LAW JOURNAL NEWSLETTERS

Employment Law Strategist

May 2011

Limitations on Third-Party Discovery in Arbitration, Helpful or Harmful to the Employer?

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In recent years, it has become almost a foregone conclusion that a savvy employer seeking to avoid costly litigation with its employees will require those employees to sign agreements that provide for mandatory arbitration of any claims arising out of their employment. However, the decision to submit all employment disputes to mandatory arbitration only should be made after a careful analysis of the pros and cons of arbitration so that the employer can determine whether the perceived benefits of arbitration actually are worth the significant disadvantages.

One perceived benefit of arbitration is that it is assumed to be less expensive than court litigation. This assumption is based in large part on the notion that discovery is limited in arbitration. However, in many cases, the same amount of discovery takes place in arbitration as it does in court litigation, and thus no cost saving is achieved.

In arbitration, the parties can issue written discovery to each other and take depositions in the same manner as they would if they were litigating in a court of law. Prior to the arbitration, the employer can send document requests and interrogatories to the plaintiff and take his or her deposition. The plaintiff also can take the deposition of a corporate representative of the employer and likely can depose any current employee of the employer. The only sense in which discovery is even arguably limited in arbitration is as it relates to third parties (*i.e.*, persons and entities that are not parties to the arbitration or the arbitration agreement).

Pre-Hearing Discovery

In this regard, some courts have held that arbitrators do not have the authority to compel third parties to provide pre-hearing discovery in arbitration. *See, e.g., Hay Group v. EBS Acquisition Corp.*, 360 F.3d 404 (3rd Cir. 2004) ("In sum, we hold that the FAA did not authorize the panel to issue a pre-hearing discovery subpoena … [and] reject[ing] any 'special needs exception' to this rule"); *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*, 549 F.3d 210 (2nd Cir. 2008) ("Thus, we join the Third Circuit in holding that section 7 of the FAA does not authorize arbitrators to compel pre-hearing document discovery from entities not party to the arbitration proceedings"). In these jurisdictions, the parties to an arbitration would not be able to require a third party to produce documents or appear for deposition prior to the arbitration hearing.

Other courts have held that pre-hearing discovery from third parties may only be compelled upon a showing of special need or hardship. *See, e.g., Comsat Corp. v. Nat'l Science Foundation*, 190 F.3d 269 (4th Cir. 1999) (holding that a party may "petition the district court to compel pre-arbitration discovery upon a showing of special need or hardship"). In

these jurisdictions, the person seeking to compel discovery would need to apply to a court to authorize the issuance of a subpoena to a third party. This could cause significant delay and added expense, unlike in court, where the parties can by right issue subpoenas to third parties prior to trial.

Pros and Cons

One could argue that these restrictions on pre-hearing discovery in arbitration are desirable because they result in less discovery, and therefore less cost. However, such restrictions on pre-hearing discovery could adversely affect the employer's ability to prevail at arbitration. Consider the following scenario: An individual sues her former employer, alleging that she was sexually harassed by a supervisor while she was employed by the company. The matter is taken to arbitration pursuant to the employer's policy. Although the supervisor denies that he engaged in any of the harassing conduct described in the complaint, the plaintiff claims that one particularly egregious act of harassment was witnessed by another former employee. The plaintiff's attorney informs the company's lawyer that he has spoken with the former employee and that this person will corroborate the plaintiff's version of events and intends to testify at the arbitration hearing. The company's lawyer calls the former employee to discuss his potential testimony, but that individual will not return the calls.

Court vs. Arbitration

If this were a lawsuit being litigated in court, the company simply would issue a subpoena to the former employee commanding him to appear at a pretrial deposition. The company's lawyer would be able to depose the former employee, finding out the exact nature of his testimony and asking questions designed to limit the damaging aspects of the testimony and tie the former employee's testimony down before the trial. If the testimony were very damaging, the company could evaluate whether or not it wants to settle the case prior to trial. However, because the claim is being pursued in arbitration, the company may have to wait until the hearing itself to find out what the former employee is going to say because, depending on the jurisdiction in which the arbitration is being held, the company may or may not be able to take the former employee's deposition before the hearing.

Conclusion

Although it is true that when both parties have the ability to compel third-party pre-hearing discovery, the potential cost-savings to be achieved through arbitration are diminished. Not having the ability to compel discovery from third parties prior to the hearing can affect the employer's ability to prevail in the arbitration because critical evidence may not be available. Any employer in a business that involves a good deal of third-party traffic, such as those in the hospitality industry, where guests, customers or vendors might witness relevant conduct, should think twice about having arbitration be the sole means through which employment disputes may be resolved.

However, the potential inability to compel third-party discovery prior to the hearing is not the only disadvantage of arbitration. Lack of direct appeal, inexperience and capriciousness of arbitrators and lax rules on the admission of evidence are just a few of the other downsides of arbitration. If the goal is trying disputes with employees before a jury, this can be achieved simply by obtaining a jury waiver from the employees. Accordingly, each employer needs to weigh the pros and cons of arbitration carefully in light of the benefits the employer hopes to be gained through mandatory arbitration of claims.

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