Is Mandatory Employment Arbitration Living Up to Its Expectations?  
A View From the Employer’s Perspective

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A funny thing is happening to employers on the road to mandatory employment arbitration. Some of them are beginning to wonder if they took the wrong route. As the courts have opened the gates to mandatory employment arbitration, the focus for many employers has shifted away from whether an employer may legally require arbitration of employment disputes to whether it makes good business sense to do so. Many employers are realizing that mandatory arbitration may not be the right path to resolving employment disputes because it may be just as expensive, and take almost as long, as the congested and costly toll road of litigation.

This paper will examine the advantages and disadvantages of mandatory employment arbitration from an employer’s point of view. It will review the arguments, generally from a policy perspective, for and against mandatory employment arbitration, and focus on two key factors in analyzing the relative advantages of mandatory employment arbitration over litigation – the time to resolution of an employment dispute and cost. It will include an analysis of the still somewhat limited data available regarding those two key factors, including new data provided by one major employer. The paper will also examine the impact of a few recent Supreme Court decisions on an employer’s ability to obtain dispositive motion relief in litigation and the difficulties of having an arbitration award reviewed on appeal. The paper will then discuss why voluntary arbitration, as a component of a broader alternative dispute resolution process, may be a better means of resolving employment disputes for employers than mandatory arbitration.

The Legal and Business Environment Regarding Mandatory Employment Arbitration

As several commentators have noted,¹ over the 18 years since the Supreme Court’s decision in Gilmer v. Interstate/Johnson Lane Corp.,² and particularly since its 2001 decision in Circuit City Stores, Inc. v. Adams,³ it has become clear that the law permits employers outside of the transportation industry to require that employees arbitrate employment disputes as long as

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certain due process requirements are met. Lower courts, both federal and state, have increasingly approved mandatory employment arbitration. The Supreme Court reiterated its approval of mandatory arbitration just this past term in 14 *Penn Plaza LLC v. Pyett* by holding that, “a collective-bargaining agreement that clearly and unmistakably requires union members to arbitrate ADEA claims is enforceable as a matter of federal law.”

Given the legal environment permitting employers to require mandatory arbitration of employment disputes, many employers have implemented such programs. A 2008 survey of corporate counsel by Fulbright and Jaworski found that of the 251 participants from the United States, 75 percent had company-required arbitration of employment disputes (non-union setting). Many employers have incorporated mandatory arbitration as part of a broader alternative dispute resolution (“ADR”) process. It is generally acknowledged that most large companies in the United States use some form of ADR to resolve employment disputes.

### Advantages and Disadvantages of Mandatory Employment Arbitration

Employers generally cite several reasons for implementing ADR processes that include mandatory employment arbitration. A non-exhaustive list of the reasons include greater privacy, increased predictability, enhanced settlement potential and possible insurance discounts. The two factors cited perhaps most often by employers in support of mandatory arbitration are that it is less expensive and faster than litigation. These factors are examined more closely below.

There are, of course, several potential disadvantages of mandatory employment arbitration. One disadvantage is employee resistance and skepticism, particularly when a program is in its initial stages. Another disadvantage is that there is some remaining, albeit decreasing, legal uncertainty regarding the implementation and administration of mandatory employment arbitration. More significant disadvantages in the eyes of many employers include the limited ability to obtain summary judgment and other dispositive

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4 See, e.g., Sherwyn, Estreicher and Heise, Assessing the Case for Employment Arbitration, supra note 1, at 1558, n.5.
7 See, e.g., David B. Lipsky, Conflict Resolution and the Transformation of the Social Contract, Presidential Address, Labor and Employment Relations Association, Proceedings of the 59th Annual Meeting (January 5-7, 2007) (“We discovered that virtually every major corporation in the United States now uses ADR to resolve employment disputes…”).
motion relief in arbitration, and the reduced appeal rights and options available in the event of an adverse arbitration award. These disadvantages will be discussed in more detail later in the paper.

Mandatory Employment Arbitration From the Employee’s Perspective

Advocates for employees argue that mandatory arbitration of employment disputes is unfair to the employees for several reasons. They claim that requiring an employee to arbitrate employment disputes constitutes a contract of adhesion that is fundamentally unfair to the employee due to the greater bargaining power of the employer. The courts have generally rejected that argument and held that an employer may require mandatory arbitration of employment claims if the arbitration agreement or program complies with certain procedural requirements that prevent procedural or substantive unconscionability. Some commentators have noted that mandatory employment arbitration is consistent with other aspects of employment over which employees rarely negotiate such as health and life insurance, pension or 401(k) plan provisions, vacation, sick pay, severance and noncompetition agreements that employers typically present to employees on a take-it-or-leave-it basis.

Employee advocates claim the expense of mandatory employment arbitration poses an undue burden on employees. Yet many mandatory arbitration programs do not require the employee to pay any of the arbitrator fees and costs associated with the arbitration, or require only a nominal payment that is generally equal to or less than the filing fee an individual would have to pay if he or she filed a lawsuit in court. The employees generally are required to pay their own attorneys’ fees and other costs in most mandatory arbitration programs, but that would also be the case if the employee attempted to resolve the matter in court.

Employee advocates also contend that some mandatory arbitration programs attempt to limit damages by disallowing certain types of damages or placing caps on damages below those set by statute or applicable case law. Many, if not most, employer programs appear to now allow damages on the same basis as allowed by law. To the extent an employer attempts to limit

11 A discussion of arguments that arbitration does not allow for the development of the law, and it is private and does not provide for public accountability, are beyond the scope of this paper.

12 See, e.g., Gilmer, supra note 2 at 33 (“Mere inequality in bargaining power, however, is not a sufficient reason to hold that arbitration agreements are never enforceable in the employment context.”), but see, Circuit City Stores, Inc. v. Adams, 279 F.3d 889 (9th Cir. 2002)(finding that Circuit City’s Dispute Resolution Agreement was “procedurally unconscionable because it is a contract of adhesion: a standard-form contract, drafted by the party with superior bargaining power, which relegates to the other party the option of either adhering to its terms without modification or rejecting the contract entirely.”).

13 Sherwyn, Estreicher and Heise, Assessing the Case for Employment Arbitration, supra note 1, at 1564.
damages in mandatory arbitration or otherwise limit remedies beyond what is allowed by law, the courts have struck down or severed the unenforceable limitations on remedies. Likewise, to the extent employers have attempted to reduce the period of limitations or otherwise reduce the length of time available to an employee to take any action in connection with an employment claim that the employee would have in the litigation, the courts have disallowed such provisions in the employer’s mandatory arbitration program.

Another argument advanced by critics against mandatory employment arbitration is that employees do not fare as well in arbitration as they do litigation, particularly in front of a jury. A number of studies have analyzed this argument, but given the differences between arbitration and litigation it is difficult to support or refute whether employees have a higher success rate in litigation compared to arbitration.

Those who have examined the success rate of employees in arbitration versus litigation have noted several problems in ensuring the process is a true apples-to-apples comparison. It is extremely rare that the same case is both arbitrated and litigated. Thus, researchers have attempted to compare matters that are as similar to each other as possible but which have proceeded down alternative paths of either arbitration or litigation. Challenges remain in ensuring that the comparison is fair.

One challenge is understanding that in the litigation system cases are routinely dismissed prior to trial by means of a motion for summary judgment or other dispositive motion, but in the arbitration system pre-hearing adjudication is rare. Accordingly, any comparison of win/loss rates at trial versus win/loss rates in arbitration are suspect at best because many of the wins for employers, who file the vast majority of the dispositive motions in employment litigation, are not included in the trial win/loss figure. Some commentators who have studied the issue and who have made a series of assumptions to level the playing field between litigation and arbitration have concluded that plaintiffs (employees) do not fare significantly better in litigation.

A point noted by commentators in comparing the win/loss rates of the parties in litigation versus mandatory arbitration is the fact that many, if not most, employers have policies that include a number of internal steps prior to

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14 See, e.g., Gannon v. Circuit City Stores, Inc., 262 F. 3d 677, 683 (8th Cir. 2001) (arbitration agreement provision limiting remedies can be severed, especially if the arbitration agreement provides specifically for severance of provisions found to be in conflict with applicable law); Paladino v. Avnet Computer Techs., 134 F.3d 1054, 1058 (11th Cir. 1998).
15 See, e.g., Circuit City Stores, Inc. v. Adams, supra note 12 at 894-895.
16 See Sherwyn, Estreicher and Heise, Assessing the Case for Employment Arbitration, supra note 1, at 1564 – 1569, citing a 1994 study of federal courts by Lewis Maltby in which definitive judgments were issued in 3419 cases, of which 60% arose as a result of dispositive motions in which employers prevailed 98% of the time.
17 Id. at 1564.
arbitration. The steps include some type of internal review, such as by Human Resources officials, higher levels of management, an ombudsman and, in some cases, mediation by an outside neutral. These steps perform what has been described as a “filtering” function. One group of commentators has written:

Differences in internal filtering between arbitration and litigation systems likely skew win/loss arbitration results in favor of employers: Employers might use the internal filters to better determine if a case has merit and then to settle the meritorious cases. Therefore, such cases would not be arbitrated.18

The same commentators make the point that because of the likely lower costs of pursuing a claim to arbitration, cases that are arbitrated are likely to have less merit, on average, than cases that are settled.19 Further, an employer with a longstanding program featuring such filtering mechanisms will have a higher win rate than a comparable employer lacking such internal filters.20

Employers Have No Inherent Preference for Arbitration Over Litigation Based on the Fairness of the Decision in Either System

While it would be naive to suggest that some employers do not analyze issues such as whether they have a better chance for success in litigation versus arbitration, that does not appear to be the most important factor for employers in assessing whether they should implement or continue a mandatory employment arbitration program.

I think most employers recognize that any ADR process, including those with mandatory employment arbitration, must be fair and give employees the opportunity to prevail if their case is meritorious. They realize that an ADR process is a means of resolving disputes with their employees or former employees. Employers understand the value in having a system that allows employees to resolve disputes with the employer, both claims that allege violation of the law, and those which do not rise to the level of a claim that could be brought in court.

Employers also understand that if a fair and neutral decision maker determines that the employer was wrong it should be required to provide the employee with an appropriate remedy. I do not believe employers have any particular bias for arbitrators as opposed to juries and/or judges in terms of which makes better decisions. In that sense I think many employers are neutral in their preference for arbitration or litigation.

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18 Id. at 1566.
19 Id.
20 Id.
Employers Are Concerned With the Speed and Cost of Dispute Resolution Systems

Employers are very concerned about the high costs associated with resolving disputes with their employees. The primary costs include the attorneys’ fees and costs associated with resolving a dispute, and paying any judgments or awards that are higher than warranted by the facts of the case at issue.

Employers are also concerned with the time it takes to resolve a dispute. The disposition time impacts the cost of resolving the dispute due to the additional attorneys’ fees that are incurred the longer a matter is litigated or arbitrated and the more back pay damages an employee may accrue. Disposition time also goes to issue of employee morale in the sense that most employees believe that “justice delayed is justice denied.” Ideally employers want the dispute resolution system that best reduces or avoids any unnecessary costs and obtains resolution in the shortest period of time.

Mandatory Employment Arbitration May Not Be Faster and Less Expensive Than Litigation

For many years the conventional wisdom has been that arbitration is a faster and less expensive alternative to litigation in resolving employment disputes. Studies based on limited and relatively old data generally supported the conventional wisdom.21 These assumptions have led many employers to adopt mandatory employment arbitration. Employers have done so with the knowledge that they will rarely be able to obtain summary judgment or other dispositive motion relief in arbitration, and that in most cases arbitration awards are not subject to review on appeal. Employers have balanced the touted advantages of mandatory employment arbitration’s lower cost and faster disposition time, with the prospect of not being able to win on summary judgment or appeal what they consider to be an unfair arbitration award. They have generally come to the conclusion that the cost and speed advantages outweigh the disadvantages of not being able to win on a dispositive motion or appeal an unfair arbitration award.

The conventional wisdom may be changing. Many employers are realizing that the costs of arbitration can be substantial. The data from a recent survey and one company’s own study are instructive. A 2008 survey of senior corporate counsel in the United States found that among the largest companies, 23% spent an average of between $50,000 and $100,000 arbitrating each employment dispute, and 19% spent $100,000 or more per dispute.22

21 See, e.g., id. at 1564 ("We conclude … that arbitration provides a quicker resolution than litigation …"), 1572-1573.
22 See Litigation Trends supra note 6 at 45. The figures for smaller companies were almost one-third spent $50,000 to $100,000 per dispute, and a quarter of them spend more than $100,000. A
A recent review conducted by a major U.S. employer, which has shared its data with the author, suggests that arbitration is just as expensive and actually takes longer to resolve a dispute than does litigation. The employer reviewed 19 single plaintiff employment disputes over a 12-month period during 2006-2007. The employer had an ADR procedure that included two separate lower level reviews of disputes by the company’s Human Resources department, a third level of review by a three member vice-president level board and, if not resolved at that stage, mandatory arbitration. During the period in question, the employer allowed 10 of the 19 plaintiffs to proceed with litigation rather than compelling arbitration.

The total outside counsel fees for the nine cases that were arbitrated was $710,323.50. The total outside counsel fees for the 10 cases that were litigated was $631,443.38. Thus, the average outside counsel fees for the arbitration cases was $78,924.83, and the average for the litigated cases was $63,144.34. The range of the attorneys’ fees for the arbitration cases was $11,462.50 to $283,583.00, and the range for the litigation cases was $5,846.75 to $215,977.70.

When arbitrator and witness fees are added, the totals were $921,422.22 for arbitration, and $704,908.20 for litigation. The total costs, including settlement, were almost identical – $938,509.15 for the arbitration cases compared with $935,086.03 for the litigation cases. Of the nine arbitration cases, five were decided in favor of the employer, two settled and two were pending, compared with three of the litigation cases having been dismissed, two settled and five pending. Thus, the average of the total costs for the arbitration cases divided by the number that were either decided in favor of the employer or settled is $134,072.73, and the average of the total costs for the litigation cases divided by the number that were either dismissed or settled is $187,017.36.

The “lifecycle” or disposition time for the two groups was somewhat surprising. The lifecycle of the average arbitration case was 21 months. The lifecycle of the average litigation case was 19 months.

The survey and study cited above obviously are not sufficient by themselves to definitively conclude that arbitration is as costly or takes as long as litigation. More information is needed. But there seems to be increasing evidence that the assumptions that arbitration is cheaper and faster than litigation may not be correct, or at least that those ostensible advantages may not be as significant as previously believed.

quarter of the mid-sized companies spend $50,000 to $100,000 and 12% average $100,000 or more per dispute.

23 The employer has asked to remain anonymous.

24 It is not clear from the data provided which of the 19 matters were dismissed, settled, or were pending, and therefore we cannot determine the precise averages for each of the categories.
Possible Reasons Why Employment Arbitration Is Taking Longer and Becoming More Expensive

There are several possible explanations for the closing gap between employment arbitration and litigation in terms of disposition time and cost. One possibility is that employment arbitrations have started to mirror employment litigation in terms of increased discovery and motion practice, thus increasing the cost both in terms of attorneys’ fees and arbitrator’s fees. This is in sharp contrast to arbitrations under collective bargaining agreements where, at least in the author’s experience, there is still little or no discovery or other pre-hearing proceedings.

The increase in discovery and pre-hearing motions may be attributable to an increase in the number of attorneys who come from a civil litigation background or who otherwise have little or no experience with traditional labor arbitrations. Traditional labor arbitrations, as noted above, typically have much less discovery and fewer pre-hearing motions. Likewise, many employment arbitrators now come from civil litigation or other backgrounds and, in the author’s experience, tend to treat employment arbitrations more like litigation than would be the case with traditional labor arbitrations.

Another factor may be that employees are more likely to be pro se in employment arbitration than would be the case in either traditional labor arbitration, where a union representative likely would be the advocate for the employee, or litigation where the employee is more likely to have counsel. Arbitrations involving pro se plaintiffs are likely to take longer and therefore be more expensive due to the plaintiff’s inexperience with the process, and the tendency, at least of some arbitrators, to allow in evidence from a pro se plaintiff that would not be allowed in if the party was represented by counsel.

Employers May Want to Reevaluate Mandatory Employment Arbitration

Whatever the reasons may be, any significant increase in the disposition time or cost of arbitration should give employers cause to reconsider whether those advantages are substantial enough to outweigh the employer’s ability to obtain dispositive motion relief in litigation. This procedural advantage of litigation has become even more prominent given the recent Supreme Court decisions in *Bell Atlantic v. Twombly* 25 and *Ashcroft v. Iqbal*. 26 Many commentators have cited those cases for the proposition that it is much easier for a federal judge to dismiss a complaint in the initial stages of the lawsuit when the complaint fails to include specific factual allegations on each element of each

A frequently quoted article indicated that in just the few months since the *Iqbal* decision it was cited over 500 times by federal judges. Employers may view these decisions as an opportunity to dismiss unmeritorious claims at the earliest stages of litigation and thereby substantially decrease the disposition time and cost of resolving the matter.

Perhaps more importantly, the employer must analyze whether the cost and speed advantages of arbitration remain sufficient to outweigh the inability of an employer to appeal an outrageous or simply unfair arbitration decision and award. Litigators know that judges and juries sometimes render decisions that the losing party does not agree with (sometimes even the winning party does not agree with the decision, particularly as to the amount of damages). The losing party, and sometimes the winning party, has the right to have the decision reviewed by an appellate court. Employers understand that if a judge or a “runaway jury” decides a case in a manner that exceeds what the law permits they will have a good chance of having the judgment reduced or reversed on appeal. Litigators also know that is almost never the case in an arbitration.

Under the Federal Arbitration Act (FAA), the scope of judicial review of an arbitration award is extremely narrow. Many, perhaps most, employers have adopted the FAA in connection with their employment arbitration agreements. Under the FAA an arbitrator’s mistake, even a mistake of law, is not a sufficient ground to invoke judicial review. As the Supreme Court recently held in *Hall Street Associates, LLC v. Mattel, Inc.* a mistake of law is not enough. Further, the Court in *Hall Street* held that the parties may not by contract expand the scope of judicial review of an arbitration award beyond the grounds identified in the FAA.

The inability to appeal an arbitrator’s decision can be critical, particularly if the amount of the award is large. Recently a California arbitrator issued an award against iFreedom Communications International Holdings Limited, and its founder, Timothy Ringgenberg, for over $4 billion, including almost $3 billion in punitive damages. The award was confirmed by the California Superior Court and judgment was entered against the defendants.

Given these developments, employers may decide that litigation is the better means of resolving employment disputes. Each company must weigh the

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27 See e.g., Lawrence W. Marquess and Jeff Timermann, Tightened Federal Pleading Rules Take Effect: Three Months After the U.S. Supreme Court’s *Iqbal* Decision, Littler Mendelson Insights (August 2009).
31 Id. at 1405.
32 Id. at 1400.
pros and cons of any time and cost advantage of mandatory arbitration over litigation. Such an analysis should consider the new legal standards that may make motions to dismiss and other dispositive motions more likely to be granted and the inability to appeal an adverse arbitration award.

**Raytheon’s Experience**

Raytheon changed its policy in 2006 and went from mandatory to voluntary arbitration of employment disputes. Raytheon still offers employees the opportunity to resolve employment disputes internally through a management review process and external mediation.

Raytheon has been very successful in resolving employment disputes over the six years since we began our ADR program. Over 90% of our ADR complaints end at the management response level (Step 2 of our four-step process). Many of these matters would not be eligible for mediation or arbitration, the third and fourth steps of our process, because they do not include claims that involve violations of law (e.g., a dispute over an employment appraisal rating that does not involve any allegation of discrimination). We have also been successful in resolving the remaining 10% of the ADR complaints at mediation – almost 2/3 (64%) of the cases submitted to mediation result in a settlement. Of the 508 ADR complaints filed over the life of our program, we have had only five cases go to arbitration.

In those cases where an employee has a legal claim and is not satisfied with the result of the management review or external mediation, the employee and Raytheon still have the opportunity to voluntarily agree to binding arbitration. However, the parties retain the right to have the courts resolve the dispute.

**Conclusion**

While employers with ADR policies and procedures may find it beneficial to maintain them, they also may want to revisit whether mandatory employment arbitration is the best final step in their ADR process. The speed and cost advantages of arbitration over litigation may not be as great as previously thought. With the Supreme Court’s recent decisions in *Twombly* and *Iqbal*, lower courts may grant employers’ motions to dismiss at a much higher rate than in the past. This would decrease the disposition time and reduce the cost of litigation as a means of resolving employment disputes. Finally, employers which continue to utilize mandatory employment arbitration must be willing to live with an undesirable arbitration award and forgo any rights they have to appeal, as opposed to the full appellate review available if they receive an adverse litigation judgment.