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California Supreme Court Clarifies When An Arbitration Award May Be Corrected

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On January 29, 2015, the California Supreme Court issued a decision clarifying the circumstances under which an arbitrator's award may be corrected. In *Richey v. Autonation, Inc.*, No. BC408319 (Cal. Jan. 29, 2015), the court examined an arbitrator's award and concluded that, although the arbitrator may have committed error in applying the defendants' proffered "honest belief" defense (a defense not provisioned under California law) the plaintiff was nevertheless afforded his statutory rights. The court explained that, because the arbitrator determined the plaintiff's employment was terminated for violating his employer's policy prohibiting outside employment while on medical leave, the plaintiff was not prejudiced by the arbitrator's arguably misplaced application of the honest belief defense.

Factual Summary

The plaintiff began working for defendant Power Toyota Cerritos in 2004. Upon hire, the plaintiff signed an agreement requiring that any employment dispute be settled by arbitration. Also upon hire, the plaintiff received an employment manual prohibiting outside employment while on a medical leave.

Around October 2007, while the plaintiff was still employed full time by the defendant, he began laying the groundwork for the February 2008 opening of his restaurant. His supervisors at the defendant took notice of his slipping performance and attendance, and met with him in February 2008 to discuss the need for improvement.

On March 10, 2008, the plaintiff injured his back at home, resulting in his physician declaring him medically unable to work. On March 28, 2008, the plaintiff sought and received a medical leave under the California Family Rights Act (CFRA) and the federal Family and Medical Leave Act (FMLA) from the defendant. The defendant also granted subsequent requests by the plaintiff to extend his leave.

On April 11, 2008, the plaintiff's supervisor sent him a letter reminding him of the defendant's policy that employees were not to pursue outside employment while on medical leave and that he should call if he had questions. The plaintiff ignored this letter. On April 18, 2008, the defendant sent an employee to observe the plaintiff's restaurant. The employee testified observing plaintiff sweep, bend and deploy a hammer.

The defendant terminated the plaintiff's employment on May 1, 2008, 27 days prior to the expiration of his medical leave. In its termination letter, the defendant explained that its decision was based on the plaintiff engaging in outside employment while on medical leave in violation of company policy.

The plaintiff subsequently filed a lawsuit in the Superior Court of California, Los Angeles County alleging multiple claims under the California Fair Employment and Housing Act (FEHA) and the CFRA. The trial court granted the defendants' motion to compel arbitration.

After an 11-day hearing, the arbitrator rejected each of the plaintiff's contentions in a 19-page order. The arbitrator framed the issue as: "whether the law provides a protective shell over [the plaintiff] that bars his termination until he is cleared to return to work by his physician, or does the law allow an employer to let an employee go, while on approved leave, for other non-discriminatory reasons?" The arbitrator concluded that "case law . . . allows [the defendant] to terminate [the plaintiff] if it has an 'honest' belief that he is abusing his medical leave and/or is not telling the company the truth about his outside employment." The arbitrator also found that "the weight of the evidence is overwhelming that [the defendant] fired [the plaintiff] for non-discriminatory reasons. His medical leave does not protect [him] from smart decisions, or bad ones, made by [the defendant], so long as the basis for the decision is legally proper."

The plaintiff sought to vacate the arbitrator's award in part, asserting that the arbitrator committed reversible legal error because he exceeded his powers when he accepted the defendants' honest belief defense. The trial court denied the plaintiff's motion, which the appellate court reversed.

California Supreme Court's Analysis

The California Supreme Court overturned the appellate court's ruling. Its analysis centered on whether the arbitrator acted "in excess of his powers," providing grounds for reversal of his award under the California Arbitration Act. One of the ways an arbitrator may exceed his or her powers is by issuing an award that violates a party's unwaivable statutory rights.¹

The court focused on its 2010 *Pearson Dental Supplies, Inc. v. Superior Court* decision.² There, the court found that the arbitrator deprived the employee of his statutory rights when he misapplied the relevant tolling statute and incorrectly held that the employee's claim was time-barred. In so erring, the arbitrator denied the employee a hearing on the merits. The arbitrator "misconstrued the procedural framework under which the parties agreed the arbitration was to be conducted, rather than misinterpreting the law governing the claim itself."³

The court then analyzed the CFRA, explaining, "the right to reinstatement is unwaivable but not unlimited."⁴ An employee's right to be placed in a position following a medical leave is not greater than if the employee had been continuously working during the leave period.⁵

The court reasoned that, even if the arbitrator erred in adopting the honest belief defense, the plaintiff failed to show that such error was prejudicial. Indeed, the arbitrator found the plaintiff was fired because he violated the defendant's policy prohibiting outside work while on medical leave, not because he was on leave. The court explained, "to hold that [the defendant] could not have fired plaintiff under any circumstances for violating company policy while on leave would ignore the rule that [the] plaintiff had 'no greater right to reinstatement . . . than if [he] had been continuously employed' during the statutory leave period."⁶ Furthermore, the court noted that the arbitrator would likely have made the same finding regardless of [the defendant]'s honest belief that the plaintiff was misrepresenting his medical condition. Accordingly, even if the arbitrator was mistaken in relying on this defense, the plaintiff was not prejudiced as a result. Thus, the plaintiff was not deprived of an unwaivable right and the court upheld the arbitrator's award.

1 See e.g. *Bd. of Educ. v. Round Valley Teachers Ass'n* (1996) 13 Cal.4th 269, 272-77.

2 *Pearson Dental Supplies, Inc. v. Superior Court* (2010) 48 Cal.4th 655.

3 *Id.* at 679-80.

4 *Richey*, S207536 (slip op., at 10).

5 See Cal. Code Regs., tit. 2, § 11089(a) and (c)(1); see also 29 C.F.R. § 825.216(a).

6 *Richey*, S207536 (slip op., at 13).

Considerations for Employers and Practitioners

The *Richey* decision is important for employers and practitioners because it demonstrates the importance of making sound and reasoned employment decisions, particularly when dealing with employees who are on medical leaves of absence. The court explained in fine detail all of the steps the employer took in advising the employee of its policies, the employer's efforts to enforce them, and the employee's subsequent disregard. The court's detailed examination of these steps contributed to its ultimate conclusion that the employer terminated the employee because of his policy violation. Absent this meticulous record, the court may have found otherwise.

The following are key takeaways:

- Draft company policies with clear and unambiguous language;
- Ensure that company policies are distributed and that employees acknowledge receipt; and
- Uniformly and consistently enforce company policies.

It is noteworthy what the *Richey* decision does not stand for. It does not assess the legality of employment provisions forbidding outside employment concurrent with medical leaves of absence. It also does not declare whether the honest belief defense applies when an employer terminates an employee based on a reasonable belief that the employee is violating company policy while on a medical leave.

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