

INTRODUCTION TO ARBITRATION

By Richard M. Borchers
President, Richard M. Borchers, P.C.

In order to be an effective advocate in arbitration, a lawyer must understand the system, its strengths and its weaknesses. As with a court, there may be jurisdictional limits that have an impact on how a case proceeds. It is crucial for a lawyer to know what jurisdictional limits may exist that would affect the client's case.

What is Arbitration? The United States Supreme Court noted in *United Steelworkers of America v. Warrior & Gulf Navigation Company*, 363 U.S. 574, 582 (1963) that "arbitration is a matter of contract." Parties to a contract can agree to resolve disputes privately through arbitration, rather than through the judicial system.

Public policy encourages resolution of disputes through arbitration. The United States Supreme Court has spoken clearly over the last two decades that arbitration is to be favored as a means of dispute resolution. *Circuit City Stores, Inc. v. Adams*, 532 U.S.105 (2001); *C & L Enterprises, Inc. v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 532, U.S. 411 (2001); *Green Tree Financial Corp. - Alabama v. Randolph*, 531 U.S. 70 (2000). These cases reflect the Court's longer-term view that arbitration is to be encouraged.

The State of Colorado, as well as most jurisdictions, has a long history of encouraging resolution of disputes through arbitration. *Hughley v. Rocky Mountain Health Maintenance Organization, Inc.*, 927 P.2d 1325 (Colo. 1996); *Lambdin v. District Court*, 903 P.2d 1126 (Colo. 1995); *Mountain Plains Constructors, Inc. v. Torrez*, 785 P.2d 928 (Colo. 1990); *Ezell v. Rocky Mountain Bean & Elevator Co.*, 76 Colo. 409, 232 P. 680 (1925); *Rains v. Foundation Health Systems Life & Health*, 23 P.3d 1249 (Colo. App. 2001). A valid and enforceable arbitration clause in a contract divests a trial court of jurisdiction to determine the merits of a dispute. *McCord v. Affinity Ins. Group, Inc.*, 13 P.3d 1224 (Colo.App.2000); *Gibson v. Wal-Mart Stores, Inc.*, 181 F.3d 1163 (10th Cir. 1999).

The Colorado General Assembly enacted the Uniform Arbitration Act in 1975. This act provided the framework for resolving initial disputes as to what issues are subject to arbitration for contracts entered into before August 4, 2004. It also provided for limited review by a court after completion of the arbitration.

In 2004, the Colorado General Assembly enacted a revised version of the Uniform Arbitration Act (UAA). This act applies to all arbitration agreements entered into on or after August 4, 2004. Parties to a contract entered into prior to August 4, 2004 may agree to application of the UAA to their contract.

Congress has enacted the Federal Arbitration Act (FAA). 9 U.S.C. § 1, et seq. The FAA is applicable to contracts that involve interstate commerce.

Examination of a Contractual Basis for Arbitration. Parties must agree to resolve disputes by arbitration. Absent such an agreement, there is no basis to compel arbitration.

A lawyer must allow the client to determine if an arbitration clause should be included in a contract. The parameters of the clause should spell out what disputes, if any, will be excluded from the clause. Otherwise, it is possible that a court may determine that all disputes are to be resolved by arbitration. *Eychner v. VanFleet*, 870 P.2d 486 (Colo.App.1993).

Contents of an Arbitration Clause: Any provision in a contract that requires arbitration of issues should be clear and delineate what the agreement is between the parties. As with other parts of the contract, the parties have great freedom to structure an arbitration clause in any way that they choose. Once that clause is agreed upon, it then becomes enforceable. The following are several things to consider when preparing an arbitration clause in a contract:

a. An arbitration clause can be extremely broad, providing submission to arbitration of all disputes. Make sure that this is what your client wants in lieu of court litigation. Second, make sure the client understands that there will be cost involved in arbitration.

b. Delineate what issues are to be arbitrated. The parties to a contract can limit the arbitration clause to only certain types of issues. If issues are limited, then an arbitrator is limited on what may be decided in the arbitration proceeding. If there is any ambiguity in the arbitration clause, it most probably will be resolved in favor of arbitration of the disputes, rather than litigation.

c. Delineate who is to determine what issues are to be arbitrated. The parties may agree that the arbitrator is to determine the arbitrability of an issue. Any such agreement must be stated with clear language and unmistakable evidence that this was the intent of the parties. *AT&T Technologies, Inc. v. Communications Workers*, 475 U.S. 643 (1986); *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995); *Galbraith v. Clark*, 122 P.3d 1061 (Colo.App. 2005). Absent a clear indication that an agreement exists for the arbitrator to determine what issues are subject to an arbitration clause, a court will be required to make such a determination. *Kaplan* at p. 945. (“We conclude that, because the Kaplans did not clearly agree to submit the question of arbitrability to arbitration, the Court of Appeals was correct in finding that the arbitrability of the Kaplan/First Options dispute was subject to independent review by the courts.”) Where the parties have agreed to allow the arbitrator to determine what will be subject to arbitration, then the parties will be bound by that. *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002).

d. The Colorado Court of Appeals has ruled in *Cabus v. Dairyland Insurance Company*, 656 P.2d 54, 56 (Colo.App. 1982) that “[g]enerally, arbitrators are not bound by either substantive or procedural rules of law, except as required under the terms of the arbitration agreement.” Include in the arbitration clause a choice of law provision, which may apply the law of a different state or jurisdiction. The parties may include also a provision that the arbitrator will be bound by decisions of the jurisdiction’s appellate courts.

e. The number of arbitrators will need to be spelled out in the arbitration clause. Absent such an agreement, it will be assumed that one arbitrator is to determine all issues.

f. The method for appointment of the arbitrator/s should be set forth. The UAA provides that the method selected by the parties for appointment of an arbitrator shall be followed. If that method cannot be followed, then a court shall appoint the arbitrator. *C.R.S. §13-22-211*. The parties have the right to set forth how the court shall appoint an arbitrator even if they cannot agree on someone to be appointed.

g. The original UAA in Colorado did not provide for pre-hearing discovery. If the parties desired such discovery, then a provision had to be set forth in the arbitration clause or agreement. *Rains v. Foundation Health Systems Life & Health, supra*. Under the present, an arbitrator may allow discovery to the extent deemed appropriate. *C.R.S. §13-22-217(3)*.

Making and Enforcing a Demand for Arbitration: Enforcement of an arbitration provision involves a two-step process. If a dispute has arisen under a contract, the aggrieved party must make a demand on the other party to arbitrate that dispute. If the other party refuses, then the aggrieved party must file an application in the appropriate district court for an order compelling arbitration. *C.R.S. § 13-22-207*.

A district court may not refuse to issue an order compelling arbitration on the basis that the claim lacks merit. *C.R.S. §13-22-207(4)*. The issue of whether merit exists is to be left to the arbitrator.

The UAA directs a district judge to summarily determine whether an issue is subject to arbitration. Please note that any order by the district court to deny arbitration or stay an arbitration is immediately appealable. *C.R.S. § 13-22-228(1)(a) & (b)*. An order compelling arbitration is *not* appealable immediately. *Gergel v. High View Homes, LLC* 58 P.3d 1132 (Colo.App. 2002).

Contesting an Application for Enforcement of an Arbitration Clause: *C.R.S. § 13-22-207* provides the mechanism for contesting the validity or extent of an arbitration clause in a contract. The UAA provides that the matter shall be determined summarily, and this places upon the party opposing arbitration a duty to convince the district court that the clause should not be enforced. A party opposing arbitration must be prepared to present evidence to the trial court at the hearing. *Estate of Grimm v. Evans*, 251 P.3d 514 (Colo.App. 2010); *E-21 Engineering, Inc. v. Steve Stock & Associates, Inc.*, 252 P.3d 36 (Colo.App. 2010); *see also, Keeton v. Wells Fargo Corporation*, 987 A.2d 1118 (D.C. 2010) (evidentiary hearing required to determine unconscionability of arbitration agreement); *Crystal Motor Car Company of Hernando, LLC v. Bailey*, 24 So.3d 789 (Fla.App 2009).

There are a number of ways to attack agreements to arbitrate. Please note that these attacks need to be made prior to the arbitration and to a district court if an application is made for an order compelling arbitration. It is not appropriate to proceed with the arbitration and then argue after the fact that the agreement to arbitrate was void. A court may hold that such acquiescence is a ratification of the arbitration and the party is bound by the result. However, there are ways to oppose an application for arbitration.

a. If no contract exists or there was no inclusion of an arbitration clause, then the application cannot be granted. The UAA and FAA require that any agreement be in writing to be enforceable. An oral agreement to arbitrate, absent some conduct thereafter, is not enforceable. The Colorado Court of Appeals has ruled that parties may by their actions form a contract that requires arbitration. *E-21 Engineering, Inc. v. Steve Stock & Associates, Inc.*, *supra*. (trial court directed to hold a hearing and determine if contract was created by the actions of the parties).

b. If a provision to arbitrate was added after the fact, then there must be clear evidence that both sides agreed to the change. A number of credit card companies have added arbitration provisions in existing contracts through use of bulk mailings. The burden is on the party claiming that a modification of an existing contract occurred and is now binding. *See e.g., McCoy v. Blue Cross Blue Shield of Utah*, 20 P.3d 901 (Utah 2001).

c. If the agreement to arbitrate was negotiated unconscionably, then a district court should not enforce the agreement. *See e.g., Sosa v. Paulos*, 924 P.2d 357 (Utah 1996); *Lhotka v. Geographic Expeditions, Inc.*, 104 Cal.Rptr.3d 844(Cal.App. 2010); *Gutierrez v. Autowest, Inc.*, 7Cal.Rptr.3d 267 (2003).

d. If the application to compel arbitration is too broad, then the district court can be requested to limit the arbitration to those issues or parties set forth in the agreement. For example, an agreement to arbitrate between two corporations would not necessarily include corporate officers in private capacities. *First Options of Chicago, Inc. v. Kaplan*, *supra*. If the agreement only relates to certain aspects of the contract, then other aspects cannot be compelled to be arbitrated. An example would be an agreement to arbitrate uninsured motorists claims, but the agreement would not extend to compel arbitration of personal property claims arising from an automobile accident.

e. If the overall agreement of the parties is void as against public policy, then the arbitration clause also would fail. *Dudding v. Norton Frickey & Associates*, 11 P.3d 441 (Colo. 2000). Please note that the FAA will affect contracts involving interstate commerce and may limit a public policy argument, unless it applies to all contracts, not just those involving arbitration. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996).

f. If the cost to arbitrate is excessive, then an argument can be made that the arbitration agreement is unenforceable. That argument was rejected on a *per se* basis by the United States Supreme Court in *Green Tree Financial Corporation-Alabama v. Randolph*, 531 U.S. 79 (2000). The Court left open the door for individual challenges. An example of an individual challenge that was successful is found in *Mendez v. Palm Harbor Homes, Inc.*, 45 P.3d 594 (Wash.App.2002). These cases reject a *per se* rule, and evidence could be presented that would preclude enforcement of an arbitration provision based on cost. *See also, State v. Matish*, 600 S.E. 2d 583 (W.V. 2004); *Leeman v. Cook's Pest Control, Inc.*, 902 S.2d 641 (Ala. 2004); *Olshan Foundation Repair Company v. Ayala*, 180 S.W.3d 212 (Tex.App. 2005).

The Tenth Circuit has ruled that arbitration clauses in employment contracts are unenforceable if the cost of the arbitration is to be shared by the employee. *Shankle v. B-G Maintenance Management of Colorado, Inc.*, 163 F.3d 1230 (10th Cir. 1999).

g. If the contract has a condition precedent before it becomes effective, then the question is whether that condition precedent has occurred. *All State Home Mortgage, Inc. v. Daniel*, 187 Md.App. 166, 977 A.2d 438 (2009)(contract required signatures of both parties to be effective and contract remained unsigned by one party).

h. If one party lacked capacity to enter into a contract, then the arbitration clause in the contract cannot be enforced. *In re Morgan Stanley & Co.*, 52 Tex.Sup.Ct. 1072, 293 S.W.2d 182 (2009).

Selecting an Arbitrator: Appointment of an arbitrator(s) is to be in conformity with the agreement of the parties. If the parties cannot agree upon an arbitrator or the agreed upon method cannot be followed, then an application may be made to an appropriate district court for appointment of an arbitrator. *C.R.S. §13-22-211*. Once the court appoints the arbitrator, that person then has all the powers conferred by the agreement of the parties.

The Arbitration Hearing: The arbitrator is given latitude to set a hearing upon at least thirty days notice served personally or by registered mail. Notice is not necessary if a party appears voluntarily for the hearing. *C.R.S. § 13-22-207*. The right to a hearing under the UAA may be waived by the parties to allow a summary resolution by the arbitrator. *Carson v. Painewebber, Inc.*, 62 P.3d 996 (Colo.App. 2002).

Under the UAA, an arbitrator may grant summary disposition of a claim, if requested by one of the parties to the arbitration. *C.R.S. § 13-22-215(2)*. The UAA provides that the arbitrator must order a hearing, unless summary disposition is granted. *C.R.S. § 13-22-215(3)*.

Arbitrators do have the authority to issue subpoenas for the hearing. *C.R.S. § 13-22-217*. Subpoenas may be enforced through an application to a district court. An arbitrator may permit a deposition of a witness who is not subject to a subpoena or is unable to attend the hearing.

The Arbitration Award: After completion of the arbitration hearing, an arbitrator is required to issue and sign a written award that resolves all pending claims. A copy of the award must then be served on the parties or mailed to them by the arbitrator. Mailing in Colorado must be by registered or certified mail.

There is no requirement by statute that the award detail any reasoning for the resolution of the dispute. If the parties want some detail, then that should be included in the arbitration agreement or relayed to the arbitrator.

Modification or Correction of an Award: A party may request that an arbitrator modify an award if there was a miscalculation of figures or description of the party or property; the award was imperfect as to form, or for purposes of clarifying the award. *C.R.S. §13-22-220*. Application must be made within twenty days of receipt or delivery of the arbitration award under the UAA.

Vacation of an Award: A party to the arbitration may seek a court order vacating the

award. In Colorado, such application under the UAA must be made within ninety days after receipt of the award. If fraud, corruption or other undue means are alleged, then the motion to vacate must be filed within thirty days after such grounds are known or should have been known.

A district court may correct an arbitration award for the following reasons: (1) there was an evident miscalculation of figures or an evident mistake in the description of any person or property; (2) the arbitrators awarded upon a matter not submitted to them and the award may be corrected without affecting the merits of the decision; or (3) the award was imperfect as to form, but did not affect the merits of the decision. *C.R.S. §13-22-215*.

In *C.R.S. §13-22-223*, the UAA provides the following grounds for vacating an award:

(1) Upon motion to the court by a party to an arbitration proceeding, the court shall vacate an award made in the arbitration proceeding if the court finds that:

(a) The award was procured by corruption, fraud, or other undue means;

(b) There was:

(i) Evident partiality by an arbitrator appointed as a neutral arbitrator;

(ii) Corruption by an arbitrator; or

(iii) Misconduct by an arbitrator prejudicing the rights of a party to the arbitration proceeding;

(c) An arbitrator refused to postpone the hearing upon showing of sufficient cause for postponement, refused to consider evidence material to the controversy, or otherwise conducted the hearing contrary to section 13-22-215, so as to prejudice substantially the rights of a party to the arbitration proceeding;

(d) An arbitrator exceeded the arbitrator's powers;

(e) There was no agreement to arbitrate, unless the person participated in the arbitration proceeding without raising the objection under section 13-22-215(3) no later than the beginning of the arbitration hearing; or

(f) The arbitration was conducted without proper notice of the initiation of an arbitration as required in section 13-22-209 so as to substantially prejudice the rights of a party to the arbitration proceeding.

(1.5) Notwithstanding the provisions of subsection (1) of this section, the fact that the relief was such that it could not or would not be granted by a court of law or equity is not grounds for vacating or refusing to confirm the award.

A motion to vacate under the UAA must be filed within ninety days of receipt of notice of the award. *C.R.S. § 13-22-223(2)*.

Confirmation and Entry of Judgment: An arbitration award may be confirmed by a district court upon application of the party receiving the award. *C.R.S. 13-22-222(1)*. Unless set aside or modified by a district court within the time limits set forth in UAA, the confirmed award becomes a judgment that may be enforced as any other judgment. *C.R.S. 13-22-225*.

Appeals: An appeal may be taken to the Colorado Court of Appeals or Colorado Supreme Court on the grounds set forth. *C.R.S. § 13-22-228*.

Injunctive Relief Prior to Arbitration Hearing: As to the 1975 UAA, the Colorado Supreme Court dealt with this issue in *Hughley v. Rocky Mountain Health Maintenance Organization*, 927 P.2d 1325 (Colo. 1996). In that case, an HMO denied a claim for cancer medical care. The HMO contract had an arbitration clause which was valid. The plaintiff sought a preliminary injunction requiring continued medical care until the arbitration panel could resolve the case. The court had determined that such authority did exist in order to preserve the status quo. Once the arbitration award was entered, the injunction would be set aside.

The 2004 UAA specifically provides that a district court may grant preliminary relief to “protect the effectiveness of the arbitration proceeding...” C.R.S. § 13-22-208(1). After the arbitrator is appointed, then the arbitrator has the authority to issue preliminary orders. C.R.S. § 13-22-208(2).

Final Thoughts: Arbitration clauses will continue to proliferate in employment and other contracts. Understanding the framework of arbitration and how it can best be used to your client’s advantage is important in light of recent decisions.