

First Wednesday

by Jeffrey A. Snyder and Erin L. McDermit

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Jeff and Erin are lawyers with Thoits, Love, Hershberger and McLean, specializing in employment law and related litigation.

They can be reached at:
(650) 327-4200 – Phone
(650) 325-5572 – Fax
jsnyder@thoits.com
emcdermit@thoits.com

[Employment Law Group:](#)
Jeffrey A. Snyder
Erin L. McDermit
Anne E. Senti-Willis
Stephen C. Gerrish

Employment Arbitration is Dealt a Heavy Blow by the California Supreme Court

A closely-divided California Supreme Court dealt employment arbitrations a potentially huge setback last month. In a 4-3 decision, the court held that an arbitrator's legal error warranted vacating an arbitration award where the error deprived an employee of his right to a hearing on the merits of his claim arising under California's Fair Employment and Housing Act ("FEHA").

The court attempted to limit its holding to the "particular circumstances of this case," but the potential expansion of this ruling to future cases is clear. Arbitration awards, even where the arbitrator gets it wrong, are supposed to be final and binding, as announced in the leading case of *Moncharsh v. Heily & Blase* (1992) 3 Cal.4th 1, nearly 20 years ago. The new case that changes the landscape is *Pearson Dental Supplies, Inc. v. Superior Court (Turcios)* (2010 Cal. LEXIS 3685), available [here](#).

The Facts

The plaintiff, Luis Turcios, was hired as a janitor by defendant Pearson Dental Supplies, Inc., in February 1999. He was terminated on January 31, 2006, at the age of 67. He filed an administrative complaint with the Department of Fair Employment and Housing ("DFEH") on April 5, 2006, claiming age discrimination. Nine days later, the DFEH issued a right to sue letter. On October 2, 2006, still within one year of being terminated, Turcios filed a lawsuit in Los Angeles Superior Court alleging age discrimination and wrongful termination against Pearson.

In March 2007, Pearson filed a motion to compel arbitration. Pearson claimed that the parties were bound to arbitrate any disputes by virtue of an employment arbitration agreement signed by Turcios while working at Pearson. The agreement stated that any dispute must be submitted to binding arbitration within one year from the date the dispute arose and, if not submitted to arbitration within one year, the claim would be void and considered waived to the fullest extent allowed by law.

The court granted Pearson's motion to compel arbitration. The parties then selected an arbitrator to conduct binding arbitration. Pearson filed a motion for summary judgment with the arbitrator, contending that Turcios's claims were time-barred because they had not been submitted to arbitration within one year after plaintiff's termination on January 31, 2006. The arbitrator, in a brief letter ruling, held in favor of Pearson and dismissed the claims as time-barred. Turcios, therefore, never got a full hearing on his claims – in arbitration or in court.

The California Supreme Court Acts to Protect Turcios's Right to a Full Hearing

The California Supreme Court, however, granted him relief. Four of the seven justices were persuaded that the arbitrator had made a clear error of law in ruling that Turcios's filing of a claim in Superior Court within one year of being fired did not satisfy the arbitration agreement's mandate that arbitrations be filed within one year of the dispute. The court held for Turcios despite the usual rule that the arbitrator's legal error is not a basis for vacating the arbitrator's award.

By signing an arbitration agreement, the parties generally take the risk of arbitral error in return for a quick, inexpensive and conclusive resolution to their dispute. Ever since *Moncharsh*, practitioners have understood that arbitrators are not necessarily bound to follow the law and may base their decisions upon broad principles of justice and equity. The California Supreme Court has now backed off of its decision in *Moncharsh*, at least in cases involving claims arising under the Fair Employment and Housing Act, and quite possibly, by extension, claims arising under the California Labor Code as well.

The Facts Make the Law

It is often said that "bad facts make bad law." The *Pearson* case has a few unique facts that may have led to a result that will indeed be "limited to the particular circumstances of this case," as the court said in its introduction. However, consider the potential breadth of the following holding in the case. According to the court:

"We therefore hold that when, as here, an employee subject to a mandatory employment arbitration agreement is unable to obtain a hearing on the merits of his FEHA claims, or claims based on other unwaivable statutory rights, because of an arbitration award based on legal error, the trial court does not err in vacating the award. Stated in other terms, construing the CAA [California Arbitration Act] in light of the Legislature's intent that employees be able to enforce their right to be free of unlawful discrimination under FEHA, an arbitrator whose legal error has barred an employee subject to a mandatory arbitration agreement from obtaining a hearing on the merits of a claim based on such right has exceeded his or her powers within the meaning of Code of Civil Procedure section 1286.2, subdivision (a)(4), and the arbitrator's

award may properly be vacated. (See *Armendariz, supra*, 24 Cal.4th at pages 106-107.)"

It is not difficult to imagine that many employees unsatisfied with arbitration results can point to a "legal error," and that the Turcios argument will be made any time a FEHA-based claim, or a wage and hour claim, does not go to a full hearing on the merits but is dismissed on a pre-hearing motion or demurrer.

As noted above, three justices, led by Justice Baxter, filed a dissenting opinion. The dissenting justices found that the effect of the court's holding is to frustrate the parties' contractual expectations and will tend to defeat the strong public policy favoring arbitration and, in particular, arbitral finality.

Takeaways From the Pearson Case

Here are a few important takeaways that could have changed the result. First, Pearson's attorney, for whatever reason, did not raise the issue of the arbitration clause until over one year had passed since Turcios was fired. Recall that Turcios sued the company in October 2006, just eight months after being fired. The company participated in litigation with him but then in February 2007, over one year after his termination, Pearson's counsel told the court, for the first time, there was an arbitration agreement in plaintiff's personnel file, and that this was something he "would have to explore." Thus, the California Supreme Court may have been swayed by the fact that Turcios was led down a garden path, thinking that the company would not insist on arbitrating but preferred to keep the case in court.

The other fact that may have influenced the result was that the arbitrator only filed a brief letter ruling dismissing Turcios's claim. The statute that might have saved his claim, Code of Civil Procedure section 1281.12, was not addressed fully in that letter. The *Pearson* majority opinion made note of the fact that the well-known employment arbitration case of *Armendariz v. Foundation Health Psychcare Services, Inc.* ((2000) 24 Cal.4th 83) requires a sufficient written arbitration decision to allow some minimal level of judicial review of an arbitration award concerning statutory FEHA rights. Practitioners and arbitrators can, therefore, take from this case that any pre-hearing ruling in an employment case, such as on a demurrer or summary judgment motion, should be supported by an unassailable written decision.

Enforceable Arbitration Agreements in the Employment Context

An employment arbitration must have these minimum protections:

(1) Provide for a neutral arbitrator; (2) allow more than a minimal amount of discovery during the arbitration process; (3) require a written arbitration award; (4) provide for all types of relief that would otherwise be available in court; and (5) allow the employee to use the arbitration process without imposing unreasonable costs or arbitrator's fees or expenses which might discourage the employee from utilizing the forum to address the grievance. (See *Armendariz, supra*).

Arbitration remains a viable option for employers, but they must watch out for compliance with substantive and procedural nuances before and during the process that may serve to invalidate the arbitration award.

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JEFFREY A. SNYDER

ERIN L. McDERMIT

Thoits, Love, Hershberger & McLean

285 Hamilton Avenue, Suite 300

Palo Alto, California 94301

Telephone: (650) 327-4200

Facsimile: (650) 325-5572

E-mail: jsnyder@thoits.com
emcdermit@thoits.com