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Ten Years (or so) After Gilmer: Arbitration of Employment Law Claims Under the Federal Arbitration Act and the Role of Rhode Island Law

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INTRODUCTION

Contributing to this Law Review issue marking the tenth anniversary of the School of Law has reminded me of how quickly time passes. It seems like only yesterday that I was in the Bickford's Family Restaurant on Jefferson Boulevard late one summer night after exiting Interstate 95 North on my move to Rhode Island. A group of men approximately my age (about thirty

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years old at that time) were sitting at the table next to me engaged in a rather spirited discussion. One said to the group, "You can't beat the guy because he's got no fare." I did not understand what the connection was between winning or losing and having or not having fare (bus, cab, etc.), until another member of the group agreed. "I know, he's too cool. You got him right where you want him and he'll clear the table on you without blinking an eye. The young ones got no fare." I pondered the exchange for a few moments and then understood. They were talking about playing pool, and the guy they could not beat had no FEAR. That mystery solved, I got back on the road.

That was ten years ago, and I have since made much progress. While I will never be able to swap stories with Rhode Islanders about the "Blizzard of 78," I know now that South County is not a county, that Gasbarro's on Federal Hill is as good a wine store as you can find anywhere, and I have seen the membership on the Rhode Island Supreme Court turn over completely.

But this is not generally the stuff of law review articles.[1] Rather than reflect on ten years spent at the law school and in Rhode Island, I have decided to use this opportunity to consider a legal development about as old as the law school – the judicial enforcement under the Federal Arbitration Act (FAA)[2] of mandatory agreements[3] to arbitrate statutory claims of employment discrimination. The story begins with the United States Supreme Court's decision in *Gilmer v. Interstate/Johnson Lane Corp.*, where the Court held that executory agreements to arbitrate claims arising under the federal Age Discrimination in Employment Act were generally enforceable.[4] The story will end, however, with a look at Rhode Island law, because under the FAA agreements to arbitrate must be enforced unless, under generally applicable state law, "grounds . . . exist for the revocation" of the

1. *But see* Michael J. Yelnosky, *If You Write It (S)he Will Come: Judicial Opinions, Metaphors, Baseball, and "The Sex Stuff,"* 28 CONN. L. REV. 813 (1996).

2. 9 U.S.C. §§ 1-16 (2000).

3. By "mandatory agreements" I mean to refer to situations where an employer requires an applicant or incumbent to agree to arbitrate any claims that might arise out of their employment relationship as a condition of future employment.

4. 500 U.S. 20 (1991).

arbitration agreement.[5] No court has considered the important question whether the application of Rhode Island law would render certain arbitration agreements between an employee and an employer unenforceable, and if so, whether Rhode Island law would be preempted by the FAA.

One mission of the School of Law has been and will continue to be to stimulate critical thought about the administration of justice in Rhode Island.[6] I am happy to again be writing about Rhode Island law.[7]

I. *GILMER* AND ITS PROGENY

Much has been written about *Gilmer* and *Circuit City Stores, Inc. v. Adams*,[8] the two cases that will be the focus of this section, so my discussion will be brief. Robert Gilmer was employed by Interstate/Johnson Lane Corp. (Interstate) as manager of financial services.[9] One condition of his employment was that he register as a securities representative with the New York Stock Exchange.[10] The registration application required that Gilmer arbitrate any dispute, claim or controversy between him and Interstate arising out of his employment or termination of employment.[11] When he sued Interstate in federal court under the Age Discrimination in Employment Act (ADEA) challenging his termination, Interstate argued that the suit was barred by the arbitration agreement.[12] The Supreme Court agreed, by a vote of 7-2, reasoning that the FAA required enforcement of the arbitration agreement.[13]

The Court explained that the FAA's primary substantive provision was passed in 1925 to "reverse the longstanding judicial

5. 9 U.S.C. § 2 (2000).

6. *See* Joseph R. Weisberger, *Foreword*, 1 ROGER WILLIAMS U. L. REV. ix (1996) (explaining how a law review can enhance the legal culture in a jurisdiction and looking forward to critical commentary on the work of the judiciary).

7. For my discussion of judicial selection in Rhode Island, which appeared in the inaugural issue of the Law Review, see Michael J. Yelnosky, *Rhode Island's Judicial Nominating Commission: Can Reform Become Reality?*, 1 ROGER WILLIAMS U. L. REV. 87 (1996).

8. 532 U.S. 105 (2001).

9. Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 23 (1991).

10. *Id.*

11. *Id.*

12. *Id.* at 24.

13. *See id.* at 35.

hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration agreements upon the same footing as other contracts."[14] That provision, section 2, states:

> [A] written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.[15]

Because it could not find that Congress intended in the ADEA to preclude the waiver of a judicial forum, the Court concluded that the FAA's "federal policy favoring arbitration" prevailed.[16]

In response to the argument that the arbitration agreements should not be enforced because there is often unequal bargaining power between employers and employees, the Court wrote, "Mere inequality in bargaining power . . . is not a sufficient reason to hold that arbitration agreements are never enforceable in the employment context."[17] However, the Court distinguished "well-supported claims that the agreement to arbitrate resulted from the sort of fraud or overwhelming economic power that would provide grounds for the revocation of any contract," and directed lower courts to consider such claims.[18]

The debate about the impact of *Gilmer* on the enforcement of rights created by employment law, particularly statutes prohibiting discrimination, was quite intense. The Court in *Gilmer* had left unresolved a huge question: Did the FAA apply to employment contracts?[19] Section 1 of the FAA provides that "nothing contained herein shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or in-

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14. *Id.* at 24.
15. 9 U.S.C. § 2 (2000).
16. *Gilmer*, 500 U.S. at 26 (quoting Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983)).
17. *Id.* at 33.
18. *Id.* (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc., 473 U.S. 614, 627 (1985)).
19. Michael J. Yelnosky, *Mediation?* 53 N.Y.U. ANN. CONF. ON LABOR 901 (2004).

terstate commerce."[20] The Court noted this exclusion in *Gilmer*, but concluded that it did not apply because the arbitration clause was in Gilmer's securities registration application, which was a contract with the securities exchanges and not with his employer.[21]

The Court did not decide the question of the scope of the section 1 exclusion for ten years (the magic number for our purposes) when in *Circuit City* it held 5-4 that "[s]ection 1 exempts from the FAA only contracts of employment of transportation workers."[22] Thus, the arbitration agreement Adams signed in his application for employment at a Circuit City retail establishment was governed by the FAA and its policy favoring arbitration. The Court remanded to the Ninth Circuit to determine the effect of that agreement on plaintiff's discrimination lawsuit filed against Circuit City in California state court.[23]

After *Circuit City*, employers could require employees or applicants to sign arbitration agreements with the expectation that those agreements would be enforced if the employee later sued the employer in court.[24] The notable exception to this rule of enforceability is a jurisprudence of "arbitral due process" that was and still is being developed by the lower courts with the imprimatur of the Supreme Court.[25] One continuing battle will thus be over how closely particular arbitral procedures must resemble formal litigation. Arbitrator selection procedures, responsibility for payment of

20. 9 U.S.C. § 1 (2000).

21. *Gilmer*, 500 U.S. at 25 n.2. Justice Stevens and Marshall would have held that the FAA excluded from its coverage all contracts of employment, and would have held that Gilmer's registration application was an employment contract. *See id.* at 39-41 (Stevens, J., dissenting).

22. Circuit City Stores, Inc. v. Adams, 532 U.S. 105, 119 (2001).

23. *Id.* at 123-24.

24. In *EEOC v. Waffle House* the Court concluded that the EEOC could not be barred from bringing suit in court against an employer on behalf of a charging party or other employee, applicant or former employee who had signed an arbitration agreement with the employer. 534 U.S. 279 (2002). Given the small number of cases brought by the EEOC each year, this ruling did not seem to create a robust exception to the general rule of enforceability on which an employer could rely after *Circuit City*.

25. *See* Green Tree Fin. Corp. v. Randolph, 531 U.S. 79 (2000); *see also infra* note 26.

the arbitrator's fees, and the remedies available in arbitration are examples of likely issues for dispute.[26]

But there is another possible obstacle to enforcement that emerged on remand in *Circuit City* that is the focus of this essay: state contract law.

II. *CIRCUIT CITY* AND ITS PROGENY

Recall that in *Circuit City* the Supreme Court remanded the case for the Ninth Circuit to apply the FAA to the arbitration agreement signed by Adams.[27] The court of appeals had held that the FAA did not apply to employment contracts, and the Supreme Court reversed on that issue.[28] But the court of appeals was undaunted. It concluded on remand that the arbitration agreement was not enforceable because it was unconscionable under California law.[29]

The court reasoned that under California law any contract is unenforceable if it is both procedurally and substantively unconscionable.[30] The arbitration agreement signed by Adams was procedurally unconscionable, according to the court, because it was a

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26. A premise underlying the Court's decision in *Gilmer* was that "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 judicial forum." Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991). Many years before, the Court had stated that "there can be no prospective waiver of an employee's rights under Title VII." Alexander v. Gardner-Denver, 415 U.S. 36, 51 (1974). If the arbitral forum is not sufficiently protective of the rights being asserted by the employee, the agreement creating that forum might be viewed as an unenforceable waiver of the employee's substantive rights. *See* Keith N. Hylton, *The Law and Economics of Agreements to Arbitrate Employment Claims*, *in* N.Y.U. WORKING PAPERS ON LABOR AND EMPLOYMENT LAW: 1998-1999, at 315-47 (Michael J. Yelnosky ed., 2001). In fact, in *Green Tree Financial Corp. v. Randolph* the Court suggested, albeit outside the employment context, that an individual who signed an agreement to arbitrate federal statutory claims might be able to resist enforcement of the agreement by showing the arbitral procedures, there the cost of the arbitration, precluded her from effectively vindicating the federal statutory right. 531 U.S. 79 (2000); *see also* Cole v. Burns, 105 F.3d 1465 (D.C. Cir. 1997) (suggesting that arbitral fairness requires neutral arbitrators, more than minimal discovery, a written award, the availability of all relief that would be available in court, and imposition of only "reasonable" costs on plaintiff).

27. Circuit City Stores, Inc. v. Adams, 279 F.3d 889, 892 (9th Cir. 2002).

28. *Id.*

29. *Id.* at 895-96.

30. *Id.* at 893-95.

contract of adhesion, a standard form contract drafted by the party with superior bargaining power that left Adams to either accept or reject the contract in its entirety without the power to negotiate over its terms.[31] The court found the agreement was substantively unconscionable because 1) only Adams and not Circuit City was required to arbitrate disputes with the other, 2) the relief available in arbitration was limited compared to what Adams would have been eligible to recover in court, 3) Adams was required to pay half the arbitrator's fees, and 4) a shorter statute of limitations would apply in arbitration than would apply in court.[32] The Supreme Court denied *certiorari*.[33]

A. *What's State Law Got to Do with It?*

Does the post-*Circuit City* world, in which courts are asked to determine whether particular arbitral procedures are sufficiently fair, include a role for state law? Yes. Do states have the power to decide whether it is good public policy to enforce mandatory agreements to arbitrate employment law claims? No. While there is room for the application of state law to contracts that are within the coverage of the FAA, the role of state law is limited.

1. *FAA Preemption*

Let's start by trying to demarcate the area reserved exclusively for operation of federal law. The FAA applies to "[a] written provision in any . . . contract evidencing a transaction involving commerce."[34] The Supreme Court has held that Congress intended in the FAA to exercise its commerce power to the fullest extent.[35] Thus, only wholly intrastate contracts are unregulated by the FAA. With respect to those contracts, few though they may be, states can legislate as they like or create common law rules to deal with arbitration agreements. All other contracts are regulated by the FAA and its policy favoring arbitration.

Moreover, the FAA applies in state court as well as federal court, requiring enforcement of arbitration agreements where ei-

31. *Id.*
32. *Id.* at 893-95.
33. Circuit City Stores, Inc. v. Adams, 535 U.S. 1112 (2002).
34. 9 U.S.C. § 2 (2000).
35. Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995).

ther state or federal law claims are being asserted by one of the contracting parties.[36] The Court has held that the FAA preempts state law "to the extent that it actually conflicts with federal law – that is, to the extent that it stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[37]

Thus, the Court held in *Southland Corp. v. Keating* that a California statute requiring judicial consideration of claims brought under the California Franchise Investment Law was preempted.[38] It held in *Perry v. Thomas* that a California statute requiring judicial consideration of claims for the collection of wages under the California Labor Code was preempted.[39] Finally, it held in *Doctor's Associates v. Casarotto* that a Montana statute that made arbitration clauses unenforceable unless notice that the contract was subject to arbitration was typed in underlined capital letters on the first page of the contract was preempted.[40]

The broad scope of FAA preemption was cited by twenty-two state attorneys general in their brief to the Supreme Court in *Circuit City,* who argued that application of the FAA to employment contracts would "have the effect of nullifying most state law already in place limiting the enforceability of arbitration in the employment context and of stifling further development of state law in this important area."[41] Just as one example, Arkansas has a statute that requires enforcement of arbitration agreements but exempts from its coverage "employer-employee disputes." [42] That statute would be preempted by the FAA with respect to arbitration agreements covered by section 2 because "Congress intended to foreclose state legislative attempts to undercut the enforceabil-

36. Southland Corp. v. Keating, 465 U.S. 1 (1984) (relying in part on Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967), where the Court held that the FAA was passed pursuant to Congress's authority to enact substantive rules under the Commerce Clause).

37. Volt Info. Sci., Inc. v. Leland Stanford Junior Univ., 489 U.S. 468, 477 (1989).

38. 465 U.S. 1, 16 (1984).

39. 482 U.S. 483, 492 (1987).

40. 517 U.S. 681, 683 (1996).

41. Brief for the State of California, et al. at 19, Circuit City Stores, Inc. v. Adams, 532 U.S. 105 (2001).

42. Ark. Code Ann. §16–108–201 (Michie 2001); Lancaster v. West, 891 S.W.2d 357, 360 (Ark. 1995).

ity of arbitration agreements."[43] In *Circuit City* the majority noted this impact on state law and explained that it was partly a product of the *Southland* holding that the FAA applies in state courts, a holding that was not ripe for reconsideration.[44]

2. *"Arbitration Federalism"*[45]

What role is left for state law where the arbitration agreement in question "evidences a transaction involving commerce" and is, thus, covered by the FAA? Recall that section 2 of the FAA requires enforcement of written agreements unless a refusal to enforce the agreement is based on "grounds as exist at law or in equity for the revocation of any contract."[46] The Court has explained that under this quoted provision of section 2, when deciding whether the parties' agreement to arbitrate is enforceable under the FAA, courts should apply ordinary state law contract princi-

43. *Perry*, 482 U.S. at 489 (citing Southland Corp. v. Keating, 465 U.S. 1, 16 (1984)). *See generally* Charles L. Knapp, *Taking Contracts Private: The Quiet Revolution in Contract Law*, 71 FORDHAM L. REV. 761, 793 (2002) (writing that "under the FAA as currently construed . . . by the Supreme Court . . . it is virtually impossible for either a court or a state legislature to take the position that an arbitration clause must meet standards of disclosure or conspicuousness any higher than those imposed on any other contractual term"); Henry R. Strickland, *The Federal Arbitration Act's Interstate Commerce Requirement: What's Left for State Arbitration Law?*, 21 HOFSTRA L. REV. 385, 400-09 (1992) (describing the wide variety of state laws that would be preempted by the FAA).

44. Circuit City Stores, Inc. v. Adams, 532 U.S. 105, 121-22 (2001). Several members of the Court have expressed the opinion that *Southland* was wrongly decided, and while a majority seem unwilling to overrule it because of considerations of stare decisis, Justices Scalia and Thomas stand ready to join three other Justices in doing so. *See* Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 285-86 (1995); *Southland*, 465 U.S. 1 (1984) (O'Connor, J., Rehnquist, J., and Stevens, J., dissenting). Justice Thomas most recently stated his belief that the FAA does not apply in state court in *Green Tree Financial Corp. v. Bazzle*, 123 S. Ct. 2402, 2411 (2003) (Thomas, J., dissenting).

45. This is the phrase coined by Professors Hayford and Palmiter to refer to the principles of FAA preemption and the remaining role of state law on the question of the enforceability of arbitration agreements. *See* Stephen L. Hayford & Alan R. Palmiter, *Arbitration Federalism: A State Role in Commercial Arbitration*, 54 FLA. L. REV. 175, 193 (2002).

46. 9 U.S.C. § 2 (2000); Circuit City Stores, Inc. v. Adams, 279 F.3d 889, 895-96 (9th Cir. 2002).

ples.[47] However, reliance on state law is limited by the terms of section 2.

> [S]tate law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. A state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with . . . section 2. . . . A court may not, then, in assessing the rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law. Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable . . . .[48]

More specifically, only "generally applicable contract defenses such as fraud, duress, or unconscionability may be applied to invalidate arbitration agreements without contravening section 2."[49]

Given the Supreme Court's interpretation of section 2 of the FAA, the structure and content of the Ninth Circuit's decision on remand in *Circuit City* makes sense, even if reasonable minds might differ as to whether the case is correctly decided. The Ninth Circuit applied California contract law, and its generally applicable doctrine of unconscionability, to hold that the arbitration agreement between Adams and Circuit City, which was executed

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47. *Circuit City*, 279 F.3d at 895; *see* First Options, Inc. v. Kaplan, 514 U.S. 938, 944 (1995). By contrast, the Court interpreted § 301 of the Taft-Hartley Act, 29 U.S.C. § 185 (2000), which provides for suits in federal court to resolve disputes involving collective bargaining agreements, as giving the federal courts the authority to fashion a body of federal common law for interpretation of those collective bargaining agreements, including their arbitration provisions. State law is wholly preempted in this area. Textile Workers Union v. Lincoln Mills, 353 U.S. 448, 450-51 (1957). Whether this would be the preferable reading of the FAA is a subject I hope to address in future work.

48. *Perry*, 482 U.S. at 493 n.9; *see also Allied-Bruce Terminix*, 513 U.S. at 281 (stating that "states may regulate contracts . . . under general contract law principles . . . [but may not] decide that a contract is fair enough to enforce all its basic terms . . . but not fair enough to enforce its arbitration clause").

49. Doctor's Assocs. v. Casarotto, 517 U.S. 681, 687 (1996).

and performed in California, was unenforceable.[50] The court explained that its decision did not run afoul of the FAA "[b]ecause unconscionability is a defense to contracts generally and does not single out arbitration agreements for special scrutiny . . . . Indeed, the Supreme Court has specifically mentioned unconscionability as a generally applicable contract defense that may be raised consistent with § 2 of the FAA."[51] Other courts have come to this conclusion,[52] and one commentator has noted that "the arbitration wars have brought unconscionability back to center stage."[53] However, some courts have concluded that the common law doctrine of unconscionability does not render mandatory arbitration agreements in employment contracts invalid, both because of the limited scope of the unconscionability doctrine of the state whose law governs and the preemptive force of the FAA. [54]

In the final section of this essay I turn to Rhode Island law in search of applicable state law that might lead courts to conclude that mandatory arbitration agreements between employers and

50. *See Circuit City*, 279 F.3d 889.

51. *Id.* at 895. In a more recent decision in which the Ninth Circuit applied California's law of unconscionability to invalidate a Circuit City arbitration agreement, the court explained in more detail how it was walking the fine line that permits invalidating arbitration agreements under state law notwithstanding the federal policy supporting arbitration expressed in the FAA: "The FAA . . . does not supplant state law governing the unconscionability of adhesive contracts. We do not here utter a blanket rule outlawing arbitration agreements in the employment context. . . . Moreover, under California contract law, a court may only refuse to enforce a contract or contract provision if it is both substantively and procedurally unconscionable." Ingle v. Circuit City Stores, 328 F.3d 1165, 1174 n.10 (9th Cir. 2003) (stating also that a contract to arbitrate between an employer and employee is presumptively unconscionable if arbitration is expressly limited to claims brought by the employee or if the claims covered by the agreement are those likely to be brought only by the employee and not the employer).

52. *See, e.g.*, Cooper v. MRM Investment Co., 199 F. Supp. 2d 771 (M.D. Tenn. 2002) (applying Tennessee law).

53. Knapp, *supra* note 43, at 794 n.120.

54. *See, e.g.*, *In re* Halliburton, 80 S.W.3d 566 (Tex. 2002) (holding that arbitration agreement was not procedurally unconscionable because employers are permitted to make "take it or leave it offers" to at-will employees, and not substantively unconscionable because there was no waiver of substantive rights, and the arbitration procedure was fair); Martindale v. Sandvik, 800 A.2d 872 (N.J. 2002) (holding that arbitration agreement in employment application was not unconscionable because the courts of New Jersey have held on numerous occasions that agreements to arbitrate do not violate public policy).

employees would not be enforceable, notwithstanding the applicability of the FAA.

III. RHODE ISLAND LAW

There are at least three interesting aspects of Rhode Island law when viewed from this vantage.

A. *Simple FAA Preemption*

The first serves as a simple illustration of the scope of FAA preemption, albeit outside of the context of mandatory agreements to arbitrate employment claims. Rhode Island has a statute that like the FAA (with an important exception I will discuss below) overrules the common law judicial hostility to arbitration.[55] However, in a least one instance the Rhode Island legislature passed a statute forbidding enforcement of arbitration agreements in a specific setting – contracts between franchisors and franchisees.[56] In 1999 the First Circuit found that statute – the Rhode Island Franchise Investment Act[57] – was preempted by the FAA because it was contrary to the FAA policy of vigorously enforcing arbitration agreements, and it was not a generally applicable contract defense within the meaning of the FAA.[58] Preemption follows from *Southland,* where the Court found that the California Franchise Investment Law, which made arbitration clauses in franchise agreements unenforceable, was preempted by the FAA. [59] If Rhode Island passed a statute making arbitration agreements between employers and employees unenforceable, the statute would be preempted by the FAA, except with respect to wholly intrastate contracts or contracts of employment of transportation workers.

B. *The Rhode Island Arbitration Act*

The second notable aspect of Rhode Island law is the Rhode Island Arbitration Act.[60] As mentioned, it was intended to overrule the common law judicial hostility to arbitration, but its original

55. R.I. GEN. LAWS § 10–3–2 (2003).
56. *See* R.I. GEN. LAWS § 19–28.1–14 (2003).
57. R.I. GEN. LAWS § 19–28.1–1 to –34 (2003).
58. KKW Enters., Inc. v. Gloria Jean's Gourmet Coffees 184 F.3d 42 (1st Cir. 1999).
59. Southland Corp. v. Keating, 465 U.S. 1 (1984).
60. R.I. GEN. LAWS § 10–3–2 (2003).

version required that to be enforceable an arbitration agreement must be "clearly written and expressed and contained in a separate paragraph placed immediately before the testimonium clause or the signatures of the parties."[61] Application of this version of the statute to mandatory agreements to arbitrate between employers and employees would have rendered many unenforceable, but the statute would have been preempted by the FAA under *Casarotto* because it would not place arbitration provisions on the same footing as other contracts.[62]

The provision in the Rhode Island act requiring specific placement of the arbitration agreement was removed in 1976,[63] but the act "conspicuously left unaffected the statutory mandate that agreements to arbitrate be 'clearly written and expressed.'"[64] The statute now provides, "When clearly written and expressed, a provision in a written contract to settle by arbitration a controversy thereafter arising out of such contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract . . . ."[65] The FAA requires that an arbitration agreement be in writing, so the question is whether the "clearly written and expressed" language of the Rhode Island statute imposes an additional requirement of "conspicuousness" on written arbitration agreements, and if so, whether that requirement is preempted by the FAA.

It appears the Rhode Island Supreme Court believes the statute imposes special requirements on arbitration agreements. In *Stanley-Bostich, Inc. v. Regenerative Environmental Equipment Co.* the court had to decide whether a buyer was bound by the arbitration provision in a letter sent by the seller in response

61. Donahue v. Associated Indem. Corp., 227 A.2d 187, 187, 189 (R.I. 1967) (requiring strict adherence to this provision).

62. Doctor's Assocs. v. Casarotto, 517 U.S. 681, 683 (1996) (holding that Montana statute requiring arbitration clause to be typed in underlined capital letters on the first page of the contract is preempted by the FAA).

63. It remains for insurance contracts: "[I]n all contracts of primary insurance, wherein the provision for arbitration is not placed immediately before the testimonium clause or the signature of the parties, the arbitration procedure may be enforced at the option of the insured . . . ." R.I. GEN. LAWS § 10–3–2 (2003).

64. Stanley-Bostitch, Inc. v. Regenerative Envtl. Equip. Co, 697 A.2d 323, 326 (R.I. 1997) (quoting R.I. GEN. LAWS § 10–3–2 (2003)).

65. R.I. Gen. Laws § 10–3–2 (2003).

to a purchase order where the buyer did not sign the seller's letter.[66] The court held first that retention of the letter by the buyer without more was not sufficient to satisfy the Rhode Island Arbitration Act's requirement of an "express and unequivocal agreement to arbitrate."[67] It also held that under the Rhode Island Uniform Commercial Code's version of section 2–207 the arbitration provision in the letter did not become part of the contract because it materially altered the terms of the bargain.[68]

The court's approach in *Stanley-Bostich* raises some interesting issues. First, it appears that where arbitration is involved the court requires an "express and unequivocal agreement," which it does not require in all contract settings, and which it views as required by the "clearly written and expressed" requirement of the state arbitration act. Judge Lageux of the United States District Court for the District of Rhode Island has read the case that way. In *A.T. Cross v. Royal Selangor, Ltd.* he concluded that under *Stanley-Bostich* and the Rhode Island Arbitration Act, Rhode Island's generally applicable doctrine of implied-in-fact contract could not be applied to arbitration agreements because "an arbitration agreement must by clearly written and expressed . . . where mutual assent is manifested in a single written document."[69]

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66. 697 A.2d at 324-25.

67. *Id.* at 327.

68. *Id*; *see also* R.I. GEN. LAWS § 6A–2–207 (1997). Under section 6A–2–207 the confirmation letter served as an acceptance of the purchase order even though it had terms, particularly the arbitration provision, that differed from the terms of the purchase order. Between merchants, and both parties were merchants in *Stanley-Bostich*, the arbitration provision would have become a part of the contract if it did not materially alter the contract.

69. A.T. Cross v. Royal Selanger, Ltd., 217 F. Supp. 2d 229, 236 (D.R.I. 2002). Judge Lageux wrote that under Rhode Island law, an implied-in-fact contract could arise where the parties conduct and communications "'evidenced mutual agreement with regard to the material terms that were to be included in the final contract as well as the simultaneous mutual intention to be bound prior to the formal execution of that contract.'" *Id.* (quoting Marshall Contractors, Inc. v. Brown Univ., 692 A.2d 665, 669 (R.I. 1997)). However, with respect to arbitration, even if both parties had expressed a desire to have disputes resolved through arbitration, no agreement to do so would be enforceable unless both parties were bound to the same arbitration agreement and their mutuality of obligation was objectively manifested in a writing. *Id.*

If the Rhode Island Arbitration Act imposes special requirements for enforcement of arbitration agreements, as compared to other contract provisions, the statute might be preempted by the FAA. However, *Stanley-Bostich* and *A.T. Cross* do not necessarily suggest that the Rhode Island Supreme Court's interpretation of the Rhode Island Arbitration Act is on a collision course with the FAA. First, Rhode Island law is not well-developed in this area. Moreover, the FAA only applies, and therefore only has preemptive effect, where an arbitration agreement is in writing. Both cases could be read as simply requiring that to be enforcable under Rhode Island law, arbitration agreements must be in writing, a state law requirement that is wholly consistent with the FAA. I am suggesting only that special rules applied to the types of writings that will suffice for arbitration agreements as opposed to other contracts might be problematic. As the U.S. Supreme Court said in *Perry v. Thomas*:

> [A] state law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with [section] 2 [of the FAA]. A court may not construe an arbitration agreement in a manner different from that in which it otherwise construes nonarbitration agreements.[70]

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70. Perry v. Thomas, 482 U.S. 483, 492 n.9 (1987). I think the court's reading of 2–207 in *Stanley-Bostich* was plausible and perhaps not preempted by the FAA. My point is that further operationalizing the "suspicion of arbitration" evident in the court's approach to impose requirements on the enforceability of arbitration contracts that are not imposed on other contracts may be preempted by the FAA.

The analysis of courts that have disagreed with the conclusion the Rhode Island Supreme Court reached in *Stanley-Bostich* – that the addition of an arbitration clause is a material alteration of a contract under section 2–207 of the U.C.C. – reflect a more favorable view of arbitration than that expressed by the Rhode Island Supreme Court, and a view that is more consistent with the FAA. The Rhode Island Supreme Court cited a New York Court of Appeals ruling in support of its conclusion that the arbitration provision materially alters the terms of a contract. Stanley-Bostitch, Inc. v. Regenerative Envtl. Equip. Co, 697 A.2d 323, 329 (R.I. 1997) (citing Diskin v. J.P. Stevens & Co., 836 F.2d 47, 50-51 (1st Cir. 1987) (citing Marlene Indus. Corp. v. Carnac Textiles, Inc., 45 N.Y.2d 327 (N.Y. 1978)). In the New York case, the court reasoned "that by agreeing to arbitrate a party waives in large part many of his normal rights under procedural and substantive law of the State." *Marlene Indus.*, 45 N.Y.2d at 33-34. This is directly contrary to the United States Supreme Court's statement in *Gilmer* that "by agreeing to ar-

C. *Unconscionability, Fraud and Duress*

The third and final observation I want to make about Rhode Island law is that the doctrines of unconscionability, fraud and duress seem insufficiently robust to pose serious obstacles to the enforcement of mandatory agreements to arbitrate employment claims.

The Rhode Island Supreme Court's statement of the test for unconscionability places a substantial burden on a party seeking

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bitrate 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 judicial forum." 500 U.S. at 26 (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)). Other courts have criticized the New York approach, which seems to have been adopted in Rhode Island, because it does not take into consideration all the costs and benefits of arbitration in a particular case, but rather presumes that the party opposing arbitration would suffer substantial economic hardship if forced to arbitrate. *See* Bergquist Co. v. Sunroc Corp., 777 F. Supp. 1236, 1246-47 (E.D. Pa. 1991) (cataloging the following costs and benefits of arbitration in the normal course: quicker resolutions, reduced cost, right to participate in selection of arbitrator, arbitral expertise, loss of right to jury trial, inability to terminate cases on motion, and limited grounds for appellate review).

But this is just a matter of disagreement over state contract law, something our federal system not only tolerates, but celebrates. While it does appear *Stanley-Bostich* may be based on a suspicion of arbitration that is inconsistent with the FAA, the 10th Circuit has explained why the FAA would not preempt the Rhode Island approach to arbitration and 2–207.

> Section 2–207 is a general principle of state law controlling issues of contract formation. As a general rule, section 2–207 proscribes binding parties to any important non-negotiated terms of contract. Presumptions against including terms, such as the New York rule, are routinely applied to any term considered significant to the contracting parties.
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> There is a world of difference between a state law rule that requires special preconditions for enforcement of arbitration clauses not required for any other terms of contract . . . and a rule of law that prohibits enforcement of any important term of contract without the express agreement of the parties and then concludes that arbitration is among the group of terms considered important enough to require such express assent . . . .

Avedon Engineering, Inc. v. Seatex, 126 F.3d 1279, 1287 (10th Cir. 1997); *see also* Supak & Sons Mfg. Co. v. Pervel Indus., Inc., 593 F.2d 135, 137 (4th Cir. 1979) (concluding that New York's interpretation of 2–207 is not prempted by the FAA).

to have a contract invalidated on those grounds. According to the court a contract is unconscionable:

> only when the inequality of the bargain [is] so manifest as to shock the judgment of a person of good sense and when terms [are] so unreasonable that no man in his senses and not under delusion would make on the one hand and no honest and fair man would accept on the other.[71]

Although there are few cases in Rhode Island elaborating on this test, the First Circuit has read Rhode Island law as requiring courts to look for both procedural unconscionability (the absence of meaningful choice on the part of the party seeking to invalidate the contract), and substantive unconscionability (terms that are unreasonably favorable to the other party to the contract) in evaluating the merits of the defense.[72] In the normal course, it would seem that Rhode Island courts would conclude mandatory arbitration agreements are not unconscionable.

Beginning with procedural unconscionability; on the one hand, the Rhode Island Supreme Court has regularly held, for example, that insurance contracts are contracts of adhesion because "an insurance policy is not a true consensual arrangement but one that is available to the premium-paying customer on a take-it-or-leave-it basis." [73] It has found that other "take-it-or-leave-it form contracts" are contracts of adhesion.[74] An arbitration provision in an employment application, employment contract or employment handbook has these characteristics and therefore also might be deemed an adhesion contract under Rhode Island law.

However, under Rhode Island law an adhesion contract is not unenforceable. If it is ambiguous, it is to be interpreted against the drafter of the contract.[75] Nevertheless, if a mandatory agreement to arbitrate employment claims is an adhesion contract, the argument that it is procedurally unconscionable is strong. If the

71. Grady v. Grady, 504 A.2d 444, 446-47 (R.I. 1986) (citing Hume v. United States, 132 U.S. 406 (1889)).

72. E.H. Ashley & Co. v. Willow Assocs., 907 F.2d 1274, 1278 (1st Cir. 1990).

73. Pickering v. American Employers Insurance Co., 282 A.2d 584, 593 (R.I. 1971).

74. Elliott Leases Cars, Inc. v. Quigley, 373 A.2d 810, 811 (R.I. 1977) (finding that a car lease was an adhesion contract).

75. Bush v. Nationwide Mutual Ins. Co., 448 A.2d 782, 784 (R.I. 1982).

agreement is not "truly consensual" because it is required employment, a court applying the unconscionability doctrine could conclude that the employee had no choice but to agree to arbitration.

On the other hand, Rhode Island continues to cling fast to the rule of at-will employment, under which an employee without a contract for a term may be terminated at any time for good reason, bad reason or no reason at all.[76] The at-will rule has been justified, in part, because it is simply a default rule – the parties can always agree to a different term to cover job security issues.[77] Thus, one assumption underlying the at-will rule is that employees have the choice to accept an at-will relationship, negotiate for more job protection, or look for employment elsewhere. Individuals faced with the decision whether to agree to arbitration as a condition of employment would, the reasoning would follow, have the same meaningful choices, suggesting that agreements between employees and employers are not ordinarily procedurally unconscionable. Moreover, the FAA may be preemptive on the question of procedural unconscionability as applied to arbitration agreements between most employees and employers.[78] The Court in *Gilmer* rejected the claim that the arbitration agreement there should not be enforced because of the inequality of bargaining power between employees and employers: "Mere inequality in bargaining power . . . is not a sufficient reason to hold that arbitration agreements are never enforceable in the employment context."[79] Arguably, only "well-supported claims that the agreement to arbitrate resulted from the sort of fraud or overwhelming economic power that would provide grounds for the revocation of any contract" can be the basis for a decision not to enforce the arbitration agreement.[80]

However, even if a mandatory arbitration agreement was deemed procedurally unconscionable by a Rhode Island court, it would ordinarily be exceedingly difficult for an employee arguing

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76. *See* Roy v. Woonsocket Instit. for Savings, 525 A.2d 915, 917 (R.I. 1987).

77. Richard A. Epstein, *In Defense of the Contract at Will*, 51 U. CHI. L. REV. 947, 953-55 (1984).

78. Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 33 (1991).

79. *Id.*

80. *Id.* (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 627 (1985)).

that the agreement should not be enforced to prove that it was substantively unconscionable. For example, the Rhode Island Supreme Court has held that a limitation of liability provision in a contract to provide security services was not unconscionable, notwithstanding the fact that it permitted the security service provider to limit its liability to $360 in a clear case of negligence, where the security company had failed to program its computer to receive signals from the alarm system it installed in plaintiffs' jewelry store.[81] The court relied on an Illinois case that evaluated the unconscionability defense in the terms the Supreme Court of Rhode Island has used.[82] Allocating the risk of loss to the plaintiff was "not a bargain 'which no man in his senses and not under delusion, would make . . . and which no fair and honest man would accept.'"[83]

Moreover, the Rhode Island legislature has passed the Rhode Island Arbitration Act, which overrules the judicial hostility to arbitration.[84] Under those circumstances it would be difficult for a court to conclude that an arbitration agreement was against the public policy of Rhode Island.

Once again, the shadow of FAA preemption looms large. As the Supreme Court stated in *Circuit City,* their FAA jurisprudence in this area is based on the understanding that it would be reasonable for an employee to agree to arbitration of employment claims.[85]

> [F]or parties to employment contracts . . . there are real benefits to the enforcement of arbitration provisions. . . . Arbitration agreements allow parties to avoid the costs of litigation, a benefit that may be of particular importance in employment litigation, which often involves smaller sums of money than disputes concerning commercial contracts.[86]

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81. Ostalkiewicz v. Guardian Alarm, 520 A.2d 563, 566 (R.I. 1997); *see also* E.H. Ashley & Co. v. Wells Fargo Alarm Services, 907 F.2d 1274, 1278-79 (1st Cir. 1990) (following *Ostalkiewicz*).

82. *Ostalkiewicz*, 520 A.2d at 565.

83. *Id.* (quoting Fireman's Fund Am. Ins. Co. v. Burns Electronic Security Services, Inc., 417 N.E.2d 131, 132-33 (Ill. Ct. App. 1981)).

84. *See* R.I. GEN. LAWS § 10–3–2 (2003).

85. Circuit City Stores, Inc. v. Adams, 532 U.S. 104, 122-23 (2002).

86. *Id.*

I think the FAA provides room for Rhode Island's doctrine of unconscionability to invalidate agreements to arbitrate entered into by particularly vulnerable employees or agreements that so favor the employer that they can be construed as a waiver of the employee's substantive rights created by state or federal law. However, this would not be unlike the arbitral due process approach currently being taken by the federal courts interpreting the substantive federal law created by the FAA.[87] The state law of unconscionability would not stand as a unique obstacle to the enforcement of arbitration agreements covered by the FAA.

Not surprisingly, it would be rare for fraud to be grounds for refusing to enforce an arbitration clause in an employment contract. In most cases, the applicant or incumbent employee will simply be offered a document for signature that includes the arbitration clause. While the Supreme Court of Rhode Island has stated that an agreement to arbitrate in an employment contract is not enforceable if the employee signatory can prove fraud in the inducement of that agreement, the employee must show that the employer made a false representation intended to induce the employee's reliance, and the employee must have justifiably relied on the statement to his or her detriment.[88] In cases where the employee is simply offered the arbitration provision on a take-it-or-leave-it basis, claims of fraud in the inducement will not be justified.

Finally, it is also unlikely that Rhode Island's common law doctrine of duress would be implicated in any litigation over the enforceability of mandatory agreements to arbitrate employment claims. Before he became Chief Justice of the Rhode Island Supreme Court, then Superior Court Judge Williams wrote that a contract can be set aside on grounds of duress under Rhode Island law only when a contracting party is compelled to enter into a contract and deprived of the exercise of free will by the unlawful act of another.[89] The threat of doing what the other party has a legal right to do is not a threat that renders a contract voidable under

87. *See supra* note 26 and cases cited.

88. Bjartmarz v. Pinnacle Real Estate Tax Serv., 771 A.2d 124, 127 (R.I. 2001) (quoting Travers v. Spidell, 682 A.2d 471, 472-73 (R.I. 1996)).

89. Tinney v. Tinney, No. NC98-0116, 1999 R.I. Super. LEXIS 140, at *42 (July 30, 1999).

the doctrine of duress.[90] In light of the at-will rule, which gives the employer the legal right to discharge an employee for good reason, bad reason, or no reason at all, conditioning an applicant's consideration for employment or an incumbent's continued employment on agreement to arbitrate employment claims is not undue or unlawful pressure that can be sanctioned through application of the doctrine of duress.

Moreover, as the Rhode Island Supreme Court has explained in circumstances quite relevant to this discussion, duress renders a contract voidable, and the "victim" may ratify the agreement by failing to object promptly.[91] Thus, the Court has concluded that even assuming that a plaintiff's decision to enter into an employment contract in which he waived a statutory right to a hearing before termination was not voluntary because his employer threatened him with loss of employment if he did not sign the contract, he could not claim duress.[92] The court explained:

> A party asserting duress must act promptly or be deemed to have affirmed the conduct in question. The plaintiff performed under the [contract] for approximately eighteen months before contesting it. . . . "A party who has received the benefit of the performance of a contract will not be permitted to deny his or her obligations unless paramount public interest requires it."[93]

This waiver doctrine would preclude application of the doctrine of duress in any case where the employee worked for some period before contesting the validity of the arbitration agreement.

CONCLUSION

Where are we then, in 2004, just over ten years since the *Gilmer* decision? Some doctrinal issues in this area have been resolved. The most important is that the FAA applies to arbitration agreements in most employment contracts. While the FAA establishes a strong presumption in favor of enforceability, one important area needing clarification is the scope of the exceptions to this

90. *Id.*
91. *See* McGee v. Stone, 522 A.2d 211 (R.I. 1987).
92. *Id.* at 214-15.
93. *Id.* (quoting City of Warwick v. Boeng Corp., 472 A.2d 1214, 1218 (R.I. 1984)).

general rule of enforceability that are based on defects in the arbitral system created by the parties' agreement – what I have been calling the "arbitral due process" issue. These exceptions to the rule of enforceability are the product of interpretations of the FAA. Under *Southland* these interpretations are applicable in federal and state court to agreements covered by the FAA. Finally, we know there is room for application of state law to arbitration agreements covered by the FAA both in state and federal court litigation based on state or federal law, but trying to ascertain the appropriate role for state law is difficult indeed. I do not suspect that we have heard the last words from the Supreme Court on these issues. And who knows? Maybe Congress will decide that with the 100th anniversary of the FAA approaching (2025) this area of the law could use some revision.