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ALERT

May 2010

MANDATORY ARBITRATION PROVISIONS IN EMPLOYMENT AGREEMENTS MAY BE INVALIDATED BY A COURT IF NOT PROPERLY DRAFTED

The New York State Court of Appeals and the Federal Second Circuit Court of Appeals each issued a decision recently, providing guidance as to which terms in a mandatory arbitration clause contained in an employment agreement might well be deemed unconscionable, thereby rendering the arbitration clause unenforceable. The Federal Court also addressed whether a non-signatory to an employment agreement containing an arbitration clause can compel a signatory to that agreement to arbitrate claims arising thereunder. These decisions also provide guidance more generally on the use of arbitration provisions in contracts, loans and other business arrangements.

In *Ragone v. Atlantic Video at the Manhattan Center*, which was decided by the Second Circuit Court of Appeals, the plaintiff/employee had been employed as a make-up artist by AVI, pursuant to a written employment agreement, and she worked for both AVI and its client, ESPN. The plaintiff/employee commenced a lawsuit against AVI and ESPN claiming that she had been sexually harassed. At issue in *Ragone* was whether the mandatory arbitration provision in her employment agreement was unconscionable and therefore unenforceable, and whether ESPN could compel plaintiff/employee to arbitrate her claim against ESPN, based on her employment agreement with AVI.

The plaintiff/employee argued that the mandatory arbitration provision was unconscionable because it: (i) shortened the statute of limitations period in which she could file a demand for arbitration; (ii) awarded attorneys' fees to the prevailing party; (iii) prevented her from appealing the arbitrator's award in court; and (iv) limited her discovery rights and right to a jury trial. However, after commencement of the action, AVI waived the statute of limitations and fee-shifting provisions.

The Court held that in light of the waiver, the mandatory arbitration provision was not unconscionable, and therefore was enforceable. However, the Court emphasized that it did so "with something less than robust enthusiasm" and that "had the defendants attempted to enforce the arbitration agreement as originally written it is not clear that we would hold in their favor".

The Court also held that petitioner/employee was required to arbitrate her claims against ESPN, stating: "[u]nder the principles of estoppel, a non-signatory to an arbitration agreement may compel a signatory to that agreement to arbitrate a dispute where a careful review 'of the relationship among the parties, the contracts they signed…, and the issues that had arisen' among them discloses that 'the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed.'"

The issue facing the New York Court of Appeals in *Brady v. Williams Capital Group, L.P.* was whether the petitioner/employee had met her burden of demonstrating that an arbitration agreement's provision for the equal sharing of arbitration fees and costs (which would have required the petitioner/employee to pay approximately $21,500.00 in up front fees) precluded petitioner/employee from pursuing her statutory rights in the arbitral forum. The New York Court of Appeals held that enforceability of an arbitration agreement's fee-sharing provision is dependent on the employee's financial ability to share arbitration fees and costs, and should be determined on a case-by-case basis. According to the Court, the inquiry should at a minimum consider the following questions: "(1) whether the litigant can pay the arbitration fees and costs; (2) what is the expected cost differential between arbitration and litigation in court; and (3) whether the cost differential is so substantial as to deter the bringing of claims in the arbitral forum." Consequently, the Court remitted this matter to a lower court for a hearing to determine whether the petitioner/employee was financially able to share the arbitrator's fees and costs.

As the above cases show, it is imperative that when drafting mandatory arbitration provisions in employment agreements, a party obtain proper representation to guide it through the nuances of the applicable law, thereby maximizing protection and the employment agreement's enforceability. Proper counseling can assist with the preparation of employment agreements, and help each client weigh the benefits and risks associated with each provision. For example, as illustrated in the cases referenced above, certain terms can be deemed by a court to be too onerous and result in the invalidation of a mandatory arbitration provision.

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We can assist you in preparing employment agreements and in reviewing your existing agreements to determine if they comply with this type of provision. We can also discuss with you other provisions that can provide further protection for your company.

Moritt Hock Hamroff & Horowitz LLP is a broad based commercial law firm with 42 lawyers and a staff of paralegals. The firm has experience in commercial foreclosure; construction law; corporate, securities & financial services; creditors' rights & bankruptcy; employment & labor law; equipment & vehicle leasing; healthcare law; intellectual property, unfair competition & licensing; litigation; marketing & advertising law; not-for-profit law; real estate law; tax; and trusts & estates.

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