered separately from the rest of the document. Agreement to the arbitration clause could potentially have far greater consequences than any other term contained in the agreement, and therefore it is reasonable to insist on separate treatment. A separate document or signature line would provide some objective indications that the arbitration agreement was entered into knowingly and on a voluntary basis.

Alternatively, Congress could enact requirements of voluntariness using the standards found in the Older Workers Benefit Protection Act (OWBPA).\(^\text{111}\) Congress enacted the OWBPA to protect the rights and benefits of older workers.\(^\text{112}\) The OWBPA imposes strict requirements for waivers of ADEA rights and claims.\(^\text{113}\) Under OWBPA, “an employee ‘may not waive’ an ADEA claim unless the employer complies with the statute.”\(^\text{114}\)

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\(^{113}\) 29 U.S.C. §626(f) (2006); see also Oubre, 522 U.S. at 427 (“The OWBPA implements Congress’ policy via a strict, unqualified statutory stricture on waivers”).

\(^{114}\) Oubre, 522 U.S. at 427.
To this end, OWBPA creates a series of prerequisites for ‘knowing and voluntary’ waivers. The eight mandatory elements for a knowing and voluntary waiver of ADEA claims are set forth in the OWBPA.\textsuperscript{115}

2. The Arbitration Agreement Should Provide Guarantees of Due Process and Fairness

The main problem with arbitration process in the employment context is that the process is almost always asymmetrical. The employer is a repeat player, one that will see this particular arbitrator over and over, while the employee is only in it for one. Any proposed standard for reasonableness should include provisions for due process and fairness.

The Constitution guarantees due process. Where the law grants a right, included within that right is the notion of a remedy. The law should provide the opportunity to be heard by an impartial decision maker. This process providing for notice and an opportunity to be heard should be as nonwaivable as the underlying right itself. Otherwise, it would render the underlying right meaningless. Forcing an employee into an unfair arbitration process for a substantive legal claim arguably deprives her of property without due process of law.\textsuperscript{116}

A due process protocol for arbitration must be developed. Fortunately, there have been private attempts to establish such a protocol.\textsuperscript{117} A due process protocol must address certain key areas. First, due process guidelines should provide a guarantee of representation for the employee, or at least the ability to choose a representative. The guidelines would also provide for

\textsuperscript{115} The requirements are as follows:
1. The waiver must be written in plain English so that the employee can understand the agreement;
2. The waiver must specifically mention that the employee is giving up his or her claims under ADEA;
3. The waiver cannot waive rights that arise after date release is signed;
4. The employee must receive consideration of value above anything to which employee is already entitled;
5. The employee must be advised to consult with an attorney;
6. The employee must have at least 21 days to consider agreement;
7. The employee must have 7 days to revoke their acceptance of the agreement.
8. If the termination is part of a reduction in force or voluntary program that affects two or more employees, employee must be given at least 45 days to consider agreement and given a “release attachment” that has a list of those selected for the program (or termination) and those who are not. 29 U.S.C. §626(f)(1).

\textsuperscript{116} Estlund, supra note 68, at 410.

some proportionate sharing of costs associated with the arbitration proceeding, to ensure that employees are not effectively prohibited from having their dispute heard. Another area of tension in the arbitration context is the availability of information sharing. Due process guidelines should provide a cost effective discovery procedure.

Arbitration qualification and selection is another potential topic area for the due process protocol. With quite complicated statutes involved, it will be important that the arbitration process provide for arbitrators who are skilled and knowledgeable. Similarly, selection of an arbitrator or panel will be an issue that should be included within the due process guidelines. Finally, a protocol should govern the arbitrator’s scope of authority.

3. The Arbitration Agreement Should Provide for Openness

The common law system works in large part because it is designed to be flexible, to grow, to adapt to changing society. And the common law is able to do this because there are published decisions that filter throughout society, and the changes, even when not compelled by the power of precedent, have influence on other courts that face similar fact patterns.

A privatized legal system, however, cannot provide the same atmosphere for growth and change. Instead, virtually every decision rendered by an arbitrator is a walled garden, cut off from all but those parties involved in the decision. The American court system was not designed to function in this manner. Surely a system built on closed, opaque models cannot serve society as a whole.

In its protocol describing the essence of a fair and enforceable arbitration agreement, the D.C. Circuit proposed written decisions. My legislative proposal would do the same – require a written decision for any arbitral award.

V. CONCLUSION

The employment agreement is not a contract in the usual sense of the word. Society has limited the ability of the parties to contract by superimposing public law onto the relationship. Therefore, the parties to an employment relationship are constrained in their ability to contract because society has decided that certain issues are too important to leave to the employer and employee.

Mandatory arbitration is one of those important issues. Consigning statutory claims like Title VII to private arbitration carries huge risks. As has been discussed herein, there is a potential for abuse that would make the
statistics meaningless by effectively depriving complainants of their right to litigate the dispute.

Nevertheless, arbitration carries important advantages. It could provide a simpler, less expensive, and more private forum for the resolution of disputes. The challenge that society faces lies in balancing the protections of the law against the advantages of arbitration. To create that balance, I believe that a standard of reasonableness be imposed on arbitration agreements. This standard of reasonableness should protect the interests of all parties: the employer, the employee, and society as a whole.