Arbitration Agreements Are Enforceable Despite Some Unenforceable Provisions, Says Third Circuit

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One of the current controversies over mandatory arbitration agreements in the employment setting involves whether employees can be required to split the costs of the arbitration process with their employers. Addressing the question of the enforceability of arbitration agreements containing such provisions, the U. S. Court of Appeals for the Third Circuit recently ruled that such a fee-splitting provision, which itself may be unenforceable, does not render the whole agreement unenforceable. In reaching its decision, the court balanced the "liberal federal policy favoring arbitration agreements," with Pennsylvania's contract law that holds that an unenforceable provision in a contract does not void the whole contract if the unenforceable provision is not an essential term. Spinetti v. Service Corporation International (3rd Cir., 2003).

The dispute in this case arose after the employee was terminated and filed suit under Title VII of the Civil Rights Act of 1964 and the Age Discrimination in Employment Act against her former employer. During the course of her employment, the employee had signed a "Principles of Employment" agreement, which contained compulsory arbitration provisions. When the employer sought to dismiss the suit and compel arbitration, the federal district court found the "legal counsel/costs" provision, which required each party to pay their own legal fees regardless of the outcome of the agreement, to be invalid. Both Title VII and the ADEA permit the award of attorney's fees to a prevailing party, the court noted. Using arbitration as a means of dispute resolution should not infringe upon statutory rights. Nor should the costs to the complaining party be prohibitive, which the district court found they were. As a result, the court ordered arbitration with the employer bearing all costs and the attorney's fees to be determined by the applicable statute.

When the plaintiff appealed on the grounds that the entire agreement was invalid, the U. S. Court of Appeals for the Third Circuit looked at the Pennsylvania state law governing a contract which contains an invalid provision. Ruling that "federal arbitration policy must be implemented in lock-step with a determination of contract validity under state law," the Third Circuit looked at Pennsylvania law to determine if the stricken costs and fees provisions were essential terms of the whole agreement. If so, the court would be obliged to invalidate the entire agreement. However, the court determined that the primary purpose of the arbitration agreement was not to regulate costs or attorney's fees but was to provide a mechanism for dispute resolution. Since the provisions in question were not essential terms to the contract, Pennsylvania law permits enforcement of the non-offending part of the agreement.

For Pennsylvania employers, this decision reinforces the arbitration process as a viable means for employment dispute resolution even if a non-essential provision in the agreement runs afoul of current law. This decision provides stability for the arbitration process on an issue in which plaintiffs and courts in other jurisdictions have found vulnerability. As long as the essential terms requiring arbitration are enforceable, invalid fee-splitting and cost sharing provisions will not render the remaining portions of the agreement void.

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