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Suggestions for Defeating Arbitration

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Abstract

In his Commentary, the author responds to Arbitration: Avoiding the Runaway Jury, *an article written by Russel Myles and Kelly Reese and published in the* Journal *last year. 23 AM. J. TRIAL ADVOC. 129 (1999). The author argues here that arbitration is an inferior form of dispute resolution because arbitration's costs to the social, political, and legal fabric of society exceed its benefits. Consequently, the author enumerates and discusses a number of strategies for defeating arbitration. Discussion begins with analysis of Alabama law and then considers the decisions of other courts.*

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I. Introduction

Like it or not, with the decision in *Allied-Bruce Terminix Cos. v. Dobson*,[1] the United States Supreme Court opened the door for product sellers, service providers, and insurers to include arbitration provisions

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[1] 513 U.S. 265, 115 S. Ct. 834, 130 L. Ed. 2d 753 (1995), *reh'g denied*, 684 So. 2d 102 (Ala. 1996).

in consumer contracts.[2] Despite evidence that the public disfavors arbitration[3] and despite repeated calls for protection of consumers,[4] the

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[2] *See Dobson*, 513 U.S. at 281.

[3] On November 12, 2000, an Alabama newspaper reported the results of a telephone survey of 415 adult residents of Alabama. Sean Reilly, *Poll: 45 Percent Don't Care for Idea of Binding Arbitration*, MOBILE REG., Nov. 12, 2000, at 1B, 3B. Claiming a 95% confidence level and a ±5% margin of error, this survey revealed that 45% of those asked thought that binding arbitration was a "bad idea." *Id.* Sixty-five percent thought binding arbitration benefitted businesses more than consumers. *Id.* Forty-four percent of those surveyed concluded that government should regulate the use of such contracts. *Id.*

[4] For example, the editors of *USA Today* wrote the following on February 1, 2000:

> Buy an item off the popular eBay auction Web site, and you've just given away your right to sue. If you have a beef with eBay, you'll go before a private arbitrator instead of a judge in court. The Web giant has even picked the place: San Jose, eBay's home, but not exactly convenient to the vast majority of consumers.
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> A growing number of e-world businesses are joining the ranks of banks and credit card companies that quietly force customers into arbitration agreements. Customers, simply by making a purchase, often automatically give up their right to sue. Unless, of course, they challenge the agreement itself. At times, consumers only realize what they've lost when there's a problem, and they can't file suit.
>
> Businesses defend arbitration as a cheap, convenient alternative to court. And many insist that their customers favor arbitration, even though it forces them to give up the right to a jury trial and generally to appeal a loss.
>
> But if arbitration is such a win-win proposition, companies should be eager to sell the idea in bold, understandable language.
>
> Many aren't even coming close:
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> • Before a New York consumer sued, computer maker Gateway had rules forcing customers to arbitrate disputes in Chicago and pay $4,000 – more than the cost of most Gateway products – just to bring a claim. In 1998, a New York judge ruled the terms "unconscionable." Gateway has changed its process.
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> • Chevy Chase Bank announced its arbitration policy to credit card holders in 1996 in minuscule print included with a billing statement. Three consumers have sued challenging the policy, and the case is now on appeal.
>
> • American Express told nearly 30 million customers of its new arbitration policy in an innocuous "F.Y.I." notice stuffed in with their April bills. Once consumers used their cards, their right to sue was automatically gone.
>
> Companies insist that such disclosures are adequate and that it's up to customers to read the materials they receive.
>
> If they did, many consumers would discover they have little control over how arbitrated disputes are handled. For instance, it costs at least $775 to get an in-person hearing before the American Arbitration Association. Go to small claims courts in most states, and the filing fee is far less than $100.

fact is that much injustice has already occurred and more will occur in the future as binding arbitration provisions continue to flood the marketplace. Litigators need not necessarily succumb to the onslaught of arbitration; this Article presents several strategies for defeating motions to compel arbitration.

First, the Article discusses persuasive social, historical, and political reasons for rejecting binding arbitration. Next, the Article enumerates important issues to consider in the effort to defeat binding arbitration. Discussion of the legal issues begins with analysis of recent Alabama Supreme Court decisions and then considers the decisions of other courts.

II. Social, Historical, and Political Issues

A threshold social issue confronting arbitration is that the process has no accountability. Unlike judges who are subject to regulation by the Judicial Inquiry Commissions, lawyers who are subject to regulation by state bar associations, and politicians who are subject to regulation by the

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> And under the rules of the National Arbitration Forum, which handles disputes for American Express, consumers cannot join in class action lawsuits, often the only tool that provides leverage over wealthy corporations.
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> At the very least, businesses intent on tossing out these consumer rights should be able to design an arbitration announcement that shouts, "Hey, look at me," or summarizes the real costs for consumers. Better yet, why not give consumers a choice: arbitration or court?
>
> If arbitration is as consumer-friendly as the companies proclaim, they should have no problem finding plenty of takers.

Consumers Losing Right to Sue, USA TODAY, Feb. 1, 2000, at 13A. The editors of *Consumer Reports* concluded a recent article about arbitration with the following requests:

> Consumers Union thinks that a fair arbitration process should be voluntary on the part of both parties to a contract and not imposed on consumers unilaterally. Rules governing the process should be clearly disclosed. Arbitration fees for indigent consumers should be waived. Finally, no arbitration clause should limit an individual's ability to join with other similarly harmed consumers in a class-action lawsuit. Only when these protections are assured can arbitration truly deliver the saving--and impartial justice--that its backers promise.

Your Money–*The Arbitration Trap: How Consumers Pay for 'Lost Cost' Justice*, CONSUMER REPORTS, Aug. 1999, at 64.

State Ethics Panels, arbitrators are subject to no regulatory entity. Arbitrators may do as they wish and they have no one to answer to for their decisions.[5]

Arbitration raises a another social issue: the costs of the process of arbitration increase with the size of the controversy. For example, according to the American Arbitration Association's (AAA) Construction Dispute Rules, a controversy over a $50,000 house would cost the homeowner $1,250 just to file a claim for arbitration.[6] A controversy over a $300,000 house will cost the homeowner $3,500.[7] On the other hand, under our traditional system of filing suit in state court a controversy involving amounts up to $10,000 requires payment of only a filing fee of $100 or so; controversies exceeding $10,000 require payment of a filing fee of $200.[8]

In addition to the money which must be sent to the AAA (and other, similar bodies) just to invoke the arbitration process, the consumer is also stuck with paying the arbitrator's expenses (which is ordinarily a steep hourly rate) and the costs associated with providing the place within which to conduct the arbitration hearing (such as a hotel conference room).[9]

Why would anyone in their right mind voluntarily incur these tremendous costs when the *public* dispute resolution system (*i.e.*, courts) is already paid for through our taxes?

Still another social concern implicated by arbitration is that resolution of civil controversies will no longer be by formal and predictable rules but will instead by subject to the vagaries of a system designed to function without clear rules. Under our historical civil justice system, the citizens

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[5] *See* 9 U.S.C.A. § 10 (West 2000) (stating that courts may vacate an arbitrator's decision only upon a showing of fraud, corruption, or undue means in the process). An arbitrator's mistakes of law are not appealable.

[6] *American Arbitration Ass'n Construction Industry Dispute Resolution Procedures Administrative Fees*, *at* http://www.adr.org (last visited Nov. 17, 2000) [hereinafter *Administrative Fees*].

[7] *Id.*

[8] The Alabama clerk for the district court reports that filing fees for disputes over $3000 and less than $10,000 is $113. The Alabama clerk for the circuit court reports that the filing fee for a controversy exceeding $10,000 is $200 (including a jury demand fee).

[9] *Administrative Fees*, *supra* note 6.

know that the rules of evidence, the rules of civil procedure, the rules of professional conduct, and local court rules all provide very clear guidance for how lawyers and parties must act while resolving controversies. For example, if a recalcitrant hospital was unwilling to turn over critical documents concerning a patient's care and treatment, the patient could go to a judge and obtain an order requiring that the records be turned over, under threat of punishment. In arbitration proceedings, on the other hand, there are no enforcement tools to protect the victim or make wrongdoers do the right thing.

Arbitration provides an unfair forum for the resolution of disputes. When was the last time you heard of an ordinary citizen signing up to become an arbitrator? How many truck drivers, postal workers, housewives, school teachers, or other working men or women are certified arbitrators? What chance will Mr. or Mrs. Ordinary Citizen have to prevail when they are judged by those who have sought the jobs as certified arbitrators, jobs such as insurance industry executives, retired building contractors, corporate attorneys and the like?[10]

Arbitration ignores the basic tenets of due process. Our country's civil justice system has developed over 200 years. In that time, thousands upon thousands of cases have been heard and decided, and from that collective experience the important fabric of our nation's laws has emerged. Included among those laws are important due process protections that spell out each citizen's rights and obligations.

Nothing in the arbitration rules requires the arbitrator to adhere to our basic rules of law.[11] To the contrary, arbitrators are free to disregard them. What is more, many arbitrators have no training in the law and would not know how to correctly enforce these rights and obligations, assuming they were inclined to do so.[12]

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[10] *See, e.g.*, Sarah Rudolph Cole, *Incentives and Arbitration: The Case Against Enforcement of Executory Arbitration Agreements Between Employers and Employees*, 64 U. MO. KANSAS CITY L. REV. 449, 478 (1996) (discussing how the arbitrator selection process favors employers over employees).

[11] *See* Murray S. Levin, *The Role of Substantive Law in Business Arbitration and the Importance of Volition*, 35 AM. BUS. L.J. 105, 113 (1997) (stating that "most arbitrators are not obligated to follow substantive law").

[12] *See* Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 WM. & MARY L. REV. 1, 51 (2000) (noting that critics would like to see judicial involvement because "arbitrators lack the qualifications and

Arbitration ignores the common law principle of stare decisis. Appellate court decisions and some trial court decisions are reported in official publications for the guidance of future disputants. Even before a dispute arises, a lawyer can read cases and advise a client on a course of conduct. The application of statutes to varying situations is developed through individual cases. This is not the case with arbitration. A dispute that is sent to arbitration disappears without a trace.[13] When consumer disputes are routinely sent to arbitration, the development of any law of consumer protection will be arrested and no adaptation to changing circumstances will occur. Thus, arbitration is the privatization of dispute resolution not only because a private individual decides the case rather than a public judicial official, but also because the result is private and no public body of law arises from the conclusion of the dispute.[14] Only the commercial repeat players will know what arbitrators are doing and what internal boundaries they have or have not developed.[15]

Finally, and most importantly, we must consider how this new movement towards arbitration runs afoul of the fundamental constitutional liberties entrusted to us by our founding fathers. The Seventh Amendment in the Bill of Rights of the United States Constitution declares that we as citizens have the right to trial by jury.[16] In Alabama, as in other

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experience necessary to decide complicated class issues"); Julian J. Moore, Note, *Arbitral Review (or Lack Thereof): Examining the Procedural Fairness of Arbitrating Statutory Claims*, 100 COLUM. L. REV. 1572, 1589 (2000) (arguing that sufficient scrutiny is not applied to the qualifications of arbitrators of employment discrimination claims).

[13] Most arbitration awards are not published. When the dispute involves labor matters, some awards are published in reporters such as Labor Arbitration Reports. Labor Arbitration Reports is published by the Bureau of National Affairs, Inc. (BNA) in Washington, D.C. The BNA selects awards for publication based upon the general interest of the material and clarity of the arbitrator's reasoning. 107 BUREAU OF NATIONAL AFFAIRS POLICY ON ARBITRATION AWARD SELECTION, LABOR ARBITRATION REPORTS: DISPUTE SETTLEMENTS vii (2000).

[14] *See* Levin, *supra* note 11, at 108-11; Stephen J. Ware, *Default Rules From Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 752 (1999) (suggesting that, "[i]f arbitration clauses appeared in the contracts of a few major hubs–such as the utilities providing water, electricity or phone service–nearly every American might well agree to arbitrate any dispute with anyone").

[15] *See* Cole, *supra* note 10, at 474 (discussing how arbitration favors repeat players over one-shot players).

[16] U.S. CONST. amend. VII.

states, our forefathers preserved this sacred right to trial by jury through Article I, Section 11 of our Constitution, which states "[t]hat the right to trial by jury shall remain inviolate."[17] Thousands of heroic men and women have sacrificed their lives to protect the unenumerable rights found within our system of law. Is it to be the legacy of our generation to give up these cherished rights without even a fight?

III. Legal Issues to Evaluate

Alabama has witnessed an avalanche of arbitration provisions in service contracts, new and used car and truck sales, mobile home sales, realtor listing contracts, medical care contracts, and insurance contracts. Alabama's Supreme Court has recently been swamped with arbitration cases. At the time of this writing, the supreme court had rendered 135 decisions concerning arbitration in just the past three years.[18] Thus, the Alabama Supreme Court has examined many important issues surrounding the enforceability of arbitration provisions. Using Alabama law as a starting point, the Article next discusses eight strategies for defeating arbitration and examines how those strategies are treated in other states.

A. General Contract Defenses May Defeat Arbitration

First and foremost, it is important to remember that under the Federal Arbitration Act (FAA), traditional contract defenses are available to avoid enforcement of unfair arbitration provisions. The Act states in part:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction,

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[17] ALA. CONST. art. I, § 11.

[18] Research on electronic databases resulted in a finding that the Alabama Supreme Court has rendered 135 arbitration related decisions in the three years preceding November, 2000.

> or refusal, shall be valid, irrevocable, and enforceable, *save upon such grounds as exist at law or in equity for the revocation of any contract.*[19]

In *Allied-Bruce Terminix Cos. v. Dobson*, the Supreme Court held that

> [Section 2 of the FAA] gives [s]tates a method for protecting consumers against unfair pressure to agree to a contract with an unwanted arbitration provision. States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause "upon such grounds as exist at law or in equity for the revocation of *any* contract."[20]

In *Doctor's Associates, Inc. v. Casarotto*, the Supreme Court noted that "generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening § 2 [of the FAA]."[21] The starting point towards defeating arbitration is determining whether contract defenses exist.

B. Is There a Written Provision in a Contract?

First, the litigator should ask whether there is a *written provision* in a *contract* concerning arbitration. The first sentence of section 2 of the FAA states that it applies to "[a] *written provision* in any maritime transaction or a *contract*."[22]

In *Ex parte Payne*, the Alabama Supreme Court granted mandamus and ordered a circuit court to set aside an order compelling arbitration because there was no contract.[23] This occurred under familiar facts--a person attempted to buy a used car, but the retail purchase order she signed said the sale was contingent on her being approved for financing.[24]

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[19] 9 U.S.C. § 2 (1999) (emphasis added).

[20] 513 U.S. 265, 281, 115 S. Ct. 834, 843, 130 L. Ed. 2d 753, 769 (1995) (quoting 9 U.S.C. § 2 (1995) (emphasis added)).

[21] 517 U.S. 681, 687, 116 S. Ct. 1652, 1656, 134 L. Ed. 2d 902, 909 (1996).

[22] 9 U.S.C. § 2 (1999) (emphasis added).

[23] 741 So. 2d 398, 404 (Ala. 1999).

[24] *Ex parte* Payne, 741 So. 2d at 399-401.

Since she was not approved, no *contract* was formed and the seller, therefore, could not invoke the arbitration provision.[25] Since there was a contingency contract, and since the "contingency" directly addressed in the contract never occurred, there was no contract.

Most state courts agree with Alabama and have held that arbitration provisions are invalid unless the provisions are in a written contract.[26]

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[25] *Id.* at 404.

[26] *See* Willis Flooring, Inc. v. Howards S. Lease Constr. Co. & Assocs., 656 P.2d 1184, 1185 (Alaska 1983); United States Fidelity & Guar. Co. v. Triple H Elec. Co., No. CA99-245, 1999 WL 1031264, at *2 (Ark. Ct. App. Nov. 10, 1999); Badie v. Bank of Am., 67 Cal. App. 4th 779, 787, 79 Cal. Rptr. 2d 273, 278 (1998); Boys Club of San Fernando Valley, Inc. v. Fidelity & Deposit Co., 6 Cal. App. 4th 1266, 1271, 8 Cal. Rptr. 2d 587, 589 (Ct. App. 1992); *In re* Marriage of Popack, 998 P.2d 464, 467 (Colo. Ct. App. 2000); Levine v. Advest, Inc., 244 Conn. 732, 745, 714 A.2d 649, 656 (1998); Bennett v. Meader, 208 Conn. 352, 360, 545 A.2d 553, 557 (1988); DMS Properties-First, Inc. v. P.W. Scott Assocs., Inc., 748 A.2d 389, 391 (Del. 2000) (interpreting the state's statute that provides, "a written agreement to submit to arbitration any controversy existing at or arising after the effective date of the agreement is valid, enforceable and irrevocable"); Henderson v. Coral Springs Nissan, Inc., 757 So. 2d 577, 578 (Fla. Dist. Ct. App. 2000); Bishop Contracting Co. v. Center Bros., Inc., 213 Ga. App. 804, 805, 445 S.E.2d 780, 781 (1994); Brown v. KFC Nat'l Mgmt. Co., 82 Haw. 226, 232, 921 P.2d 146, 152 (1996); Gumprecht v. Doyle, 128 Idaho 242, 244, 912 P.2d 610, 612 (1995); Johnson v. Noble, 240 Ill. App. 3d 731, 734, 608 N.E.2d 537, 540, 181 Ill. Dec. 464, 467 (1992) (denying defendant's motion to compel arbitration of plaintiff's breach of contract and breach of fiduciary duty claims where the claims were based on an oral agreement prior to and independent of a written contract containing an arbitration clause); CAC Graphics, Inc., v. Taylor Corp., 154 Ill. App. 3d 283, 286, 507 N.E.2d 171, 173, 107 Ill. Dec. 507, 509 (1987); Int'l Creative Mgmt., Inc. v. D & R Entm't Co., 670 N.E.2d 1305 (Ind. Ct. App. 1996); I.D.C., Inc. v. McCain-Winkler Partnership, 396 So. 2d 590, 592 (La. Ct. App. 1981); Roosa v. Tillotson, 695 A.2d 1196, 1198 (Me. 1997); Barnstead v. Ridder, 39 Mass. App. Ct. 934, 936, 659 N.E.2d 753, 755 (1996); Carpenter v. Pomerantz, 36 Mass. App. Ct. 627, 628, 634 N.E.2d 587, 588 (App. Ct. 1994); Mitchell v. Dahlberg, 215 Mich. App. 718, 547 N.W.2d 74 (1996); Anderson v. Federated Mut. Ins. Co., 465 N.W.2d 68, 69 (Minn. Ct. App. 1991); Roth v. Scott, 112 Nev. 1078, 1083, 921 P.2d 1262, 1265 (1996); *In re* Lincoln-Woodstock-Co-op Sch. Dist., 143 N.H. 598, 600, 731 A.2d 992, 994 (1999); American States Ins. Co. v. Sorrell, 258 A.D.2d 782, 783, 684 N.Y.S.2d 711, 712 (N.Y. App. Div. 1999); Brumm v. McDonald & Co. Sec., Inc., 78 Ohio App. 3d 96, 101, 603 N.E.2d 1141, 1144 (1992); School Dist. of City of Erie v. Erie Educ. Ass'n, 749 A.2d 545, 547 (Pa. Commw. 2000); Midomo Co. v. Presbyterian Housing Dev. Co., 739 A.2d 180, 183 (Pa. Super. Ct. 1999) (stating that, "[i]n order for an agreement to arbitrate to fall within Uniform Arbitration Act, two requirements must be met: First, the agreement must be in writing; and second, the agreement must expressly provide for arbitration under the

A few states have held that an agreement to arbitrate disputes need not be in the form of a written contract.[27] In *Lyman v. Kern*, the New Mexico Court of Appeals discussed "common law arbitration" and stated that, "[a]lthough preferably any agreement to arbitrate should be placed in writing, New Mexico continues to recognize common law arbitration."[28] Under common law arbitration, the parties' agreement to arbitrate need not be reduced to a writing.[29] If parties can demonstrate that an intent to submit to arbitration existed at the time of the contract's formation, common law arbitration is applicable and specific documentation is not required.[30]

Act"); Stanley-Bostitch, Inc. v. Regenerative Envtl. Equip. Co., 697 A.2d 323, 326 (R.I. 1997); Thunderstik Lodge, Inc., v. Reuer, 585 N.W.2d 819, 822 (S.D. 1998); Equity Residential Properties Mgmt. Corp. v. Silvers, 1998 WL 549289, at *4 (Tex. App. Aug. 31, 1998); Pacific Dev., L.C., v. Orton, 982 P.2d 94, 97 (Utah Ct. App. 1999); Joder Bldg. Corp. v. Lewis, 153 Vt. 115, 118, 569 A.2d 471, 472 (1989); Jones v. Davis, 2000 WL 628789, at *1, 2 (Wash. Ct. App. May 12, 2000).

[27] Quigley v. KPMG Peat Marwick, LLP, 330 N.J. Super 252, 270-71, 749 A.2d 405, 415-16 (2000) ("'[I]n determining whether the parties have agreed to arbitrate, state law contract principles apply[, and the] . . . duty to arbitrate, and the scope of arbitration are dependent solely on the parties' agreement.'"); Wasserstein v. Kovatch, 261 N.J. Super. 277, 285, 618 A.2d 886, 890 (1993) (stating that "[p]arties can consent to arbitration even in the absence of a written agreement") (citing Stop & Shop Cos. v. Gilbane Bldg Co., 364 Mass. 325, 330, 304 N.E.2d 429, 432 (1973)); Halvorson-Mason Corp. v. Emerick Constr. Co., 304 Or. 407, 412, 745 P.2d 1221, 1224 (1987) (noting that arbitration statutes do not require written agreement, do not replace common-law arbitration when statute does not apply.); Coventry Teachers' Alliance v. Coventry Sch. Comm., 417 A.2d 886, 889 (R.I. 1980) (stating that a "party's willingness to arbitrate a specific issue need not be express but may be implied from the conduct of the parties") (citing Ficek v. Southern Pac. Co., 338 F.2d 655, 656 (9th Cir. 1964)); Hot Springs County Sch. Dist. No. 1 v. Strube Constr. Co., 715 P.2d 540, 545 (Wyo. 1986) (stating that agreement to arbitrate does not have to be in writing and can arise as a result of the parties' conduct to existing dispute regardless of whether parties previously contracted for arbitration).

[28] 128 N.M. 582, 585, 995 P.2d 504, 507 (Ct. App. 1999).

[29] *Lyman*, 995 P.2d at 507.

[30] *Id.* (noting that "[c]ommon law applies when arbitration agreements fail to meet statutory formalities"); *see* Wetzel v. Sullivan, King & Sabom, P.C., 745 S.W.2d 78, 81 (Tex. Ct. App. 1988) (stating that, "[e]ven if a written agreement is not executed and no writing exists that satisfies the [arbitration statute], a common law right to arbitration is enforceable if an appropriate agreement to submit to arbitration is shown").

C. Does the Contract Substantially Affect Interstate Commerce?

The next step asks whether the maritime transaction or contract at issue substantially involves *interstate commerce*. Absent a substantial connection with interstate commerce, there is no authority for federal regulation by the FAA under Congress's Commerce Clause Power.[31] Transactions purely *intrastate* in nature are *not* regulated by federal law.

The Alabama Supreme Court in *Sisters of the Visitation v. Cochran Plastering Co.*[32] cited *United States v. Lopez*[33] as requiring proof of a "substantial effect" on interstate commerce before a pre-dispute arbitration provision will be deemed to be enforceable under the FAA.[34] The court held that *Lopez* recognized limits on the power of Congress to regulate through the Commerce Clause such that the proponent of an arbitration provision will bear the burden of proving that the transaction has a "substantial effect" on commerce given factors such as the parties' citizenship, tools and equipment used, allocation of costs of services and materials, subsequent movement across state lines, and degree of separability from other contracts.[35] *Sisters of the Visitation* could be recognized within the world of arbitration as a landmark decision, making it required reading for any attorney confronted with a pre-dispute arbitration agreement.

Earlier, in *Rogers Foundation Repair, Inc. v. Powell*, the Alabama Supreme Court held that a contract by an Alabama corporation to perform repairs on a chimney of an Alabama residence did *not* have a substantial effect on interstate commerce even though the contract contained a recitation which stated that it did.[36] The court granted a petition for

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[31] *See* 9 U.S.C.S. § 1 (Law. Co-op. 1999).

[32] No. 1981513, 2000 WL 264243 (Ala. Mar. 10, 2000) (Lyons, Houston, Cook, Johnstone, & England, J.J., concurring; Brown, J., concurring in the result; Hooper, C.J., Maddox, See, J.J., dissenting).

[33] 514 U.S. 549, 559, 115 S. Ct. 1624, 1630, 131 L. Ed. 2d 626, 637 (1995) (stating "that the proper test [of the scope of the Commerce Clause] requires an analysis of whether the regulated activity 'substantially affects' interstate commerce").

[34] *Sisters of the Visitation*, 2000 WL 264243, at *2 (citing *Lopez*, 514 U.S. at 560).

[35] *Id.* at *6.

[36] 748 So. 2d 869, 870-72 (Ala. 1999).

mandamus and reversed a trial court order requiring arbitration upon holding that there was no substantial effect on interstate commerce and that the FAA could not be invoked.[37] Similarly, in *Southern United Fire Insurance Co. v. Knight*, the court held that an automobile insurance policy issued by an Alabama corporation does *not* "substantially affect" interstate commerce; therefore, an arbitration provision contained in such a policy will not be enforced.[38]

All other state courts addressing the issue have held that the arbitration provision in the agreement is valid only when the parties' agreement affects interstate commerce.[39]

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[37] *Powell*, 748 So. 2d at 872.

[38] 736 So. 2d 582, 586-87 (Ala. 1999).

[39] *See* McEntire v. Monarch Feed Mills, Inc., 631 S.W.2d 307, 309 (Ark. 1982); Dryer v. Los Angeles Rams, 40 Cal. 3d 406, 411, 709 P.2d 826, 829, 220 Cal. Rptr. 807, 810 (1985); Grohn v. Sisters of Charity Health Serv. Colo., 960 P.2d 722, 725 (Colo. Ct. App. 1998); Levine v. Advest, Inc., 244 Conn. 732, 747, 714 A.2d 649, 657 n.13, 658 (Conn. 1998); Pullman, Inc. v. Phoenix Steel Corp., 304 A.2d 334, 337 (Del. Super. Ct. 1973); Brown v. KFC Nat'l Mgmt. Co., 82 Haw. 226, 233, 921 P.2d 146, 153 (1996); University Casework Sys., Inc. v. Bahre, 172 Ind. App. 624, 636, 362 N.E.2d 155, 163 (1977); R.J. Palmer Constr. Co. v. Wichita Band Instrument Co., 7 Kan. App. 2d 363, 365, 642 P.2d 127, 129 (1982); Kodak Mining Co. v. Carrs Fork Corp., 669 S.W.2d 917, 920 (Ky. 1984); Collins v. Prudential Ins. Co. of Am., 752 So. 2d 825, 828 (La. 2000); Baxter Health Care, Corp. v. Harvard Apparatus, Inc., 35 Mass. App. Ct. 204, 207, 617 N.E.2d 1018, 1019 n.2 (Ct. App. 1993); Burns v. Olde Discount Corp., 212 Mich. App. 576, 580, 538 N.W.2d 686, 688 (1995); Northwest Mechanical, Inc. v. Public Utils. Comm'n, 283 N.W.2d 522, 523-24 (Minn. 1979); IP Timberlands Operating Co. v. Denmiss Corp., 726 So. 2d 96, 107 (Miss. 1998); Mueller v. Hopkins & Howard, P.C., 5 S.W.3d 182, 185-86 (Mo. Ct. App. 1999); Smith Barney, Inc. v. Painters Local Union No. 109 Pension Fund, 254 Neb. 758, 762, 579 N.W.2d 518, 521 (1998); Sentry Sys., Inc., v. Guy, 98 Nev. 507, 508-09, 654 P.2d 1008, 1008-09 (1982); Bleurner v. Parkway Ins. Co., 277 N.J. Super. 378, 388-90, 649 A.2d 913, 918-19 (Super. Ct. Law Div. 1994); Yale Materials Handling Corp. v. White Storage & Retrieval Sys., Inc., 240 N.J. Super. 370, 375-76, 573 A.2d 484, 487-88 (Super. Ct. App. Div. 1990); Laur & Mack Contracting Co. v. Di Cienzo, 234 A.D.2d 999, 1000, 651 N.Y.S.2d 831, 832 (N.Y. App. Div. 1996); Paramore v. Inter-Regional Fin. Group Leasing Co., 68 N.C. App. 659, 663, 316 S.E.2d 90, 92 (Ct. App. 1984); Cross v. Carnes, 132 Ohio App. 3d 157, 163-64, 724 N.E.2d 828, 832-33 (Ct. App. 1998); Shaffer v. Jeffery, 915 P.2d 910, 915 n.10 (Okla. 1996); Duquesne Light Co. v. New Warwick Mining Co., 443 Pa. Super. 53, 56, 660 A.2d 1341, 1343 (Super. Ct. 1995); Towles v. United Healthcare Corp., 338 S.C. 29, 36, 524 S.E.2d 839, 843 (Ct. App. 1999); Dinsmore v. Piper Jaffray, Inc., 593 N.W.2d 41, 43-44 (S.D. 1999); Frizzell Constr. Co. v. Gatlinburg, L.L.C., 9 S.W.3d 79, 82-83 (Tenn. 1999); Trade-Industrial Centre "COTO," Ltd. v. Amherst Int'l, Inc., 85 Wash. App. 1076, 1997 WL 190953, at *1 (Ct. App. 1997).

D. Was There an Agreement by Plaintiff?

Another question to be answered is whether there is clear and unmistakable evidence of an *agreement by the plaintiff to arbitrate*. Counsel should determine, for example, whether all of the plaintiffs were parties to the contract. Did a minor enter into a contract containing an arbitration clause without the consent of his parents? Did a husband sign a new car purchase form but his wife did not? Do each of the documents containing arbitration provisions bear the plaintiff's signature and thereby evidence his agreement to arbitrate? Without any appropriate signature, what evidence is required to determine whether the plaintiff actually agreed to the arbitration provision?

One state has held that, if a party fails to sign an arbitration agreement, the party is not bound by the agreement.[40] In *Brown v. KFC National Management Co.*, a husband and wife brought claims of race discrimination and tort against the defendant.[41] The court determined that the husband had signed and was bound by an arbitration provision.[42] The court stated that wife's tort claims were not bound by the arbitration provision because the wife had not signed the provision.[43] The court reasoned that while the wife's claims were derivative of her husband's, the wife's claims were separable and her potential damages were not coextensive with her husband's.[44]

Federal decisions have also held that arbitration will not be enforced absent evidence the plaintiff signed a document specifically agreeing in writing to arbitration.[45]

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[40] Brown v. KFC Nat'l Mgmt. Co., 82 Haw. 226, 243 921 P.2d 146, 163 (1996).

[41] *Brown*, 921 P.2d at 150.

[42] *Id.* at 159.

[43] *Id.* at 163.

[44] *Id.*; *see also* Liberty Communications, Inc. v. MCI Telecomms. Corp., 733 So. 2d 571, 575 (Fla. Dist. Ct. App. 1999) (the individual signed in a corporate capacity thus the clause was not binding on the individual).

[45] *See* Grundstad v. Ritt, 106 F.3d 201, 205 (7th Cir. 1997) (holding that the guarantor was not bound by the arbitration agreement); *see also* IDS Life Ins. Co. v. SunAmerica Life Ins. Co., 136 F.3d 537, 542 (7th Cir. 1998) ("As the plaintiffs did not agree to arbitrate any dispute they might have with SunAmerica Life, they cannot be

The results from the Alabama Supreme Court on this issue, on the other hand, are a mixed bag. In *Ex parte Rush*, the court found evidence of an agreement to arbitrate even though the homeowner did *not* sign a "termite protection plan" document containing an arbitration provision but did renew his termite policy with Terminix each year for nine years.[46] The court concluded that, because of consistent renewal of the policy, the homeowner impliedly consented to the arbitration provision.[47]

The Supreme Court has determined that an arbitration provision in the parties' contract is binding only if the parties agreed to the provision.[48] In *Quigley v. KPMG Peat Marwick, LLP*, the New Jersey Superior Court noted "that the duty to arbitrate[] and the scope of arbitration are

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forced to give up their judicial remedies . . . merely because they have an arbitrable dispute with affiliates of the defendant."); *see also* Rosenberg v. Merrill, Lynch, Pierce, Fenner & Smith, Inc., 170 F.3d 1, 20 (1st Cir. 1999) (concluding that the plaintiff did not agree to an arbitration clause because the defendant failed to certify that the plaintiff was "familiar" with the clause); McCreary v. Liberty Nat'l Life, 6 F. Supp. 2d 920 (N.D. Miss. 1998) (noting an application for a policy, signed by the plaintiff, did not constitute an agreement by the plaintiff to arbitrate when an endorsement adding an arbitration clause was received).

[46] 730 So. 2d 1175, 1177 (Ala. 1999).

[47] *Rush*, 730 So. 2d at 1178. *Cf. Ex parte* Dickinson, 711 So. 2d 984, 989 (Ala. 1998) (holding that a non-signatory is not bound to an arbitration clause).

[48] *See* AT&T Tech., Inc. v. Communication Workers of Am., 475 U.S. 643, 648, 106 S. Ct. 1415, 1418, 89 L. Ed. 2d 648 (1986) (citing Steelworkers v. Warrior & Gulf Navigation Co., 363 U.S. 574, 80 S. Ct. 1347, 4 L. Ed. 2d 1409 (1960)); *c.f.* A.C. Beals Co. v. Rhode Island Hosp., 110 R.I. 275, 284, 292 A.2d 865, 869-70 (1972) (holding that an arbitration clause in boiler manufacturer's written proposal for boiler construction which could be properly positioned only by deleting one paragraph and by incorporating by reference a purchase order was not "clearly written and expressed" within the meaning of statute; the statute provided that agreements to arbitrate are valid only when they are clearly written, expressed, and contained in a separate paragraph placed immediately before the testimonium clause or signature of the parties); Buraczynski v. Eyring, 919 S.W.2d 314, 319 (Tenn. 1996) (stating that a retroactive arbitration clause is enforceable); *In re* H.E. Butt Grocery Co., 17 S.W.3d 360, 372 (Tex. App. 2000) (stating that "a party who signs a contract containing an arbitration provision does not have to be told about the provision, but [rather] is presumed to know the contents of the contract"); Joder Bldg. Corp. v. Lewis, 153 Vt. 115, 119, 569 A.2d 471, 473 (1989) (holding that the parties' agreement to be bound by an arbitration award did not meet the requirement of the statute because the agreement did not "state clearly that signing the agreement forecloses any court remedies concerning any dispute that arises which is covered by the arbitration agreement").

dependent solely on the parties' agreement."[49] The court further stated that, "'[i]n the absence of a consensual understanding, neither party is entitled to force the other to arbitrate their dispute. Subsumed in this principle is the proposition that only those issues may be arbitrated which the parties have agreed shall be.'"[50] In finding for the plaintiff, the court reasoned that an arbitration clause "'should clearly state its purpose'" because such clauses deprive citizens of access to the courts.[51] The court concluded that, "[i]f [the] defendant wanted to enter into an agreement to bind plaintiff to arbitration under all circumstances, it should have written an inclusive arbitration clause."[52]

In contrast to *Quigley*, the Montana Supreme Court in *Solle v. Western States Insurance Agency, Inc.* found that an employee's contract was subject to arbitration.[53] The *Solle* court reasoned that "'any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.'"[54]

Some states have even held that parties may agree to arbitration despite the fact that the parties did not sign the contract.[55] Georgia's appellate

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[49] 330 N.J. Super. 252, 270-71, 749 A.2d 405, 415-16 (N.J. Super. Ct. App. Div. 2000) (quoting Cohen v. Allstate Ins. Co., 231 N.J. Super. 97, 101, 555 A.2d 21, 23 (N.J. Super. Ct. App. Div. 1989)).

[50] *Quigley*, 749 A.2d at 416 (quoting *In re* Arbitration Between Grover & Universal Underwriters Ins. Co., 80 N.J. 221, 228-29, 403 A.2d 448, 452 (1979)).

[51] *Id.* (quoting Marchak v. Claridge Commons, Inc., 134 N.J. 275, 282, 633 A.2d 531, 535 (1993)).

[52] *Id.* at 417 (citing Singer v. Commodities Corp. (U.S.A.), 292 N.J. Super. 391, 405, 678 A.2d 1165, 1172 (N.J. Super. Ct. App. Div. 1996)).

[53] 999 P.2d 328, 333 (Mont. 2000).

[54] *Solle*, 999 P.2d at 332 (quoting Snap-on Tools Corp. v. Vetter, 828 F. Supp. 468, 473 (D. Mont. 1993)).

[55] U.S. Fidelity & Guar. Co. v. Triple H Elec. Co., 1999 WL 1031264, at *2 (Ark. App. Nov. 10, 1999) (holding that, even though an arbitration clause itself need not be signed by the parties in order to be effective, "there must still be a writing to which the parties' conduct may attach"); Dodge of Winter Park, Inc. v. Morely, 756 So. 2d 1085, 1086 (Fla. Dist. Ct. App. 2000) (granting motion to compel arbitration despite the fact that automobile dealership inadvertently neglected to sign the agreement); Convest, L.L.C. v. Corporate Sec. Group, Inc., 234 Ga. App. 277, 280, 507 S.E.2d 21, 24 (Ct. App. 1998) (quoting Valero Refining v. M/T Lauberhorn, 813 F.2d 60, 64 (5th Cir. 1987)) (concluding that a party may be bound by an agreement to arbitrate even in the absence of his signature); Schwarzschild v. Martin, 191 Conn. 316, 322, 464 A.2d 774,

court reasoned that, under Georgia law, a party may be bound by an arbitration agreement even if the party did not sign the agreement.[56] The court explained that a party may become bound by an agreement when he indicates his consent to the agreement by accepting the benefits provided by the contract.[57]

E. Determine Who Was Intended to Be Covered By the Arbitration Provision

The next step when dealing with arbitration provisions is to determine whether all the wrongdoers are parties to the contract containing the arbitration provision. There have been several recent Alabama Supreme Court decisions that have addressed the specificity needed in an arbitration provision before a related party–not a signatory to the contract–may nevertheless invoke the arbitration provision for its own use and benefit.

The basic test for claims against non-signatories is whether the claims against them are "*inextricably intertwined*" with the claims against the party or parties who did sign the document containing the arbitration provision.

In *Universal Underwriters Life Insurance Co. v. Dutton*, a consumer purchased a new car and entered into an arbitration agreement with the dealership.[58] The dealership then assigned the car loan to a lender.[59]

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777 (1983) (holding that "a party who signs an arbitration agreement, petitions a court for arbitration, then participates in the arbitration proceedings may not later avoid his agreement because of a claim that the other party did not sign the agreement"); *In re* Succession of Taravella, 734 So. 2d 149, 151 (La. Ct. App. 1999) (citing Hurley v. Fox, 520 So. 2d 467 (La. App. 4th Cir. 1998), *on remand*, 559 So. 2d 887 (La. App. 4th Cir. 1990) (holding that, when an agreement lacks a signature, the actions and the conduct of the party or parties, who did not sign, may show the effect or validity of the agreement)); American States Ins. Co. v. Sorrell, 258 A.D.2d 782, 783-84, 684 N.Y.S.2d 711, 712 (App. Div. 1999) (finding that "[t]here is . . . no requirement that the writing be signed, provided there is other proof that the parties actually agreed to arbitrate").

[56] Comvest, L.L.C. v. Corporate Soc. Group, Inc., 234 Ga. App. 277, 280-81, 507 S.E.2d 21, 24-25 (Ct. App. 1998).

[57] *Comvest, LLC*, 507 S.E.2d at 24-25.

[58] 736 So. 2d 564, 566-67 (Ala. 1999).

[59] *Dutton*, 736 So. 2d at 567.

included in the sale was a policy of credit life insurance.[60] The consumer filed a claim against the dealership, the lender assignee, and the credit insurance company claiming fraud in connection with the sale of the credit insurance policy.[61] The Alabama Supreme Court enforced the arbitration agreement as to the dealer, its salesman, and the lender assignee, but refused to enforce arbitration as to the credit insurance company, reasoning that claims against the credit insurance company were not within the scope of the contract's arbitration provision.[62]

Alabama is one of a vast majority of states that apply contract and agency law principles to determine whether a non-signatory third party is bound by an arbitration provision.[63] For example, in *Elf Atochem North*

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[60] *Id.* at 566-67.

[61] *Id.* at 566.

[62] *Id.* at 568-70.

[63] *See* American Ins. Co. v. Cazort, 361 Ark. 314, 321, 871 S.W.2d 575, 579 (1994) (stating that it is "clear that nonsignatories to a contract may be deemed as parties, through ordinary contract and agency principles, for the purpose of the Federal Arbitration Act"); Boys Club of San Fernando Valley, Inc. v. Fidelity & Deposit Co., 6 Cal. App. 4th 1266, 1271-73, 8 Cal. Rptr. 2d 587, 589-90 (Ct. App. 1992); Busconi v. Digbello, 39 Conn. App. 753, 764, 668 A.2d 716, 722 (Ct. App. 1995); Liberty Communications Corp. v. MCI Telecomm., 733 So. 2d 571, 574, 24 Fla. L. Weekly 1103 (Dist. Ct. App. 1999); Comvest. L.L.C. v. Corporate Sec. Group, Inc., 234 Ga. App. 277, 280-81, 507 S.E.2d 21, 24-25 (Ct. App. 1998) (stating that contract and agency law principles will govern who the arbitration agreement may be enforced against, and that the signature of a party may not be necessary); Rath v. Managed Health Network, Inc., 123 Idaho 30, 31, 844 P.2d 12, 13 (1992); Jacob v. C & M Video, Inc., 248 Ill. App. 3d 654, 618 N.E.2d 1267, 1271, 188 Ill. Dec. 697, 701 (App. Ct. 1993) (stating that when a president of the franchisees signed in his representative capacity on behalf of the franchisees rather than in his individual capacity, the president as an individual was considered a nonparty to the arbitration agreement and he could not compel arbitration or be compelled to arbitrate under the franchise agreements); Curtis G. Testerman Co. v. Buck, 340 Md. 569, 576-80, 667 A.2d 649, 653-55 (1995); Rae F. Gill, P.C. v. DiGiovanni, 34 Mass. App. Ct. 498, 503-06, 612 N.E.2d 1205, 1208-09 (Ct. App. 1993); Hetrick v. Friedman, 237 Mich. App. 264, 267, 602 N.W.2d 603, 605 (Ct. App. 1999) (holding that a health insurer was not required to arbitrate any claim it had against the defendant, where the health insurer had intervened in an insured's medical malpractice action, but did not sign the arbitration agreement entered into by the insured and the defendant); Byrd v. Sprint Communications Co., 931 S.W.2d 810, 813 (Mo. Ct. App. 1996); Wasserstein v. Kovatch, 261 N.J. Super. 277, 286, 618 A.2d 886, 890 (1993); Monette v. Tinsley, 126 N.M. 748, 750, 975 P.2d 361, 363 (1999) (holding that the guarantor of a promissory note was only a witness to the contract and that the guarantor is not generally a party against whom the underlying contract terms

America, Inc. v. Jaffari, the plaintiff argued that a Limited Liability Company (LLC) should not be bound by an arbitration provision because no one signed the provision on behalf of the LLC.[64] The court quoted a Delaware statute stating that an LLC's agreement is "'any agreement, written or oral, of the member or members as to the affairs of a limited liability company and the conduct of its business.'"[65] Applying the statute, the court determined that the LLC was bound to the agreement by the signatures of the LLC's members.[66]

F. Determine What Was Intended to Be Arbitrated

The next possible means of avoiding arbitration is scrutinizing the scope of what the parties agreed to arbitrate. For example, "disputes 'arising out of' the contract" is narrower in scope than "disputes . . . relating to . . . the contract," which, in turn, is narrower than a provision that covers any and all disputes between the parties to the contract, their successors and assigns.[67]

On this issue, *American Bankers Life Assurance Co. v. Rice Acceptance Co.*[68] is illustrative. There, the arbitration provision was limited to disputes "*as to the meaning or interpretation of this Agreement.*"[69] The

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may be enforced); H.I.G. Capital Mgmt., Inc. v. Ligator, 650 N.Y.S.2d 124, 124, 233 A.D.2d 271, 271 (N.Y. App. Div. 1996); Ambulatory Care Review Servs. v. Blue Cross & Blue Shield of Minn., 131 Ohio App. 3d 450, 457, 722 N.E.2d 1040, 1045 (Ct. App. 1998) (stating that two marketing firms which had not entered into an arbitration agreement could not be required to arbitrate disputes involving the agreement); South Carolina Pub. Serv. Auth. v. Great W. Coal, Inc., 312 S.C. 559, 563, 437 S.E.2d 22, 25 (1993); Dane County v. Dane County Union Local 65, 210 Wis. 2d 267, 279, 565 N.W.2d 540, 545 (Ct. App. 1997) (stating that "arbitration is based upon the agreement of the parties involved to submit certain claims and issues to arbitration").

[64] 727 A.2d 286, 293 (Del. 1999).

[65] *Elf Atochem N. Am., Inc.*, 727 A.2d at 293 (quoting DEL. CODE ANN. tit. 6, § 18-101(7) (1974)).

[66] *Id.*

[67] Selma Med. Ctr., Inc. v. Manayan, 733 So. 2d 382, 385 (Ala. 1999).

[68] 739 So. 2d 1082 (Ala. 1999).

[69] *American Bankers*, 739 So. 2d at 1083 (emphasis added).

court rejected an attempt to enforce arbitration of the plaintiff's *fraud* cause of action upon finding that it was not an issue contemplated by what the parties agreed to arbitrate.[70]

On the other hand, in *Selma Medical Center, Inc. v. Manayan*, the court held that a provision applying to "any dispute *[that] shall arise concerning any aspect of this Agreement*" *was* broad enough to cover a claim of fraud in the inducement.[71]

Other courts have likewise examined whether a party's claim is subject to an arbitration provision by contemplating the scope of the provision.[72]

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[70] *Id.* at 1084.

[71] 733 So. 2d 382, 384 (Ala. 1999) (emphasis added).

[72] *See* Security Watch, Inc. v. Sentinel Sys., Inc., 176 F.3d 369, 373, 374 (6th Cir. 1999) (holding arbitration provision to after-arising claims not applicable to pre-agreement claim); Univ. of Alaska v. Modern Constr., Inc., 522 P.2d 1132, 1138 (Alaska 1974); Smith v. Logan, 166 Ariz. 1, 799 P.2d 1378, 1379 (Ct. App. 1990); Gross v. Recabaren, 206 Cal. App. 3d 771, 777, 253 Cal. Rptr. 820, 824 (Ct. App. 1988) (stating that court should attempt to give effect to the scope of arbitration agreed to by the parties); A. Sangivanni & Sons v. F.M. Floryan & Co., 158 Conn. 467, 473, 262 A.2d 159, 163 (1969); Int'l Marine Holdings, Inc. v. Stauff, 44 Conn. App. 664, 668, 691 A.2d 1117, 1120 (Ct. App. 1997); Anadarko Petroleum Corp. v. Panhandle E. Corp., 1987 WL 18103, at *3 (Del. Ch. Oct. 6, 1987) (The court determined that the plaintiff's economic coercion claim fell within the arbitration provision in a gas purchase contract containing the following language: "If and whenever any controversy shall arise . . . the same shall be submitted for determination by a board of arbitrators."); Seifert v. U.S. Home Corp., 750 So. 2d 633, 638 (Fla. 1999); Banderas v. Doman, 224 Ga. App. 198, 201, 480 S.E.2d 252, 255 (Ct. App.), *cert. denied*, 552 U.S. 864 (1997), *reh'g denied*, 522 U.S. 1071 (1998); Brown v. KFC Nat'l Mgmt. Co., 82 Haw. 226, 232 n.7, 921 P.2d 146, 152 n.7 (1996) (noting that the mere existence of an arbitration agreement does not mean that parties must submit disputes which are outside the scope of the arbitration agreement); Gumprecht v. Doyle, 128 Idaho 242, 244, 912 P.2d 610, 612 (1995); Johnson v. Baumgardt, 216 Ill. App. 3d 550, 558, 159 Ill. Dec. 846, 851, 576 N.E.2d 515, 520 (App. Ct. 1991) (stating that "parties are bound to arbitrate only those issues which the clear language of the agreement, unextended by construction or implication, shows they have agreed to arbitrate"); Int'l Creative Mgmt., Inc. v. D & R Enm't Co., 670 N.E.2d 1305, 1310 (Ind. Ct. App. 1996); Iowa v. State Police Officers Council, 525 N.W.2d 834, 836 (Iowa 1994); Kansas Gas & Elec. Co. v. Kansas Power & Light Co., 12 Kan. App. 2d 546, 551, 751 P.2d 146, 150 (Ct. App. 1988); Collins v. Prudential Ins. Co. of Am., 752 So. 2d 825, 831 (La. 2000); Granger N., Inc. v. Cianchette, 572 A.2d 130, 138 (Me. 1990); Fisher v. Merchants' Ins. Co., 95 Me. 486, 489, 50 A. 282, 283 (1901) (stating that "a stipulation in a contract providing for the settlement by arbitration of all controversies and disputes that might subsequently arise between the parties is invalid because its effect would be to oust the courts of their jurisdiction"); Contract Constr., Inc. v. Power Tech. Ctr. Ltd. P'ship, 100 Md. App. 173, 178, 640 A.2d

In re Marriage of Popack, the court considered the scope of an arbitration agreement that governed marital disputes between the parties.[71] The court

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251, 253 (Ct. Spec. App. 1994); Wilson v. McGrow, Pridgeon & Co., 298 Md. 66, 79, 467 A.2d 1025, 1031 (1983); Geller v. Temple B'Nai Abraham, 11 Mass. App. Ct. 917, 918, 415 N.E.2d 246, 247 (Ct. App. 1981); DeCaminada v. Coopers & Lybrand, L.L.P., 232 Mich. App. 492, 496, 591 N.W.2d 364, 366 (1998); Minnesota Teamsters Pub. & Law Enforcement Employees' Union, Local #320 v. County of St. Louis, 611 N.W.2d 355, 358 (Minn. Ct. App. 2000); Hayob v. Osborne, 992 S.W.2d 265, 269 (Mo. Ct. App.), *reh'g denied* (June 1, 1999); Smith Barney, Inc. v. Painters Local Union No. 109 Pension Fund, 254 Neb. 758, 764, 579 N.W.2d 518, 522 (1998); Kindred v. Second Judicial Dist. Court of the State of Nev., 996 P.2d 903, 907 (Nev. 2000); Demers Nursing Home, Inc. v. R.C. Foss & Son, Inc., 122 N.H. 757, 760, 449 A.2d 1231, 1232-33 (1982); Quigley v. KPMG Peat Marwick, LLP, 330 N.J. Super. 252, 274-75, 749 A.2d 405, 417 (N.J. Super. App. 2000) (holding that "the trial court erred in ordering arbitration, since the arbitration clause . . . did not include claims of discriminatory discharge"); Bleunner v. Parkway Ins. Co., 277 N.J. Super. 378, 403, 649 A.2d 913, 926 (1994); Yale Materials Handling Corp. v. White Storage & Retrieval Sys., Inc., 240 N.J. Super. 370, 374, 573 A.2d 484, 486 (N.J. Super. Ct. App. Div. 1990); Monette v. Tinsley, 126 N.M. 748, 753, 975 P.2d 361, 366 (1999); ACRS, Inc. v. Blue Cross & Blue Shield of Minn., 131 Ohio App. 3d 450, 456, 722 N.E.2d 1040, 1044 (Ct. App. 1998); Pierman v. Green Tree Fin. Servicing Corp., 933 P.2d 955, 956 (Okla. Ct. App. 1997); Snow Mountain Pine, Ltd. v. Tecton Laminates Corp., 126 Or. App. 523, 589, 869 P.2d 369, 372 (Ct. App. 1994); Midomo Co. v. Presbyterian Hous. Dev. Co., 739 A.2d 180, 190 (Pa. Super. Ct. 1999) (holding that arbitration clause in lease agreement for proposed personal care facility "does not apply to tort claims, because tort claims are neither specifically nor implicitly delineated in [the arbitration clause,] which limits itself to disputes regarding specific aspects of the [l]ease [a]greement only, [and thus,] the arbitration provision does not apply to [fraudulent and negligent misrepresentations claims or to claim of interference with contract]"); Hazleton Area Sch. Dist. v. Bosak, 671 A.2d 277, 282-83 (Pa. Commw. Ct. 1996) (finding that the school district's complaint against an architect and engineer did not involve a breach of contract but rather professional negligence, and since the arbitration provision stated that "claims or disputes arising out of or relating to the agreement, or its breach, shall be decided by arbitration," then the trial court was correct in denying the motion to compel arbitration); S.C. Pub. Serv. Auth. v. Great W. Coal, Inc., 312 S.C. 559, 563, 437 S.E.2d 22, 25 (1993); Anderson County v. Architectural Techniques Corp., 1993 WL 346473, at *4 (Ct. App. Sept. 9, 1993); *In re* H.E. Butt Grocery Co., 17 S.W.3d 360, 366-67 (Tex. Ct. App.), *mandamus denied*, (June 1, 2000); McCoy v. Blue Cross & Blue Shield of Utah, 980 P.2d 694, 697 (Ct. App.), *petition granted*, 994 P.2d 1271 (Utah 1999); Doyle & Russell, Inc. v. Roanoke Hosp. Ass'n, 213 Va. 489, 494, 193 S.E.2d 662, 666 (1973); Kimberly Area Sch. Dist. v. Zdanovec, 222 Wis. 2d 27, 37, 586 N.W.2d 41, 46 (Ct. App. 1998), *rev. denied*, 590 N.W.2d 490 (1999); Haynes v. Kuder, 591 A.2d 1286, 1289 (D.C. 1991).

[71] 998 P.2d 464, 466-67 (Colo. Ct. App. 2000) (concluding that the subject arbitration agreement was not limited to the prior legal proceedings and included the present proceedings).

stated that the scope of an arbitration agreement must be determined by "examin[ing] the wording and must ascertain and give effect to the mutual intent of the parties as well as the subject matter and purposes to be accomplished by the agreement."[74]

By way of contrast, when the court in *Mugnano-Bornstein v. Crowell* held that the breadth of an arbitration clause covered the party's dispute, it reasoned that just because "an arbitration agreement is comprehensive in scope does not render it invalid. Rather, where an arbitration clause is broad . . ., 'there is a strong presumption of arbitrability.'"[75] The court further stated that an arbitration agreement need not "contain a list of the specific claims or causes of action which are subject to arbitration in order to be enforceable."[76]

G. Consumer Warranty?

Once counsel passes the initial questions, the next potentially dispositive issue is whether the arbitration provision is contained in a document evidencing a written consumer warranty. Provisions in the Magnuson-Moss Warranty Act[77] and corresponding regulations issued by the Federal Trade Commission pursuant to that Act specify that any alternative dispute resolution offered by a written warrantor *shall be non-binding*.[78] Therefore, if a binding arbitration requirement conflicts with the federal requirement in the Magnuson-Moss Warranty Act, any arbitration of the warranty claim must be non-binding.[79]

For example, in *Southern Energy Homes, Inc. v. Lee*, the Alabama Supreme Court ruled that an arbitration provision in a written warranty

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[74] *In re* Marriage of Popack, 998 P.2d at 467.

[75] 42 Mass. App. Ct. 347, 353, 677 N.E.2d 242, 246 (Mass. App. Ct. 1997) (citation omitted).

[76] *Mugnano-Bornstein*, 677 N.E.2d at 247.

[77] 15 U.S.C. § 2301 (1997). *See generally* Jean Braucher, *An Informal Resolution Model of Consumer Product Warranty Law*, 1985 WIS. L. REV. 1405 (discussing dispute resolution alternatives in consumer product warranty context).

[78] Informal Dispute Settlement Procedures, 16 C.F.R. § 703 (2000).

[79] 15 U.S.C. § 2301 (1997).

was void because it violated the Magnuson-Moss Warranty Act.[80] Because the provision was void, the court concluded that the consumer could not be forced to arbitrate even non-warranty claims that the consumer had against the warrantor.[81] However, in a narrow five-to-four holding in *Southern Energy Homes, Inc. v. Ard*, the same court subsequently overruled *Lee* and held that the Magnuson-Moss Warranty Act does not invalidate arbitration provisions in a written warranty.[82]

Interestingly, shortly before Alabama released the second *Southern Energy* case, a Texas Court of Appeals held that an agreement compelling arbitration of a written warranty claim was invalid and unenforceable. The court reasoned that the FAA was superseded by the Magnuson-Moss Warranty Act's provisions prohibiting binding arbitration.[83] The Texas court agreed with the Alabama Supreme Court's reasoning in the first *Southern Energy* case, and held that the Magnuson-Moss Warranty Act "clearly reflects an intent by Congress to prohibit the use of binding arbitration clauses in written warranties."[84]

Moreover, the District Court for the Middle District of Alabama, in *Wilson v. Waverlee Homes, Inc.*, held not only that the Magnuson-Moss Warranty Act prohibits binding arbitration clauses in consumer warranties, but also that a warrantor may not invoke an arbitration clause in a retail sales contract.[85] The court found that allowing the warrantor to invoke the seller's arbitration clause would circumvent the prohibition in the Magnuson-Moss Warranty Act.[86]

The narrow reversal of the Alabama Supreme Court's stance in the second *Southern Energy* case is especially curious in light of what three courts–two judges in the Middle District of Alabama and the Texas Court

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[80] 732 So. 2d 994, 998 (Ala. 1999), *overruled by* Southern Energy Homes, Inc. v. Ard, No. 1971998, 2000 WL 709500 (Ala. June 2, 2000).

[81] *Southern Energy Homes, Inc.*, 732 So. 2d at 999.

[82] 2000 WL 709500, at *4 (Ala. 2000).

[83] *In re* Van Blarcum, 19 S.W.3d 484, 491 (Tex. App. 2000).

[84] *Id.*

[85] 954 F. Supp. 1530, 1537 (M.D. Ala.), *aff'd*, 127 F.3d 40 (11th Cir. 1997).

[86] *Wilson*, 954 F. Supp. at 1537; *see also* Boyd v. Homes of Legend, Inc., 981 F. Supp. 1423, 1435-36 (M.D. Ala. 1997); Rhode v. E & T Investments, Inc., 6 F. Supp. 2d 1322, 1331 (M.D. Ala. 1998)

of Appeals–have held. Furthermore, it seems especially odd that, after the federal courts have held that the FAA does not preempt Alabama Code section 8-1-41(3),[87] the Alabama Supreme Court would still find federal preemption of Alabama law. Perhaps in the next case, the Alabama Supreme Court will agree with the decisions of the other courts that have considered the subject, and reinstate its original view that arbitration provisions violate the Magnuson-Moss Warranty Act. It is not known how the United States Supreme Court would rule on this issue, because none of these cases have been presented for certiorari review. Therefore, although the current rule in Alabama state courts allows arbitration clauses in warranties, the United States Supreme Court could reinstate the first *Southern Energy* rule by holding that the Magnuson-Moss Warranty Act does invalidate arbitration provisions in a written warranty.

H. Conform with Due Process Protocol?

The next issue for review concerns whether a court may deem the arbitration provision unenforceable because of a failure to comply with the American Arbitration Association's Consumer Due Process Protocol.[88] In *Ex parte Napier*, the Alabama Supreme Court cited the Consumer Due Process Protocol with approval, thereby impliedly suggesting that arbitration provisions subject to AAA's rules must either conform with the protocol or else run the risk of being deemed unenforceable.[89]

By way of background, this "protocol" is the product of an Advisory Committee composed of both consumer lawyers and business lawyers who recommended to the American Arbitration Association that it adopt

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[87] ALA. CODE § 8-1-41(3) (1993).

[88] Virtually all the details concerning the costs, location of proceedings, selection of arbitrators, etc., are available on the AAA's Web site. *American Arbitration Association, Dispute Resolution Services Worldwide*, *at* http://www.adr.org (last visited Nov. 17, 2000).

[89] 723 So. 2d 49, 52 n.2 (Ala. 1998).

a principle called Principle Eleven "special provisions relating to binding arbitration."[90] The provisions state:

> Consumers should be given:
> a. clear and adequate notice of the arbitration provision and its consequences, including a statement of its mandatory or optional character;
> b. reasonable access to information regarding the arbitration process, including basic distinctions between arbitration and court proceedings, related costs, and advice as to where they may obtain more complete information regarding arbitration procedures and arbitrator rosters;
> c. notice of the option to make use of applicable small claims court procedures as an alternative to binding arbitration in appropriate cases; and,
> d. a clear statement of the means by which the Consumer may exercise the option (if any) to submit disputes to arbitration or to court process.[91]

The Practical Suggestions section of the Reporter's Comments of the Advisory Committee basically suggests that consumers should have clear and adequate notice of the arbitration provision as well as basic information regarding the arbitration process at the time they are called upon to consent to arbitration. The Practical Suggestions expressly state: "*In all cases, there should be some form of conspicuous notice of the agreement to arbitrate and its basic consequences.*"[92]

When commercial entities and insurers specify in their arbitration provisions that they are to be governed by American Arbitration Association rules, they necessarily are imposing upon themselves the standards required by AAA's due process protocol. Those entities should not be able to avoid the requirements of their own self-imposed standards of care. Accordingly, the prudent lawyer should compare the manner and method of obtaining the consumer's consent to arbitration against the requirements imposed by the AAA. If there is a significant discrepancy between the AAA's standards and the entities' own contract provisions or conduct, the lawyer may argue that the commercial entity or insurer failed to abide by its own self-imposed standards.

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[90] *American Arbitration Ass'n, Consumer Due Process Protocol, Principle 11: Agreements to Arbitrate*, at http://www.adr.org (last visited Nov. 17, 2000).

[91] *Id.*

[92] *Id.* (emphasis added).

Other states have also considered the notice requirements of an arbitration agreement.[93] In *Powertel, Inc. v. Bexley*, the court considered whether the plaintiff had received sufficient notice.[94] The plaintiff filed suit against Powertel on her behalf and as a representative of a class of persons whose long distance bills had been wrongfully computed.[95] The day after the plaintiff filed her complaint she received her monthly Powertel bill.[96] Included with the bill was a pamphlet that detailed the parties service agreement.[97] Powertel added a new provision to the contract.[98] The provision stated that the parties agreed that any "unresolved dispute controversy or claim" shall be settled by arbitration.[99]

The plaintiff continued her telephone service with Powertel for ten days after she received notice of the arbitration provision with her bill.[100] Powertel argued that the plaintiff's failure to cancel her service was an implied agreement to the arbitration provision and an agreement to dismiss her suit and resolve the underlying dispute with arbitration.[101] Rejecting Powertel's argument, the court stated:

> [W]e hold that the arbitration clause in this case is unconscionable and therefore unenforceable. It is an adhesion contract which not only provides for a method of dispute resolution but also dictates a one-sided waiver of important substantive rights. Moreover, we conclude that the arbitration

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[93] *See, e.g.*, Home Lumber Co. v. Appalachian Regional Hosps., Inc., 722 S.W.2d 912, 915 (Ky. Ct. App. 1987) (noting that "the usual test [for enforcing the arbitration clause in an agreement] is whether a reasonable person would have been aware of the clause under the circumstances, not whether the person signing the contract was actually and subjectively aware of the arbitration clause's presence"); Obstetrics & Gynecologists v. Pepper, 101 Nev. 105, 108, 693 P.2d 1259, 1261 (1985) (holding that medical clinic agreement requiring patients to submit all disputes to arbitration was unenforceable because the agreement was never explained to the patient); *In re* H.E. Butt Grocery Co., 17 S.W.3d 360, 372 (Tex. App. 2000).

[94] 743 So. 2d 570 (Fla. Dist. Ct. App. 1999).

[95] *Bexley*, 743 So. 2d at 572.

[96] *Id.*

[97] *Id.*

[98] *Id.*

[99] *Id.*

[100] *Bexley*, 743 So. 2d at 572.

[101] *Id.* at 572-73.

> clause cannot apply retroactively to the pending lawsuit. [The plaintiff] had filed the suit before she was even aware of Powertel's intention to modify the contract to require arbitration. Although the arbitration clause refers to unresolved disputes, its language is far too general to constitute a voluntary dismissal of a dispute which had by then ripened into a lawsuit.[102]

In *McCoy v. Blue Cross & Blue Shield of Utah*, the court considered whether the defendant had proffered sufficient evidence to show that it complied with notice requirements concerning its arbitration agreement.[103] The defendant established only that the plaintiff "would have" received the notice because the plaintiff's name was one of many included on magnetic tape.[104] The court found the evidence "insufficient to establish compliance with the plan's notice provision."[105]

I. Elements of Unconscionability?

The next step is to examine all the facts and circumstances surrounding the relative sophistication, financial strength, and bargaining power of the parties in order to determine whether the agreement is so unconscionable that it should be deemed unenforceable as a matter of law.

The doctrine of unconscionability is codified in Alabama's version of the Uniform Commercial Code in the Code of Alabama, which states:

> If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.[106]

A similar definition of unconscionability is found in Alabama's Consumer Credit Act:

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[102] *Id.* at 574.

[103] 980 P.2d 694, 696 (Utah Ct. App. 1999).

[104] *McCoy*, 980 P.2d at 697.

[105] *Id.* at 698.

[106] ALA. CODE § 7-2-302 (1975).

> With respect to a consumer credit transaction, if the court as a matter of law finds the contract or any provision of the contract to have been unconscionable at the time it was made, the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable provision, or it may so limit the application of any unconscionable provision as to avoid any unconscionable result.[107]

Alabama law does not provide an explicit standard for determining the unconscionability of a contract or contractual provision, but the Alabama Supreme Court *has* articulated several factors in determining unconscionability. In *Layne v. Garner* the court considered the following factors:

> In addition to finding that one party was unsophisticated and/or uneducated, a court should ask (1) whether there was an absence of meaningful choice on one party's part, (2) whether the contractual terms are unreasonably favorable to one party, (3) whether there was unequal bargaining power among the parties, and (4) whether there were oppressive, one-sided or patently unfair terms in the contract.[108]

More recently, in *Ex parte Dan Tucker Auto Sales, Inc.*, a concurring opinion by Justice Lyons applied the same four-factor test in determining the unconscionability of an agreement.[109] Justice Lyons noted that

> unconscionability, under general principles of Alabama law, can be reduced to a four-part test: (1) whether there is an absence of meaningful choice on one party's part; (2) whether the contractual terms are unreasonably unfavorable to one party; (3) whether there was unequal bargaining power between the parties; and (4) whether the contract contained oppressive, one-sided or patently unfair terms.
>
> I believe that a showing of financial hardship, lack of choice, and one-sidedness could, in a proper case, lead to a finding of unconscionability and a concomitant holding of unenforceability of an arbitration agreement that would not conflict with governing federal law.[110]

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[107] *Id.* § 5-19-16.

[108] 612 So. 2d 404, 408 (Ala. 1992).

[109] 718 So. 2d 33, 43 (Ala. 1998) (Lyons, J., concurring).

[110] *Ex parte Dan Tucker Auto Sales, Inc.*, 718 So. 2d at 43 (citation omitted).

In *Ex parte Napier*, the Court listed other factors that might be "germane to a determination of unconscionability," including:

> [A] refusal of [a plaintiff's] request for assistance after she had notified someone that she was unable to see or to understand [the arbitration clause]; [a plaintiff's] inability to obtain the product made the basis of this action from this seller, or from another source, without having to sign an arbitration clause; the oppressiveness or unfairness of the mechanism of arbitration; or the fairness of a discount or other *quid pro quo* in exchange for [a plaintiff] accepting an arbitration agreement.[111]

Still further, in *Ex parte Parker*, the court stated that "lack of mutuality of a remedy can be one factor, along with others, that a court may consider in determining whether an arbitration clause is unconscionable."[112] The reader should note, however, that in *Ex parte McNaughton* the court held that the absence of a mutuality of remedy, standing alone, does not render an arbitration provision unconscionable.[113]

So, what additional factors should counsel look for when attempting to establish that the agreement would be unconscionable if enforced against your client? Counsel should scrutinize each of the following:

1. Lack of meaningful bargaining power and whether the contract is adhesive;
2. Excessive or unreasonable costs to invoke arbitration (for example, AAA's Construction Industry Dispute Resolution Rules) and determine whether prohibitive costs to invoke arbitration are such that they impose a financial hardship);
3. Hardship imposed by location of arbitration proceedings;
4. Hardship caused by selection or bias of the arbitrator;
5. Deprivation of adequate remedies (*i.e.*, no class actions; thwarting of right to rely upon state or federal statutory remedies like Deceptive Trade Practices Act, Title VII, ADEA, etc.);
6. Was the plaintiff forced to sign the arbitration clause under duress (*e.g.*, at a hospital as a condition of undergoing emergency surgery)?

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[111] 723 So. 2d 49, 52 (Ala. 1998) (emphasis added).

[112] 730 So. 2d 168, 171 (Ala. 1999).

[113] 728 So. 2d 592, 598-99 (Ala. 1998).

7. Was the consumer given an adequate opportunity to read and understand the arbitration provision? Were their questions concerning arbitration fully and truthfully answered?[114]

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[114] The following cases discuss reasons why courts have found arbitration provisions unconscionable or unenforceable: Randolph v. Green Tree Fin. Corp. 178 F.3d 1149 (11th Cir. 1999), *cert. granted by* Green Tree Fin. Corp.-Ala. v. Randolph, 120 S. Ct. 1552 (2000) (serious concerns with respect to filing fees, arbitrators' costs, and other arbitration expenses rendered arbitration clause unenforceable); Hooters of Am. v. Phillips, 173 F.3d 933 (4th Cir. 1999) (bias); Shankle v. B-G Maint. Mgmt. of Colo., Inc., 163 F.3d 1230 (10th Cir. 1999) (holding that barriers of access to effective alternative forum for resolving statutory claims may render arbitration provision unenforceable); Paladino v. Avnet Computer Techs., Inc., 134 F.3d 1054, 1062 (11th Cir. 1998) (forcing a plaintiff to bear the brunt of "hefty" arbitration costs and "steep filing fees" to vindicate statutory rights rendered arbitration provision unenforceable); Baron v. Best Buy Co., 75 F. Supp. 2d 1368 (S.D. Fla. 1998) (bias); Knepp v. Credit Acceptance Corp., 229 B.R. 821 (N.D. Ala. 1999); Broemmer v. Abortion Serv. of Phoenix, Ltd., 173 Ariz. 148, 152-53, 840 P.2d 1013, 1017-18 (1992) (holding that an agreement to arbitrate was unenforceable because it was an adhesion contract, it was beyond the plaintiff's reasonable expectations, and it contained no conspicuous or explicit waiver of rights to jury trial); Kinny v. United Healthcare Servs., Inc., 70 Cal. App. 4th 1322, 1324, 83 Cal. Rptr. 2d 348, 350 (Ct. App. 1999) (holding that the arbitration agreement lacked mutuality, that the terms were unconscionable, and that the arbitration agreement was therefore unenforceable); Cheng-Canindin v. Renaissance Hotel Assocs., 50 Cal. App. 4th 676, 57 Cal. Rptr. 2d 867 (Ct. App. 1996) (bias); *In re* the Marriage of Yisroel Meir Popack & Chana Elka Popack, 998 P.2d 464, 468 (Colo. Ct. App. 2000) (discussing that arbitration agreements must be conscionable and entered into by parties voluntarily in order to be enforceable); Worldwide Ins. Group v. Klopp, 603 A.2d 788, 791 (Del. 1992) (holding that an arbitration provision permitting either party to demand a trial *de novo* in the event that the arbitration award exceeds a stated amount is against public policy and unenforceable); Graham v. State Farm Mut. Auto. Ins. Co., 565 A.2d 908, 912 (Del. 1989) ("A contract of adhesion may be declared unenforceable, in whole or in part, if its terms are unconscionable within the meaning of [6 DEL. CODE ANN. tit. 2, § 302 (1999)]. Nevertheless, mere disparity between the bargaining power of parties to a contract will not support a finding of unconscionability. . . . For a contract clause to be unconscionable, its terms must be 'so one-sided as to be oppressive.'" (citations omitted)); Powertel, Inc. v. Bexley, 743 So. 2d 570, 575 (Fla. Dist. Ct. App. 1999) (noting that "[o]ne of the hallmarks of procedural unconscionability is the absence of any meaningful choice on the part of the consumer" and also holding that limits on class actions lead to a finding of substantive unconscionability); Sun Drilling Prods. Corp. v. Rayborn, 703 So. 2d 818, 819 (La. Ct. App. 1997) (noting that, "[u]nder the Federal Arbitration Act, generally applicable state law contract defenses, such as fraud, duress or unconscionability, may be applied to invalidate arbitration agreements without contravening Section 2 of the Act"); Hannon v. Original Granite Aquatech Pools, Inc., 385 Mass. 813, 824, 434 N.E.2d 611, 618 (1982) (holding that "inclusion of a clause in a contract allowing one party, but not the other, to demand arbitration is not 'unconscionable' per se"); Ballard v. Southwest

J. Insurance Contract?

The next issue for examination concerns whether arbitration provisions contained within insurance contracts are valid and enforceable. In two plurality opinions, the Alabama Supreme Court rejected arguments that the McCarran-Ferguson Act[115] reverse-preempts the Federal Arbitration Act, thereby allowing the Alabama anti-arbitration statute[116] to preclude enforcement of an arbitration provision in an insurance policy. In *American Bankers Insurance Co. of Florida v. Crawford*[117] and *Ex parte Foster*,[118] Justice Lyons was recused and Justice England had not yet

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Detroit Hosp., 119 Mich. App. 814, 819, 327 N.W.2d 370, 372 (Ct. App. 1982) (holding that arbitration agreement was unenforceable because it did not allow for a fair and impartial tribunal and the circumstances under which it was executed rendered it unconscionable); Quigley v. KPMG Peat Marwick, L.L.P., 330 N.J. Super. 252, 266, 749 A.2d 405, 412-13 (N.J. Super. Ct. App. Div. 2000) (stating that employee's signature on arbitration agreements was not coerced); Myers v. Terminix Int'l Co., 91 Ohio Misc. 2d 41, 47, 697 N.E.2d 277, 280-81 (Com. Pl. 1998) (finding an arbitration clause that contained an undisclosed "filing fee" to be unconscionable and therefore invalid); Williams v. Aetna Fin. Co., 83 Ohio St. 3d 464, 700 N.E.2d 859 (1998) (lack of mutuality of remedy); Williams v. Gruntal & Co., 447 Pa. Super. 357, 361, 669 A.2d 387, 389 (Super. Ct. 1995) (stating that, "if the agreement to proceed in the alternative forum has the effect of seriously impairing the plaintiff's ability to pursue a cause of action, the court will strike such an agreement as unreasonable"); Zak v. Prudential Property & Cas. Ins. Co., 713 A.2d 681, 683-85 (Pa. Super. Ct. 1998) (stating that the clause in an automobile insurance policy making an arbitration award binding if it did not exceed the $15,000 limits of the Financial Responsibility Law was unconscionable and void as against public policy because the policy allowed the insurer to obtain a trial for arbitration award of any significant amount, but bound the insured to an award of nothing or a minuscule amount, and it implicated a provision of the Unfair Insurance Practices Act that prohibits attempts to compel settlements by publicizing a practice of appealing arbitration in favor of insureds); Buraczynski v. Eyring, 919 S.W.2d 314, 320 (Tenn. 1996) (reiterating that "[c]ourts will not enforce adhesion contracts which are *oppressive to the weaker party or which serve to limit the obligations and liability of* the stronger party"); *In re* H.E. Butt Grocery Co., 17 S.W.3d 360, 371 (Tex. App. 2000) (stating that, "[i]n determining whether arbitration is proper, the only question for the courts is procedural unconscionability, *i.e.*, whether the arbitration agreement was procured in an unconscionable manner"); Sosa v. Paulos, 924 P.2d 357 (Utah 1996).

[115] 15 U.S.C.A. § 1012(b) (West 1997).

[116] ALA. CODE § 8-1-41(3) (1975).

[117] 757 So. 2d 1125, 1136 (Ala. 1999).

[118] 758 So. 2d 516, 520 (Ala. 1999).

filled the vacancy left from Justice Kennedy's retirement.[119] The vote was four-to-three in both decisions, with Justices Houston, Cook, and Johnstone dissenting as to the McCarran-Ferguson issues.[120] If fewer justices than a majority of the nine-member court vote for an opinion, it does not become a binding precedent of the court.[121] Thus, if a similar case arises and Justices Lyons and England join the dissenters, a majority would accept the argument that the McCarran-Ferguson Act reverse-preempts the Federal Arbitration Act and allows the Alabama statute prohibiting specific enforcement of pre-dispute arbitration clauses to apply to insurance contracts.

Several states agree with the *Crawford* and *Foster* plurality decisions and hold that insurance contracts can be subject to arbitration.[122] In *Mercury Insurance Group v. Superior Court*, the California Supreme Court cited a statutory basis for subjecting an insurance contract to arbitration.[123] California Insurance Code section 11580.2 states that an auto liability insurance policy shall also "provide that the determination as to whether the insured shall be legally entitled to recover damages, and if so entitled, the amount thereof, shall be made by agreement between the insured and the insurer, or in the event of disagreement, by arbitration."[124]

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[119] *Crawford*, 757 So. 2d at 1136; *Foster*, 758 So. 2d at 520.

[120] *Crawford*, 757 So. 2d at 1136; *Foster*, 758 So. 2d at 520.

[121] Phoenix Ins. Co. v. Stuart, 289 Ala. 657, 664-65, 270 So. 2d 792, 798-99 (1972); *see* First Nat'l Bank of Mobile v. Bailes, 293 Ala. 474, 479, 306 So. 2d 227, 231 (1975).

[122] *See* Hillman v. Nationwide Mut. Fire Ins. Co., 855 P.2d 1321, 1326-27 (Alaska 1993); Fisher v. National Gen. Ins. Co., 192 Ariz. 366, 369, 965 P.2d 100, 103 (Ct. App. 1998); Mercury Ins. Group v. Superior Court, 19 Cal. 4th 332, 342, 965 P.2d 1178, 1182, 79 Cal. Rptr. 2d 308, 312-13 (1998); Merrill Lynch & Co. v. City of Waterbury, 34 Conn. App. 11, 13, 640 A.2d 122, 123 (Ct. App. 1994); Dancs v. Pacific Ins. Co., 78 Haw. 325, 335, 893 P.2d 176, 186 (1995); Cady v. Allstate Ins. Co., 113 Idaho 667, 669, 747 P.2d 76, 78 (Ct. App. 1987); Towe, Hester & Erwin, Inc. v. Kansas City Fire & Marine Ins. Co., 947 P.2d 594, 599 (Okla. Ct. App. 1997) (holding that "contracts between an insurer and its employees or independent contractors . . . are not excluded from application of the [FAA]"); Mendelson v. State Farm Mut. Auto. Ins. Co., 285 Or. 269, 274, 590 P.2d 726, 728-29 (1979).

[123] 19 Cal. 4th 332, 341, 965 P.2d 1178, 1182, 79 Cal. Rptr. 2d 308, 312 (1998).

[124] *Mercury Ins. Group*, 965 P.2d at 1182.

Other courts, however, have found that insurance contracts may not be subject to arbitration.[125] In contrast to the Alabama and California court decisions discussed above, in *Munich American Reinsurance Co. v. Crawford*, the court held that a district court had no power to compel arbitration because the FAA is reverse preempted under the McCarran-Ferguson Act.[126] The court reasoned that, "by operation of the McCarran-Ferguson Act, a federal act that permits states to exert broad power over the insurance industry, state laws regulating the business of insurance may suspend federal remedies based on conflicting federal statutes–here, the FAA."[127]

K. Evidence of Fraud?

Finally, you should consider whether the facts suggest fraud in the inducement or execution of the contract. Bear in mind that, if you allege fraud in the inducement as to the overall contract, Alabama law holds that

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[125] Mutual Reinsurance Bureau v. Great Plains Mut. Ins. Co., 969 F.2d 931 (10th Cir.), *cert. denied*, 506 U.S. 1001 (1992); Quakenbush v. Allstate Ins. Co., 121 F.3d 1372 (9th Cir. 1997); Friday v. Trinity Universal, 22 Kan. App. 2d 935, 940, 924 P.2d 1284, 1287 (Ct. App. 1996) (holding that the McCarran-Ferguson Act prevents the FAA from preempting provisions in the KUAA; therefore, arbitration clauses in insurance contracts can be inapplicable); Buck Run Baptist Church, Inc. v. Cumberland Surety Ins. Co., 983 S.W.2d 501, 504 (Ky. 1998) (explaining that, "[i]n the case of the ordinary insurance contract between a policyholder and an insurance company, it can readily be understood why the legislature exempted future disputes from being subjected to compulsory arbitration because such contracts are contracts of adhesion to which the insured parties have limited bargaining power"); *see also* Young v. Security Union Title Ins. Co., 292 Mont. 310, 316, 971 P.2d 1233, 1236 (1988) (holding that arbitration provisions in insurance policies are invalid and unenforceable); Rawlings v. Amco Ins. Co., 231 Neb. 874, 875, 438 N.W.2d 769, 770 (1989) (finding that "arbitration agreements entered into before a dispute arises which purport to deny the parties the right to resort to the courts nonetheless oust the courts of their jurisdiction and are thus against public policy and therefore void and unenforceable"); *In re* Union Indem. Ins. Co., 137 Misc. 2d 575, 580, 521 N.Y.S.2d 617, 620 (1987); Little v. Allstate Ins. Co., 167 Vt. 171, 174, 705 A.2d 538, 540 (1997) (discussing whether the FAA preempts the Vermont Arbitration Act and makes irrevocable an agreement to arbitrate uninsured motorist coverage dispute).

[126] 141 F.3d 585, 596 (5th Cir. 1998).

[127] *Munich*, 141 F.3d at 596.

the issue would be resolved by the arbitrator.[128] On the other hand, were you to allege that there was fraud solely with respect to obtaining the arbitration provision, that issue would be decided by the court.[129]

The Alabama Supreme Court recently gave a broad hint that it would be receptive to fraud allegations:

> The method adopted by [Blue Cross] to obtain the waiver of a policyholder's constitutional right to a jury trial does cause us some concern, however. If the evidence had presented a fact question as to whether Clark had been notified of the amendment; or had presented a fact question as to whether, if properly notified, she would have been unable to understand that she was agreeing to be bound by the arbitration provision; or had suggested fraud in the inducement, duress, or unconscionability, then Clark would be entitled to the writ and the issue of arbitrability would be determined by a jury.[130]

Similarly, in a recent special concurrence, Justice Johnstone distinguished fraud in the inducement from fraud in the execution, and notes that the court has not considered whether an assertion of fraud in the execution of the entire contract is grounds for denying a motion to compel arbitration.[131]

The majority of courts deciding the issue have held that claims of fraud in the inducement of the whole contract are subject to arbitration, but claims of fraud against the arbitration clause itself are resolved by the courts.[132] For example, the court's holding in *Wilharm v. M.J. Construc*

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[128] *See* Rollins, Inc. v. Foster, 991 F. Supp. 1426, 1433 (M.D. Ala. 1998); Brilliam Homes, Ltd. v. Lind, 722 So. 2d 753, 754 (Ala. 1998).

[129] *See* Liberty Fin., Inc. v. Carson, No. CV-98-72, 2000 WL 1074072, at *3 (Ala. Aug. 4, 2000) (finding that the alleged fraud did not come within the scope of the items to be decided by arbitration as outlined in the agreement).

[130] *Ex parte* Shelton, 738 So. 2d 864, 870-71 (Ala. 1999).

[131] Quality Truck & Auto Sales, Inc. v. Yassine, 730 So. 2d 1164, 1170-71 (Ala. 1999) (Johnstone, J., concurring specially).

[132] *See* Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 404, 87 S. Ct. 1801, 1806, 18 L. Ed. 2d 1270, 1277 (1967) (holding that "a federal court may consider only issues relating to the making and performance of the agreement to arbitrate"). Smith v. Logan, 166 Ariz. 1, 2, 799 P.2d 1378, 1379 (Ariz. Ct. App. 1990) (stating that fraudulent inducement claim was arbitrable, absent a claim that the arbitration clause itself was fraudulently induced); Rosenthal v. Great W. Fin. Sec. Corp., 14 Cal. 4th 394, 416, 926 P.2d 1061, 1074 (1996) (stating that claims of fraud in the execution are not arbitrable, but claims of fraud in the inducement are arbitrable); National Camera, Inc.

tion Co.[133] is illustrative. There the dispute arose from a contract to build

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v. Love, 644 P.2d 94, 95 (Colo. Ct. App. 1982) (noting that claims of fraud in the inducement of the contract, as opposed to the arbitration clause itself, fall under the contract provision for arbitration); A. Sangivanni & Sons v. F. M. Floryan & Co., 158 Conn. 467, 472, 262 A.2d 159, 162-63 (1969) (holding that "[t]he mere fact that the plaintiff will or may claim fraudulent inducement does not . . . give the defendants any right to refuse to arbitrate a 'disagreement pertaining to' the contract" when the arbitration agreement provides for arbitration "[i]n case of any disagreement pertaining to the contract"); Anadarko Petroleum Corp. v. Panhandle E. Corp., 1987 WL 13520, at *11 (Del. Ch. July 7, 1987) (stating that, "where there is no claim of fraud in the inducement of the arbitration clause itself, but only fraud in the inducement of the contract as a whole, the arbitration clause is separable and the fraudulent inducement claim must be arbitrated"); Passerrello v. Robert L. Lipton, Inc., 690 So. 2d 610, 611 (Fla. Dist. Ct. App. 1997) (noting, "[i]t is well settled, however, that where the entire agreement is alleged to have been fraudulently induced, not the arbitration provision itself, the entire matter is to be resolved by arbitration"); Robinson-Humphrey Co. v. Williams, 193 Ga. App. 892, 894, 389 S.E.2d 345, 347 (Ct. App. 1989); Lee v. Heftel, 81 Haw. 1, 4, 911 P.2d 721, 724 (1996); Monical v. NCR Corp., 126 Ill. App. 3d 790, 791, 467 N.E.2d 644, 645, 81 Ill. Dec. 773, 774 (App. Ct. 1984); Goebel v. Blocks & Marbles Brand Toys, Inc., 568 N.E.2d 552, 557 (Ind. Ct. App. 1991); Darcres v. John Deere Ins. Co., 548 N.W.2d 576, 578 (Iowa 1996); Holmes v. Coverall North Am., Inc., 336 Md. 534, 546, 649 A.2d 365, 371 (1994); Meyer v. State Farm Fire & Cas. Co., 85 Md. App. 83, 91, 582 A.2d 275, 279 (Ct. Spec. App. 1990); Scanlon v. P & J Enter., Inc., 182 Mich. App. 347, 349, 451 N.W.2d 616, 617 (Ct. App. 1990); Downey v. Christensen, 251 Mont. 386, 391, 825 P.2d 557, 560 (1992); Sentry Sys., Inc. v. Guy, 98 Nev. 507, 509, 654 P.2d 1008, 1009 (1982) (reiterating that "a general claim of fraud in the inducement of a contract is arbitrable but a specific claim of fraud in the inducement of the arbitration clause itself is for the courts to decide"); Bleumer v. Parkway Ins. Co., 227 N.J. Super. 378, 402, 649 A.2d 913, 925 (N.J. Super. Ct. Law Div. 1994) (stating that "FAA policy favoring enforcement of arbitration agreements is so strong that claims of fraud in inducement of entire agreement, as distinguished from a claim of fraud in the inducement of the arbitration clause itself, must, under a broadly worded arbitration clause, be submitted to arbitrator for resolution unless expressly excluded by the arbitration clause"); *In re* Cullman Ventures, Inc., 252 A.D.2d 222, 228, 682 N.Y.S.2d 391, 395 (App. Div. 1998) (citations omitted) (stating that "[FAA] privately negotiated arbitration agreements are to be enforced according to their terms, absent an established ground for setting aside a contractual provision, such as fraud, duress, coercion or unconscionability"); Titus & McConomy v. Jalisi, 713 A.2d 646, 648 (Pa. Super. Ct. 1998) (determining that contract to arbitrate fee dispute between law firm and client was valid, enforceable, and irrevocable, in absence of proof of mutual mistake of fact, fraud in the inducement, or coercion in its securement); Anderson v. Erie Ins. Group, 384 Pa. Super. 387, 395, 558 A.2d 886, 890 (Super. Ct. 1989); South Carolina Pub. Serv. Auth. v. Great W. Coal, Inc., 312 S.C. 559, 562, 437 S.E.2d 22, 24 (1993); Berkley v. H & R Block E. Tax Servs., 2000 WL 548934, *3 (Tenn. Ct. App. May 4, 2000); *In re* Education Mgmt. Corp., 14 S.W.3d 418, 426 (Tex. Ct. App. 2000); Hercules & Co. v. Shama Rest. Corp., 613 A.2d 916, 919 (D.C. 1992).

[133] 118 Ohio App. 3d 531, 534-35, 693 N.E.2d 830, 833 (Ct. App. 1997) (per curiam).

a home.[134] The defendant sought to dismiss the case from court and additionally filed to stay the matter pending arbitration.[135] The defendant contended that the plaintiff failed to "challenge[] the validity of the arbitration clause itself."[136] The Ohio court agreed and stated that under the doctrine of severability, "a court is not permitted to consider a claim for rescission of an entire contract where there is no dispute as to the legitimacy of the arbitration clause."[137] The court further stated that "'in the face of a valid arbitration clause, questions regarding the validity of the entire contract must be decided in arbitration.'"[138]

A few states have held that claims of fraud in the inducement of the contract take the dispute out of arbitration.[139] In *Fouquette v. First American National Securities, Inc.*, for example, the court noted that under Minnesota law, "an arbitration clause is not severable from the entire contract."[140] The court further stated that "allegations of fraud

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[134] *Wilhelm*, 693 N.E.2d at 831.

[135] *Id.* at 832.

[136] *Id.*

[137] *Id.* (citing Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 404, 87 S. Ct. 1801, 1806, 18 L. Ed. 2d 1270, 1277-78 (1967)).

[138] *Id.* (quoting Weiss v. Voice/Fax Corp., 94 Ohio App. 3d 309, 313, 640 N.E.2d 875, 878 (Ct. App. 1994)).

[139] *See* Sun Drilling Prods. Corp. v. Rayborn , 703 So. 2d 818, 819 (La. Ct. App. 1997), *cert. denied*, 525 U.S. 1000 (1998) (stating "that the question of fraud in the inducement is not arbitrable"); Fouquette v. First Am. Nat'l Sec., Inc., 464 N.W.2d 760, 762-63 (Minn. Ct. App. 1991) (stating that "Minnesota law differs from federal law in that an arbitration clause is nonseverable," hence claims of fraud in the inducement are "not arbitrable"); Pittsfield Weaving Co. v. Geove Textiles, Inc., 121 N.H. 344, 346-47, 430 A.2d 638, 640 (1981) (stating that the applicable federal and state arbitration statutes "do not vest in arbitrators the historical jurisdiction possessed by the courts to determine fraud or unconscionability at the inception of a contract"); Shaw v. Kuhnel & Assocs., Inc., 102 N.M. 607, 609, 698 P.2d 880, 882 (1985) (stating that issues of fraud in the inducement were for the court to decide, and if no fraud is found then the remaining issues could be determined by the arbitrator); Shaffer v. Jeffery, 935 P.2d 910, 917 (Okla. 1996) (stating "that allegations of fraud in the inducement of an agreement to arbitrate must be resolved by the court prior to either compelling arbitration or dismissing the case")).

[140] 464 N.W.2d 760, 762 (Minn. Ct. App. 1991) (citing Cell v. Moore & Schley Sec. Corp., 449 N.W.2d 144, 149 n.4 (Minn. 1989)).

vitiating the primary subject matter of the contract will also vitiate the arbitration clause."[141]

L. Other Conceivable Defenses

Must a person be a licensed attorney to serve as an arbitrator? The Alabama Code defines the authority to practice law as follows:

> (a) Only such persons as are regularly licensed have authority to practice law.
> (b) For the purposes of this chapter, the practice of law is defined as follows: Whoever,
> . . . .
> (4) As a vocation, enforces, secures, settles, adjusts or compromises defaulted, controverted or disputed accounts, claims or demands between persons with neither of whom he is in privity or in the relation of employer and employee in the ordinary sense;
> is practicing law.[142]

Violation of Alabama Code section 34-3-6(b)(4) is a crime. The Alabama Code also provides for the unlawful practice of law as follows:

> Any person, firm or corporation who is not a regularly licensed attorney who does an act defined in this article to be an act of practicing law is guilty of a misdemeanor and, on conviction, must be punished as provided by law. Any person, firm or corporation who conspires with, aids and abets another person, firm or corporation in the commission of such misdemeanor must, on conviction, be punished as provided by law.[143]

In general most other states' statutes and court rules have not addressed whether arbitrators must be attorneys. Provisions in several states' arbitration acts permit parties to choose their own arbitrator, and if the parties fail to choose an arbitrator, the statutes generally provide that the

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[141] *Fouquette*, 464 N.W.2d at 762-63 (citations omitted).

[142] ALA. CODE § 34-3-6 (1975).

[143] *Id.* § 34-3-7.

state courts may establish rules for the selection of arbitrators.[144] For example, section 2A:23A-22(b) of the New Jersey Alternative Procedure for Dispute Resolution Act provides that,

> [i]f the parties fail to stipulate the number or names of the arbitrators, the arbitrators shall be selected, in accordance with rules of court adopted by the Supreme Court of New Jersey, from a list of arbitrators compiled by the assignment judge, to be comprised of *retired judges* and *qualified attorneys* in this State with at least seven years' negligence experience and recommended by the county or State bar association.[145]

New Jersey Rules of Courts for Civil Practice in the Superior Court, Tax Court, and Surrogate's Court echo the language of the state's arbitration act if the parties to a dispute fail to stipulate an arbitrator.[146] The Rule further provides that if the parties choose an arbitrator, the stipulated arbitrator is subject to approval of the Assignment Judge.[147]

Illinois' Code of Civil Procedure provides that "[t]he qualification and the method of appointment of arbitrators shall be prescribed by rule."[148]

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[144] *See* ALASKA STAT. § 09.43.030 (Michie 2000) (stating that arbitration agreements may stipulate a method of appointment of arbitrators; further providing that, if parties fail to stipulate an arbitrator, upon application the court may appoint an arbitrator); ALASKA STAT. § 09.43.200 (Michie 2000) (providing that arbitrators of small claims shall be members of the Alaska Bar or a court appointed arbitrator); HAW. REV. STAT. ANN. § 658-4 (Michie 2000) (providing that if parties fail to choose an arbitrator, upon application, the circuit court shall designate an arbitrator); HAW. REV. STAT. ANN. Rules of the Circuit Court of State of Hawaii Exhibit A--Hawaii Arbitration Rule 10 (Michie 2000) (providing that arbitrators in the circuit courts shall be licensed to practice law or must be able to "provide the Judicial Arbitration Commission with proof of equivalent qualifying experience"); MO. REV. STAT. § 435.360 (West 1992); N.H. REV. STAT. ANN. § 542.4 (1999) (providing that, if parties fail to select arbitrator upon application, court may appoint arbitrator); Florida Court Rules 11.010 (1999) (stating that "[a]rbitrators shall be members of The Florida Bar, except where otherwise agreed by the parties"); Georgia Rules of Court, Rule 6-304 (providing that arbitrators of fee disputes shall be members of the State Bar of Georgia); Mo. Spec. Rules of Practice for the District Courts, Fourth Judicial Circuit Rule 5.04(a) (providing that all arbitrators shall be attorneys); N.H. Rules of Superior Ct. Rule 170(d)(1) (stating that neutral arbitrators shall be attorneys approved by the court).

[145] N.J. STAT. ANN. § 2A:23A-22(b) (2000).

[146] N.J. Rules of Court Rule 4:21A-2(b) (1999).

[147] *Id.* 4:21A-2(a).

[148] 735 ILL. COMP. STAT. ANN. 5/2-1003A (West 1992).

The Illinois Supreme Court Rules and the Rules of the Circuit Court of Cook County both provide that arbitrators shall be "members of the bar engaged in the practice of law and retired judges within the circuit in which the court is situated."[149]

Accordingly, you may have a fruitful basis for excluding as an arbitrator anyone assigned to your dispute who is not a licensed attorney. This may very well foreclose appointments from AAA's "list of neutrals" when they are former insurance industry executives, building contractors, bankers, and the like.

IV. Conclusion

This Article is intended to serve two purposes. First it warns of the negative consequences of the onslaught of binding arbitration. Second, the Article arms the reader with many strategies to combat arbitration when it is not in the client's best interests. Until the United States Supreme Court retreats from *Allied-Bruce Terminix Cos. v. Dobson*[150] or Congress acts to protect the rights of consumers, members of the plaintiffs' trial bar must continue to fight binding arbitration with all the skill and zeal that may be brought to bear on this new injustice.

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[149] Ill. St. S. Ct. Rule 87(a); Rules of the Circuit Court of Cook County Rule 8.4(a)(4).

[150] 513 U.S. 265, 115 S. Ct. 834, 130 L. Ed. 2d 753 (1995).