

## LABOR & EMPLOYMENT LAW ALERT

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### Courts Issue Decisions On Several Important Arbitrations

**During the last month, courts have ruled in several important cases on issues involving the rights of each of the parties in arbitration.**

The United States Supreme Court issued a very important decision on who decides whether a dispute is arbitrable, a court or the arbitrator. A Third Circuit Court of Appeals decision presented a textbook case on how to draft an unconscionable arbitration agreement and waive your right to enforce that agreement, in one fell swoop. A New Jersey Supreme Court ruling provided a wonderful

example of exactly how much authority an arbitrator can have when an employer fails to define crucial terms in a contract, like “just cause.” Each of these cases should be read with care; they provide important lessons in drafting and enforcing arbitration agreements.



### U.S. Supreme Court Holds That Arbitrators Have The Authority To Rule On Challenges To Enforceability Of An Arbitration Agreement As A Whole

**Over the last several years, courts have struggled with who decides whether a dispute is subject to a mandatory arbitration agreement, the courts or the arbitrators.** This question is important, especially since the answer will sometimes determine who wins the underlying dispute. In late June, the Supreme Court held that under the Federal Arbitration Act (“FAA”), where an arbitration agreement includes a **provision** that the arbitrator will determine the enforceability of the agreement, and a party to that agreement specifically challenges the enforceability of that **provision**, a district court

will consider the challenge, but if a party challenges the enforceability of the agreement **as a whole**, the **arbitrator** will consider the challenge. *Rent-A-Center, West, Inc. v. Jackson*, No. 09-497 (June 21, 2010).

In *Rent-A-Center*, an employee who had signed an arbitration agreement with a provision to arbitrate all disputes filed a discrimination lawsuit. The employer sought to enforce the arbitration agreement. When the employee contended the agreement was unconscionable, the employer argued that, according to a provision in the agreement, only the arbitrator could determine the agreement’s validity. The district court agreed, ruling an arbitrator had the authority to rule on the agreement’s enforceability and on the question of arbitrability. The Ninth Circuit reversed, finding that even though the agreement left to the arbitrator the power to determine its

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validity, the issue of unconscionability is for the court to determine. The Supreme Court reversed for two relevant provisions of the agreement: the first, requiring arbitration of all disputes arising out of an employee’s employment, including discrimination claims; and the second, giving the “Arbitrator...exclusive authority to resolve any dispute relating to the [Agreement’s] enforceability...including...any claim that all or any part of this Agreement is void or voidable.” The Court found the second provision enforceable under Section 2 of the FAA because the agreement to arbitrate enforceability was severable from the rest of the arbitration

agreement and the employee did not challenge the delegation provision, specifically, so it must be treated as valid under Section 2 and enforced.

**The Bottom Line:** Employers should revise their agreements to include a provision that the arbitrator shall decide issues regarding the enforceability of the agreement as a whole. This provision will dramatically improve the odds that an arbitration agreement will be enforced. Please call us if we can be of help.

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## **Third Circuit Steps In To Preclude Arbitration Where There Are Unconscionable Terms and Waiver**

**Of course, *Rent-A-Center* should not be read to mean that the issue of unconscionability will always be decided by an arbitrator.** Sometimes, an arbitration agreement can be so “one-sided” that a court will step in to prevent arbitration.

In *Nino v. The Jewelry Exchange, Inc.*, No. 09-1268 2010 U.S. App. LEXIS (3d Cir. June 15, 2010), the Court reversed a district court decision to dismiss a sex and national origin bias claim in favor of arbitration where it found the agreement infected with “pervasive one-sidedness.” It held that the district court should not have severed the unconscionable provisions from the remainder of the agreement, and should not have enforced arbitration where the employer had engaged in protracted litigation, including discovery and depositions, before seeking arbitration.

In this case, the district court decided that several provisions in the agreement were unconscionable. **First**, it found the agreement procedurally unconscionable, noting that the employee depended on the employer as to his immigration status and his right to work in St. Thomas, to which location the employer had just transferred him. **Second**, the agreement was presented on a take-it-or-leave-it basis, and there was disparity of bargaining power between the single retail employee and his multinational employer. **Third**, the limitations period of the arbitration agreement was substantively unconscionable because: (i) it required that an employee file a grievance within five days (too small a window); and (ii) it could not be waived except by agreement of both parties; and no notice requirement was imposed on the employer. **Fourth**, it was unconscionable that the parties bear their own attorney’s fees, costs and expenses because it “work[ed] to ‘the disadvantage of an employee needing to obtain legal assistance,’” and “undermine[d] the legislative intent behind fee-

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shifting statutes like Title VII.” **Fifth**, a provision that permitted the employer to strike two of a panel of potential arbitrators while the employee was permitted only one strike was further evidence of unconscionability.

The Third Circuit agreed with the district court’s determinations of unconscionability, but disagreed with its conclusion that improper provisions could be severed from the arbitration agreement. The Circuit Court observed that a court should decline to enforce an agreement in its entirety when “the agreement demonstrates that the employer sought to impose arbitration on the employee, an inferior, one-sided forum that worked to the employer’s advantage.” In this instance, the “one-sided nature of the arbitration agreement reveals unmistakably that [the employer] ‘was not seeking a *bona fide* mechanism for dispute resolution, but rather sought to impose a scheme that it knew or should have known would provide it with an impermissible advantage.’ ” The “only conceivable purpose” behind the agreement’s one-sided provisions, the Circuit concluded, was “to stack the deck in [the employer’s] favor,” rendering severance of the unconscionable terms inappropriate.

In *Nino*, the Third Circuit also reversed the district court’s finding that the employer had not waived its right to compel arbitration after litigating the case for 15 months. Relying on factors for deciding waiver set out in an earlier case, *Hoxworth v. Blinder, Robinson & Co., Inc.*, 980 F.2d 912 (3d Cir. 1992), the Court had found several factors favoring waiver: (i) the employer waited 15 months to move to compel arbitration; (ii) the employee was required to file three motions to compel discovery against the employer; (iii) the employer, despite attending at

least 10 pre-trial conferences, never raised the issue of arbitration; and (iv) substantial discovery had been conducted, including interrogatories, disclosures, document production, and depositions. Although the employer had listed arbitration as an affirmative defense in its Answer, the court held that “the significance of this factor diminished, the longer [the employer] litigated this case without raising the prospect of arbitration.”

**The Bottom Line:** The *Nino* case teaches numerous lessons for, while the courts generally favor arbitration, its favored status is not without limitation. If you have an arbitration agreement, you should make sure it is not so one-sided as to be judged unfair. Limitation periods and potential damages should be co-extensive with applicable state and federal discrimination laws. Arbitrators should be chosen through a neutral agency, like the American Arbitration Association or the Federal Mediation and Conciliation Service. Costs should be allocated fairly so that employees are not deterred from filing for arbitration. Care should be exercised in the manner and timing of presenting the agreement; in *Nino*, the employer presented the agreement only after relocating the employee who was then in no position to reject it. Finally, and very importantly, if an employee subject to an arbitration agreement files a lawsuit, the time to seek its enforcement and compel arbitration is at the beginning of the process, not after substantial time spent in litigation. *Nino* is a very important case that every employer using arbitration agreements should study.

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## Parties Who Fail To Define “Just Cause” For Discharge Leave It To The Arbitrator

**Labor agreements frequently provide that an employer may discharge an employee only for “just cause.”** What happens when the term is not adequately defined? If the dispute goes to arbitration, the definition will be left to the arbitrator. That is the holding of the New Jersey Supreme Court, in *Linden Board of Education v. Linden Education Association on behalf of John Mizichko*, Docket No. A-17-09 (N.J. June 8, 2010).

In *Linden*, the Linden Education Association filed a grievance on behalf of a custodian who was fired for working in a room where female students were undressing. The labor agreement required that grievances be resolved through binding arbitration and stated that an employee with contractual tenure, such as a custodian, “shall not be disciplined, discharged or not reappointed without just cause.” There was no definition of “just cause” in the agreement. When the Parties went to arbitration, they framed the question for the arbitrator as follows: “Did the Board of Education have just cause to terminate the employment of [the custodian]? And, if not, what shall be the remedy?” After the hearing, the arbitrator determined that the custodian was motivated by a desire to get his work done, but knew about the rule, and the possible consequences of violating it. Therefore, there was just cause to impose discipline. Concluding that progressive/corrective discipline was an integral part of the just cause concept, the arbitrator imposed a ten-day suspension without pay after noting that this was the custodian’s first offense and finding that termination was disproportionate to the gravity of the misconduct.

The Board filed a complaint to vacate the award in the Superior Court. That court confirmed the award and concluded that the arbitrator did not exceed his authority by imposing a lesser penalty. The Appellate Division reversed the trial court’s judgment, holding that the arbitrator, having found that the employee violated the rules, had no authority to consider other remedies. The Association appealed to the New Jersey Supreme Court, where the decision was reversed.

According to the New Jersey Supreme Court, the parties got what they bargained for: a contractual interpretation of the labor agreement by the arbitrator. Even if the arbitrator got it wrong, judicial review is extremely limited and an award will be upheld so long as the result is reasonably debatable. Besides, it held a standard of just cause may be imposed upon disciplinary actions even if such a standard is not spelled out in the agreement. Under the New Jersey Arbitration Act, N.J.S.A. 2A:24-1 to -11, a reviewing court may vacate an award only if it was procured by fraud or undue means, there was partiality or corruption in the arbitrators, the arbitrators were guilty of misconduct prejudicial to the rights of any party, or the arbitrators exceeded or so imperfectly executed their powers that a mutual, final and definite award was not made.

In the *Linden* case, the die was cast when the parties framed the submission to the arbitrator as “Did the Board of Education have just cause to terminate the employment of [custodian]? And, if not, what shall be the remedy?” According to the New Jersey Supreme Court, the questions implied that a remedy other than termination would be

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appropriate, because if the arbitrator did not find just cause to terminate, the parties asked him to both fashion and impose an appropriate remedy.

The Agreement in *Linden* did not define “just cause” and there was nothing in the questions submitted that limited the power of the arbitrator to fill in the gap, giving meaning to that term. The arbitrator did so. He first explained that, in general, just cause requires that, before an employee is disciplined, he should know of the existence of a pertinent rule and that this rule is reasonably related to the business of the employer, and the possible consequence of a violation. Although the arbitrator found just cause for discipline, he also concluded that the facts were insufficient to justify a finding of just cause that would result in termination. The arbitrator declared that when termination is imposed, just cause “requires that the penalty

not be disproportionate given the totality of the circumstances, including mitigating factors[.]” and “the Board has not proven that termination of [custodian’s] employment is appropriate.”

**The Bottom Line:** The Court’s decision in *Linden* is applicable both to labor contracts and individual employment agreements. There are two important lessons from the case. **First**, when drafting the agreement, care should be taken to define “just cause” in as much detail as necessary. Where possible, the agreement should specifically indicate that a violation of a particular rule will result in discharge, rather than that a violation “will result in discipline up to and including discharge.” **Second**, when framing the submission to the arbitrator, the agreement should attempt to limit or foreclose the arbitrator’s authority to modify the discipline imposed.

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## District Court Refuses To Vacate Arbitration Award Where Grievant Fails To Produce Evidence

**The United States District Court for the District of New Jersey just issued another decision showing exactly how difficult it is to vacate an arbitration award.** In *International Brotherhood of Teamsters, Local 701 v. CBF Trucking*, Docket No. 09-5525 (D.N.J. June 9, 2010), a federal district court judge denied an employer’s cross-motion to vacate an arbitration award, rejecting the employer’s argument that the grievant’s failure to produce tapes bearing on his inconsistent accounts of events leading to his discharge deprived the employer of a fair hearing in arbitration. The grievant, a mail carrier for a U.S. Postal Service contractor, was terminated

for failing to complete one of his runs. At arbitration, the grievant alleged, for the first time, that a security guard had told him he did not have to complete the run. The arbitrator, noting that the employer failed to refute the grievant’s contention at arbitration, ordered the grievant’s reinstatement. The Union moved the District Court to enforce the award. The employer moved to vacate, arguing that the grievant should have produced tapes he had made that showed him insisting that he had made all his runs, contrary to his arbitration testimony.

As with *Linden*, the District Court correctly pointed out that it could not vacate the award unless the employer could prove that the award was infected with fraud or undue means, evident partiality, or corruption in the arbitrators, or the arbitrator was guilty of misconduct prejudicial

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to the rights of any party. The Court found that the grievant's failure to disclose the tapes was not fraud that deprived the employer of a fair hearing, especially since the employer already knew of the grievant's prior insistence that he made all his runs. The Third Circuit has held that an arbitrator's failure to hear relevant evidence is insufficient grounds on which to vacate an arbitration award where the party is not prejudiced or denied a fair hearing. *See Century Indemnity Co. v. Certain Underwriters at Lloyd's, London*, 584 F.3d 513, 557 (3d Cir. 2009). Further, the arbitrator's award had noted the

grievant's inconsistency. The tapes were not new evidence that would have swayed the arbitrator.

**The Bottom Line:** This case reemphasizes the difficulty of vacating arbitration awards. Arbitration demands commitment and preparation. While arbitration may be less costly and time consuming than a trial, the downside is that the ability to appeal an award successfully is extremely limited. This limitation must be considered when you prepare for and try your case.

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## Elevator Repair Firm Not Required To Arbitrate Where It Is Not A Successor Business

**Quite often, a union who is party to a labor agreement with one company will try and bind another company to that agreement by claiming the second company is a “successor business,” a “single employer,” or an “alter ego,” or some other corporate configuration.**

The attempt to bind the second company is part of a larger attempt to burden it with liability for unpaid wages or benefit contributions.

In *Century Vertical Systems Inc. v. Local 1, International Union of Elevator Constructors*, No. 09-CV-4257 (2d Cir. May 28, 2010), a union party to a contract with Century Industrial Services, Inc. demanded arbitration with Century Vertical System Inc., d/b/a PRO Elevator, over a dispute involving allegedly late wage rates and fringe benefit contributions. Vertical filed a lawsuit seeking a stay of arbitration, but the District Court found that Vertical was a

successor business to Century Industrial Services, Inc., and as such, was required to arbitrate under Industrial's collective bargaining agreement with Local 1. As the lower court explained, a “successor employer” can be bound by an arbitration provision contained in a labor agreement entered into by the predecessor employer where: (1) the contracting employer disappears into another by merger, (2) the successor company expressly or impliedly assumes the labor agreement, or (3) the successor employer is an alter ego of the predecessor employer.

The facts are these: after the owner of Industrial decided to give up the business, two of his employees took over the business and formed a new company. Vertical retained the same location and phone number as Industrial, which eventually filed for bankruptcy, and ultimately hired four out of fourteen Industrial employees. Subsequently Local 1 demanded that Vertical submit to arbitration as stipulated by its “Joinder Agreement” with Industrial over

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wage and fringe benefit contributions. Based on these facts, the Second Circuit Court of Appeals reversed, holding that Vertical was not a “successor business” and was therefore not required to arbitrate with the Elevator Constructors’ union over a wage and benefit dispute.

In reversing, the Second Circuit found that there was no continuity of identity in the workforces of the two companies and that the lower court erred in “entirely discounting the lack of overlap” in the companies’ workforces, focusing on the

fact that only four of 14 Vertical field employees had any prior association with Industrial.

Moreover, there was no evidence that Vertical assumed any of Industrial’s obligations. The court held that because there was no substantial continuity of identity in the work force hired by Vertical with that of Industrial’s, and because Vertical did not assume any obligations under the collective bargaining agreement through a merger or as an alter ego of Industrial, there was no basis in law or fact to conclude that Vertical was bound by the collective bargaining agreement’s arbitration provision.

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## Upcoming Speaking Engagements:

**July 29, 2010:** Litigating the Employment Discrimination Case. Sponsored by the New Jersey Bar Association, Labor and Employment Section. *Fairfield, NJ.*

**August 6, 2010:** Unemployment Insurance 101: Understanding and Assessing U.I. Liabilities and Costs. Sponsored by Lorman Educational Services. *New Brunswick, NJ.*

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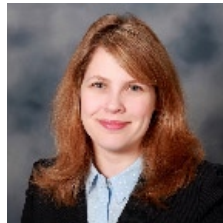
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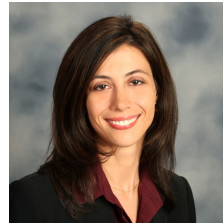
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