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Arbitrability and Vulnerability

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ARBITRABILITY AND VULNERABILITY

by CAROLYN L. DESSIN*

INTRODUCTION

Arbitration is cool.¹ Everybody's doing it. In the eighty-five years since the passage of the Federal Arbitration Act,² that seems to be the prevailing sentiment. Recent decades have seen the meteoric rise of arbitration as a form of alternative dispute resolution.³ Arbitration is widely regarded as a less expensive, more expeditious alternative to litigation.

Courts frequently note that federal policy clearly favors arbitration.⁴ No judicial enthusiasm for arbitration seems more complete than that evidenced in the jurisprudence of the United States Supreme Court.⁵

Along with the rise of arbitration, however, there has also been a rise in the amount of criticism of arbitration.⁶ Some suggest that nothing short of a complete

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1. Arbitration is:

An agreement between two or more persons to submit an existing or future dispute to third persons (arbitrators) who are chosen by the parties. The power of the arbitrators to act depends upon the scope of the agreement. This is the core value of private autonomy, for without an agreement there is no duty to arbitrate.

Richard E. Speidel, *Common Legal Issues in American Arbitration Law*, in *ARBITRATION LAW IN AMERICA* 31 (Edward Brunet et al. eds., 2006) (internal citations omitted).

2. 9 U.S.C. §§ 1-16 (2006).

3. See generally Jean R. Sternlight, *Creeping Mandatory Arbitration: Is It Just?*, 57 STAN. L. REV. 1631, 1636 (2005) [hereinafter Sternlight, *Creeping Mandatory Arbitration*] (discussing the increase of mandatory arbitration); Jean R. Sternlight, *The Rise and Spread of Mandatory Arbitration as a Substitute for the Jury Trial*, 38 U.S.F. L. REV. 17, 17 (2003) [hereinafter Sternlight, *Rise and Spread*] (discussing the increase of mandatory arbitration).

4. See, e.g., *Seaboard Coast Line R.R. Co. v. Trailer Train Co.*, 690 F.2d 1343, 1348 (11th Cir. 1982) (citing 9 U.S.C. §§ 1-14 (1982) (current version at 9 U.S.C. §§ 1-16 (2006)); *Ultracashmere House Ltd. v. Meyer*, 664 F.2d 1176, 1179-80 (11th Cir. 1981); *Seaboard Coast Line R.R. v. Nat'l Rail Passenger Corp.*, 554 F.2d 657, 660 (5th Cir. 1977); *J. S. & H. Constr. Co. v. Rich. Cnty. Hosp. Auth.*, 473 F.2d 212, 214-15 (5th Cir. 1973).

5. See Thomas E. Carbonneau, "Arbitracide": *The Story of Anti-Arbitration Sentiment in the U.S. Congress*, 18 AM. REV. INT'L ARB. 233, 233-38 (2007) ("For more than forty years, the U.S. Supreme Court has touted the recourse to arbitration With the exception of an isolated case, the judicial doctrine on arbitration constantly endeavors to achieve the enforcement of arbitral agreements and awards and thereby erect and maintain a *de facto*, albeit functional, private process for the adjudication of civil disputes." (footnotes omitted)).

6. Compare David S. Schwartz, *If You Love Arbitration, Set It Free: How "Mandatory" Undermines "Arbitration,"* 8 NEV. L.J. 400, 401 (2007) (criticizing the Supreme Court's interpretation of the Federal Arbitration Act because it has resulted in two "fundamental errors" that, one, state law is preempted and, two, that "stronger parties in regulated transactions [are allowed] to compel arbitration

overhaul of the Federal Arbitration Act will correct problems that have arisen in the arbitration context.⁷

One of the main focuses of the criticism has been against mandatory binding pre-dispute arbitration in the consumer context.⁸ The United States has condoned this species of arbitration in an unparalleled fashion, and some suggest that our country has gone too far.⁹ One of the major concerns in this area is that it is unlikely that a consumer can knowingly agree to arbitrate claims that have not yet arisen.¹⁰

This Article focuses on mandatory pre-dispute arbitration agreements in the context of a situation involving a vulnerable party. As the discussion will illustrate, there is no precise definition of vulnerability. Although most of the cases discussed herein involve older vulnerable adults, the concerns in this area frequently arise in other contexts as well. Thus, the author suggests that the discomfort exhibited by courts in dealing with these cases may suggest a broader discomfort with mandatory pre-dispute arbitration agreements in the consumer context.

I. A BRIEF HISTORY OF MANDATORY PRE-DISPUTE ARBITRATION AGREEMENTS

When the Federal Arbitration Act was enacted in 1925, most commentators agree that Congress was not contemplating arbitration agreements involving consumers.¹¹ In fact, the rare comments in the legislative history suggest the

as a condition of doing business”), and Jean R. Sternlight, *In Defense of Mandatory Binding Arbitration (If Imposed on the Company)*, 8 NEV. L.J. 82, 82 (2007) (“I drafted an article arguing on policy grounds that companies ought not to be able to deprive ‘little guys’ of the opportunity to litigate their disputes.”), with, e.g., Peter B. Rutledge, *Who Can Be Against Fairness? The Case Against the Arbitration Fairness Act*, 9 CARDOZO J. CONFLICT RESOL. 267, 267-68 (2008) (suggesting that a legislative proposal to ban more predispute arbitration clauses between individuals and companies would only benefit “trial lawyers” and would make it harder to get an attorney, would drive up the cost of resolving disputes, and would delay the time it takes to get relief).

7. E.g., ARBITRATION LAW IN AMERICA, *supra* note 1, at 1.

8. Cf. Thomas E. Carbonneau, *Arguments in Favor of the Triumph of Arbitration*, 10 CARDOZO J. CONFLICT RESOL. 395, 398-400 (2009) (noting that thinkers on the left find problems with the equity of “adhesionary” or “disparate-party” arbitration in consumer and other transactions because they are contracts “imposed unilaterally by the stronger party upon the weaker party on a take-it-or-leave-it basis” and that thinkers on the right also find problems with the equity of such mandatory arbitration because “[c]oerced agreements are not consensual undertakings”). In response to the possibility of sweeping prohibition of consumer pre-dispute arbitration provisions, Professor Carbonneau states: “The nullification of arbitration agreements in entire transactional areas is a radical and costly solution to the problem of coerced acquiescence to, or participation in, arbitration.” *Id.* at 401.

9. See, e.g., Jean R. Sternlight, *Is Alternative Dispute Resolution Consistent with the Rule of Law?: Lessons from Abroad*, 56 DEPAUL L. REV. 569, 570-71 (2007) (summarizing that critics of the alternative dispute resolution boom in the United States since the 1970s argue that ADR in the private setting does not serve the same functions of the “elaboration of law,” public accountability, education, protecting the legal positions of weaker members of society, including women, and preventing prejudices from influencing the resolution of conflicts).

10. Cf. Richard E. Speidel, *Consumer Arbitration of Statutory Claims: Has Pre-Dispute [Mandatory] Arbitration Outlived Its Welcome?*, 40 ARIZ. L. REV. 1069, 1078 (1998) (explaining that in the employment context, if an employee agrees to arbitrate all claims “arising out of or related to” an employment contract, the employee is understood to have agreed to the breadth of the agreement because he or she otherwise would have bargained to exclude claims from the agreement to arbitrate).

11. See, e.g., David S. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and*

framing legislators viewed such a use of arbitration as inappropriate.¹²

The Federal Arbitration Act is extremely broad in its scope. It provides:

A written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract . . . 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 . . . 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.¹³

Thus, the Federal Arbitration Act clearly *allows* binding pre-dispute arbitration agreements.¹⁴ Whatever one thinks of such agreements, there is a statutory basis for enforcement in the Federal Arbitration Act.

After the parties enter into an arbitration agreement, disputes are to be resolved in accordance with the agreement. If a dispute arises, and the agreement calls for arbitrating that type of dispute, the party who desires arbitration will often file a motion to compel arbitration and stay litigation if the other party begins a litigation proceeding. To determine the merits of the motion to compel arbitration, the court first must determine whether the dispute is one that the parties intended to arbitrate.¹⁵ Doubts are to be resolved in favor of arbitration.¹⁶ If the court determines that the claim is within the purview of the arbitration agreement, the

Consumer Rights Claims in an Age of Compelled Arbitration, 1997 WIS. L. REV. 33, 78 (1997) (“If the FAA was intended to have a direct impact on constituencies other than the business community—such as consumers, or employees—one would expect some effort on the part of the Act’s proponents to convince such groups about how they too would benefit from enforcement of arbitration agreements. But virtually nothing of the sort appears in the legislative history or supporting commentary. On the contrary, these sources make abundantly clear that the FAA was an act by and for the business community to regulate relationships among its members.”).

12. Jean R. Sternlight, *Consumer Arbitration*, in ARBITRATION LAW IN AMERICA, *supra* note 1, at 127. Professor Sternlight notes “when one Senator voiced a concern that arbitration contracts might be ‘offered on a take-it-or-leave-it basis to captive customers or employees,’ the Senator was reassured by the bill’s supporters that they did not intend for the bill to cover such situations.” *Id.* at 127-28 (citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 414 (1967) (Black, J., dissenting) (citing *Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration: Hearing on S. 4213 and S. 4214 Before the Subcomm. of the S. Comm. on the Judiciary*, 67th Cong. 10 (1923) (statement of Sen. Walsh, Member, S. Comm. on the Judiciary))).

13. 9 U.S.C. § 2.

14. For an interesting divergence of views on Congress’s intent in passing the Federal Arbitration Act, compare IAN R. MACNEIL, AMERICAN ARBITRATION LAW 116-17 (1992) (recounting that the American Bar Association (ABA) initially proposed the legislation and that it was the intent of both the ABA and of Congress that the Act was not to “create substantive federal regulatory law superseding state law”), with Christopher R. Drahozal, *In Defense of Southland: Reexamining the Legislative History of the Federal Arbitration Act*, 78 NOTRE DAME L. REV. 101, 163-65, 167 (2002) (arguing that the legislative history, while ambiguous, shows that Congress did not intend for the Act to apply only in federal court and that, in light of that history, there is less reason to amend the Act “to limit the enforceability of pre-dispute arbitration agreements”).

15. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985).

16. *See Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983) (reasoning that the Federal Arbitration Act establishes that any doubts about the scope of what can be arbitrated should be decided in favor of arbitration).

court must then decide “whether legal constraints external to the parties’ agreement foreclosed the arbitration of those claims.”¹⁷

Following the lead of the Supreme Court, courts in the United States have overwhelmingly decided cases in favor of arbitrability.¹⁸ Because the arbitration is based on a federal statute, the courts have little choice in the matter.

Furthermore, the preemption doctrine limits the states’ ability to enact limits on arbitrability.¹⁹ Two results seem to flow from this fact. First, any limitation to arbitrability will most likely have to be implemented at the federal level. Second, state courts that are displeased with the results caused by a broad interpretation of arbitrability may be inclined to find other ways to undermine seemingly enforceable arbitration clauses.²⁰

The contours of Federal Arbitration Act preemption have been addressed by the Supreme Court. In *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*,²¹ the Supreme Court considered the extent of preemption. The Court noted that the federal act preempts state law only when state law conflicts with the federal act’s purpose of enforcing mutually agreed arbitration clauses.²² Over the years, the Supreme Court has consistently struck down state attempts to curtail arbitration.²³

The debate in recent years about the desirability of binding pre-dispute arbitration agreements in the consumer context has become increasingly intense and the rhetoric has become increasingly vitriolic.²⁴ Although this Article will not undertake a comprehensive review of the discourse, some discussion of the discourse is necessary to address the issue at hand.²⁵

Along with the increase in debate, various legislators have introduced legislation designed to curtail arbitrability. For example, in 2009, Representative Hank Johnson re-introduced the Arbitration Fairness Act of 2009.²⁶ That Act would

17. *Mitsubishi Motors Corp.*, 473 U.S. at 628.

18. See generally Alan Scott Rau, “*The Arbitrability Question Itself*,” 10 AM. REV. INT’L ARB. 287 (1999) (thoroughly discussing the arbitrability question, including an interesting treatment of the question of whether the arbitrator or the court decides the arbitrability question and discussing the favorable treatment of arbitrability in courts).

19. See generally David S. Schwartz, *Correcting Federalism Mistakes in Statutory Interpretation: The Supreme Court and the Federal Arbitration Act*, 67 LAW & CONTEMP. PROBS. 5 (Winter/Spring 2004) (providing an extensive and thoughtful critique of preemption in the arbitration context).

20. See *infra* text accompanying notes 31-90 (discussing how courts have dealt with these matters).

21. 489 U.S. 468 (1989).

22. *Id.* at 477-78.

23. See Carbonneau, *supra* note 5, at 233 (noting that the Supreme Court “has protected arbitration from inhospitable state regulation”).

24. E.g., *id.* at 249. Professor Carbonneau discusses the Arbitration Fairness Act by saying:

The legislative critique mouths the criticism of arbitration advanced by the ATLA. Regardless of how justice is defined, arbitration undeniably depreciates the business interest, adversarial skills, and the professional necessity of ATLA members by creating a more effective and efficient civil dispute resolution process. Eliminating the option for arbitration is equivalent to relegating American citizens to the emergency room for their health care needs.

Id.

25. For a more thorough examination of the historical development of and difficulties arising in regulating consumer arbitration, see Sternlight, *supra* note 12.

26. H.R. 1020, 111th Cong. (2009).

prohibit binding pre-dispute arbitration agreements in most consumer settings.²⁷ Similarly, Representative Linda Sánchez and Senator Mel Martínez re-introduced the Fairness in Nursing Home Arbitration Act of 2009.²⁸ The Nursing Home Bill would prohibit binding pre-dispute arbitration agreements in nursing home entrance contracts.²⁹

Not surprisingly, much of the reform sentiment is encouraged by organizations of trial lawyers like the American Association for Justice, which is the organization formerly known as the American Trial Lawyers Association.³⁰ Self-interest alone, however, does not seem to explain the increasing calls for change in the law regarding binding pre-dispute arbitration agreements in the consumer context.

II. RECENT CASELAW INVOLVING MANDATORY PRE-DISPUTE ARBITRATION AGREEMENTS AND A VULNERABLE PARTY

A. *Who is vulnerable?*

Presumably, any discussion of caselaw involving vulnerable parties should begin with a definition of vulnerability. There is, however, no generally agreed upon definition of vulnerability.

The core concept in a definition of vulnerability is the idea that “one is incapable of protecting himself or herself from the overreaching acts of unscrupulous people.”³¹ Inherent in this are two related concepts.³² First, the individual may have a weakened capacity to “resist the influence of others.”³³ Second, the individual may have a deficit in the ability to understand when another person might be attempting to take advantage.³⁴

In defining vulnerability, many states have used age as a proxy for vulnerability. Consider, for example, the definition of “vulnerable” in the Michigan protective services statute: “‘Vulnerable’ means a condition in which an adult is unable to protect himself or herself from abuse, neglect, or exploitation because of a mental or physical impairment *or because of advanced age*.”³⁵ Other states have adopted similar definitions.

Arguably, a definition of vulnerability based on attainment of a certain age or on age alone is the result of ageist stereotyping. Vulnerability comes from deficits in cognition or ability, not from attainment of an age. Although many people

27. *Id.*

28. H.R. 1237, 111th Cong. (2009) and S. 512, 111th Cong. (2009). Representative Linda Sánchez and Senators Mel Martínez and Herb Kohl introduced the bill to the House and Senate on February 26 and March 3, 2009, respectively. The bills have been referred to committee in both the House and Senate.

29. H.R. 1237.

30. *See, e.g., Most Vulnerable Americans Protected by Fairness in Nursing Home Arbitration Act*, AM. ASS’N FOR JUSTICE (Mar. 5, 2009), <http://www.justice.org/cps/rde/xchg/justice/hs.xml/7799.htm> (advocating in favor of the Fairness in Nursing Home Arbitration Act and its provisions).

31. Carolyn L. Dessin, *Financial Abuse of the Elderly: Is the Solution a Problem?*, 34 MCGEORGE L. REV. 267, 308 (2003).

32. *Id.*

33. *Id.*

34. *Id.*

35. Mich. Comp. Laws. § 400.11(f) (2008) (emphasis added).

associate the aging process with an inevitable lessening of cognition and ability, the reality is much more encouraging.³⁶ In fact, studies have repeatedly shown that the percentage of older people who suffer from mental deficits serious enough to interfere with the activities of daily living is actually fairly small.³⁷

To further complicate attempts to craft a meaningful definition, vulnerability can be situational. An individual may be vulnerable to physical attacks, but fully capable of protecting himself against financial scams.

For purposes of considering the issue at hand, the focus should be on a definition of vulnerability that centers on three attributes. First, is the individual so impaired that he or she cannot form the requisite mental intent to execute an agreement to arbitrate? Second, is the individual impaired in a way that will prevent him or her from participating in the arbitral process? Third, does the situation suggest vulnerability?

With respect to the first attribute, it is clear that one must have the capacity to enter an agreement to arbitrate. Without agreement, there is no duty to arbitrate.³⁸ Courts have used the capacity to contract standard when assessing this type of issue. Traditionally, courts have held that a person lacks capacity to contract when he or she cannot understand the terms of the agreement on the table.³⁹ This is a well-established and, for the most part, readily applied rule of law.

With respect to the second attribute, there has been little discussion of the effect that impairment of one of the parties has on the arbitral process. The same is true for the third attribute, although in reviewing the caselaw, one can infer that courts are uncomfortable enforcing arbitration agreements in some circumstances.

B. Examples of Caselaw Involving Vulnerable Parties

1. Nursing Home Entrance Agreements

Arguably, an arbitration clause contained in an agreement between a nursing home and a resident provides the best example of a consumer-entity arbitration agreement with a vulnerable party on one side. It is difficult to imagine a time when an individual would be more vulnerable than when one is in such need of skilled care that the individual is required to enter a nursing home.

36. See, e.g., H.B. GIBSON, *THE EMOTIONAL AND SEXUAL LIVES OF OLDER PEOPLE: A MANUAL FOR PROFESSIONALS* 55 (1992) (suggesting that the model of aging as deterioration is false); Marie R. Haug & Marcia G. Ory, *Issues in Elderly Patient-Provider Interactions*, 9 RES. ON AGING 3, 6 (1987) (suggesting that many medical students believe negative stereotypes about geriatric patients' health).

37. See, e.g., OFFICE OF TECH. ASSESSMENT, *LOSING A MILLION MINDS: CONFRONTING THE TRAGEDY OF ALZHEIMER'S DISEASE AND OTHER DEMENTIAS* 16 tbl.1-4 (1987) (noting that approximately one percent of persons aged 65-74, seven percent of persons aged 75-84 and twenty-five percent of those 85 or older suffer from dementia).

38. See, e.g., *Harrison v. Nissan Motor Corp.*, 111 F.3d 343, 350 (3d Cir. 1997) (“[T]he essence of arbitration, we think, is that, when the parties agree to submit their disputes to it, they have agreed to arbitrate these disputes through to completion . . .”).

39. See RESTATEMENT (SECOND) OF CONTRACTS §15(1) (“A person incurs only voidable contractual duties by entering into a transaction if by reason of mental illness or defect . . . he is unable to understand in a reasonable manner the nature and consequences of the transaction, or . . . he is unable to act in a reasonable manner in relation to the transaction and the other party has reason to know of his condition.”).

As a preliminary matter in considering this type of case, it may be important to remember that nursing home litigation is a lucrative and growing area of legal practice.⁴⁰ Those who are distrustful about plaintiff-side attorneys' motives may suggest that the growing number of challenges to mandatory arbitration in this area is more about greed than about protecting the vulnerable, but that debate is outside the scope of this article.

In February and March 2009, members of Congress re-introduced the Fairness in Nursing Home Arbitration bill.⁴¹ The bills were referred to Committee, and seemingly no further action has been taken. The bills would seriously curtail the use of binding arbitration clauses in nursing home entrance agreements.

Creative attorneys have tried a number of different approaches to avoiding arbitration clauses included in nursing home entrance contracts. If the clause can be avoided, plaintiffs can resort to litigation to resolve disputes.

As discussed in the previous section, one could challenge enforceability of the clause based on the incapacity of the nursing home resident. There are several problems with this approach. First, the resident is often not the one signing the agreement. If a spouse or adult child of the resident signs the agreement, competency is usually not an issue. Second, even if the resident signs and is arguably incompetent, the contract is voidable, not void.⁴² Presumably, one acting on behalf of the resident could avoid the contract, but that issue would need to be addressed. Finally, the resident or his representative might not wish to arbitrate, but might also not want to avoid the entire contract. Obviously, this problem will not arise in a wrongful death action but could arise in other contexts such as a suit for injury caused by the nursing home.

2. Durable Powers of Attorney

Sometimes, one who does not wish to be bound by an arbitration clause will argue that a signature by an agent on an agreement to arbitrate cannot bind the principal or those whose claims are based on rights of the principal. Although this argument frequently arises in the nursing home agreement context, it can also arise in other contexts.

Under traditional agency law, an agent can perform any act that his principal empowers him to perform.⁴³ In the modern estate planning context, most powers of attorney are durable powers of attorney.⁴⁴ A durable power is one that is intended to be effective even if the principal becomes incompetent.⁴⁵

40. See, e.g., David G. Stevenson & David M. Studdert, *The Rise of Nursing Home Litigation: Findings from a National Survey of Attorneys*, 22-2 HEALTH AFF. 219 (March/April 2003) (noting the rapid growth of nursing home litigation in recent years).

41. H.R. 1237; S. 512.

42. See RESTATEMENT (SECOND) OF CONTRACTS § 15 (1981) (noting that contracts entered into by people with mental illness are "voidable").

43. See RESTATEMENT (THIRD) OF AGENCY § 2.01 (2006) ("An agent acts with actual authority when, at the time of taking action that has legal consequences for the principal, the agent reasonably believes . . . that the principal wishes the agent so to act.").

44. See, e.g., Carolyn L. Dessin, *Acting as Agent under a Financial Durable Power of Attorney: An Unscripted Role*, 75 NEB. L. REV. 574, 575 (1996) (noting that such powers of attorney have become "extremely popular").

45. Before the enactment of statutes allowing durability, a power of attorney would become

The breadth of possible authority in an agent coupled with the notion of durability would seem to suggest that an agent could consent to arbitration even on behalf of a vulnerable, incompetent adult. Why then have some courts expressed an unwillingness to allow agents to consent to arbitration on behalf of their principals?

3. Trust Disputes

In the event that a trustee breaches a fiduciary duty owed to a trust beneficiary, the beneficiary can bring an action against the trustee. Not surprisingly, corporate trustees have begun to seek the inclusion of binding arbitration clauses in agreements of trust. This section focuses on the responses of American courts to arbitration clauses in trust instruments.⁴⁶

When faced with binding pre-dispute arbitration clauses, most courts have upheld the agreements and enforced the arbitration clause.

Commentators have considered the benefits and detriments of alternative dispute resolution in the trust and probate area.⁴⁷

a. Trust Beneficiary vs. Trustee

In a recent Texas case, the Court of Appeals refused to compel arbitration. In *Citizens National Bank v. Bryce*,⁴⁸ the court considered a case involving a suit by a trust beneficiary and the executor of the settlor's estate against a trustee for misappropriation and mismanagement.⁴⁹ The case is somewhat unusual in that the arbitration clause was contained in a partnership agreement that the Bank signed as trustee.⁵⁰ Nevertheless, the underlying dispute was a suit by a trust beneficiary against a trustee for breach of fiduciary.

Relying on the fact that the trustee had engaged in discovery for twenty months after the suit was filed, the trial court concluded that the trustee had waived any right it had to compel arbitration. The trial court thus denied the trustee's motion to compel arbitration and the Court of Appeals affirmed.⁵¹

The Court of Appeals reasoned that "[a] party implicitly waives its arbitration rights when it substantially invokes the judicial process to the other party's

ineffective upon the incompetence of the principal. *Id.* at 576.

46. The issue of arbitration in the trust contract is starting to emerge as an international issue as well. See Tina Wüstemann, *Arbitration of Trust Disputes*, in *NEW DEVELOPMENTS IN INTERNATIONAL COMMERCIAL ARBITRATION* 33, 34-35 (Christoph Müller ed., 2007) (noting discussion of trust disputes in foreign jurisdictions).

47. See, e.g., Ray D. Madoff, *Mediating Probate Disputes: A Study of Court Sponsored Programs*, 38 REAL PROP. PROB. & TR. J. 697, 719-20 (2004) (discussing ways to overcome skepticism about mediation among lawyers); Susan N. Gary, *Mediating Probate Disputes*, 13 PROB. & PROP. 11, 12-14 (1999) (noting the potential benefits and drawbacks of mediation); Roselyn L. Friedman & Erica E. Lord, *Using Facilitative Mediation in a Changing Estate Planning Practice*, 32 EST. PLAN. 15, 18-20 (2005) (noting that mediation is "well-suited" to disputes involving trusts and estates); Robert N. Sacks, *Mediation: An Effective Method to Resolve Estate and Trust Disputes*, 27 EST. PLAN. 210, 211 (2000) (noting that courts are increasingly supporting mediation as a means of resolving trusts and estates disputes).

48. 271 S.W.3d 347 (Tex. App. 2008).

49. *Id.* at 351.

50. *Id.* at 352.

51. *Id.* at 359.

detriment or prejudice.”⁵² Examining the length and extent of discovery, the Court of Appeals held that the trustee had, indeed, invoked the judicial process to the extent that it waived any right to compel arbitration.⁵³

The Florida legislature addressed this issue by enacting legislation that attempts to require courts to enforce arbitration agreements found in trusts.⁵⁴ Not surprisingly, some see such legislation as serving many salutary purposes.⁵⁵

b. Trust Beneficiary vs. Party with Whom Trustee Contracted

Sometimes, the attempt to arbitrate will be made by someone other than the trustee of the trust. These cases usually arise out of a contract between the trustee and a third party, i.e., one outside the trust.⁵⁶ Frequently, as part of seeking assistance with assets management, the trustee will contract with a financial services company. These contracts often include mandatory pre-dispute arbitration clauses. If a beneficiary becomes dissatisfied with the financial performance of the trust, the beneficiary may sue both the trustee and the financial services third party. The question then arises whether the beneficiary will be bound by the arbitration clause.

In cases such as this, the beneficiary will invariably argue that she should not be bound by the agreement to arbitrate because she was not a signatory to it. The majority of courts addressing this issue have decided that the beneficiary can be bound by the trustee’s signature.⁵⁷

Courts have addressed beneficiary challenges to arbitration clauses in this context with a variety of responses. There is, of course, an underlying principle that

52. *Id.* at 355 (citing *Perry Homes v. Cull*, 258 S.W.3d 580, 589-90 (Tex. 2008)).

53. *Id.* at 355-57.

54. FLA. STAT. ANN. § 731.401 (West 2010). The Florida statute provides:

(1) A provision in a will or trust requiring the arbitration of disputes, other than disputes of the validity of all or a part of a will or trust, between or among the beneficiaries and a fiduciary under the will or trust, or any combination of such persons or entities, is enforceable.

(2) Unless otherwise specified in the will or trust, a will or trust provision requiring arbitration shall be presumed to require binding arbitration under s. 44.104.

Id.

55. Michael P. Bruyere & Meghan D. Marino, *Making Arbitration Truly Mandatory*, TR. & EST. 22, 22 (Jul. 2008). The authors state:

Mandatory arbitration is often good for everyone involved in a trust dispute. Grantors are assured that their private lives remain out of the courts and therefore free from public exposure. Trustees can protect trust assets, while limiting their liability, thus reducing the overall cost of trust administration. Beneficiaries can avoid the emotional damage and cost of protracted litigation. And the public doesn’t have to fund a legal process in which the wealthy battle over their trust funds.

Id.

56. See generally Alan Scott Rau, *Evidence and Discovery in American Arbitration: The Problem of “Third Parties,”* 19 AM. REV. INT’L ARB. 1 (2008) (discussing the many issues that arise when third parties are involved in arbitration disputes).

57. See, e.g., *Baker v. Am. Express Fin. Advisors, Inc.*, No. B193400, 2008 WL 223776, at *6 (Cal. Ct. App. Jan. 29, 2008) (finding that the trustee of a trust had the power to bind beneficiaries to an arbitration agreement); *Merrill Lynch v. Eddings*, 838 S.W.2d 874, 879 (Tex. App. 1992) (“We hold that the settlor and beneficiaries of a trust are bound by a clause in an account agreement to arbitrate the claims arising out of transactions in the trust’s account.”).

only parties who voluntarily agree to binding arbitration should be forced to arbitrate claims. There are, however, a number of exceptions to this general principle.

First, the court may find that the beneficiary is equitably estopped from resisting arbitration.

Second, the court may hold that because the agreement containing the arbitration clause is the source of the beneficiary's claim, the beneficiary can be compelled to arbitrate. This was the reasoning underlying the decision of the Court of Appeals of Washington in *In re the Jean F. Gardner Amended Blind Trust*.⁵⁸ In *Gardner*, a trust beneficiary sued both the trustee and a securities broker with whom the trustee contracted.⁵⁹ The contract included a provision agreeing to arbitrate all disputes arising under the agreement.⁶⁰ The court concluded that all of the beneficiary's claims arose under the agreement and, therefore, the beneficiary was bound to the arbitration agreement.⁶¹

However, some courts disagree on this issue. In *Clark v. Clark*,⁶² a case raising a virtually identical issue, the Oklahoma Court of Appeals came to the opposite result.⁶³ Here, the trust beneficiary was held to not be bound by the agreement's arbitration clause.⁶⁴ In contrast to *Gardner*, the court in *Clark* determined that the beneficiary's case arose independent of the agreement, and that the trustee was not an agent of the beneficiary.⁶⁵ Since the beneficiary had not been a party to the initial agreement to arbitrate, the court held that he could not be said to have waived his constitutional right to access the courts.⁶⁶

Third, the court may hold that the beneficiary is a third-party beneficiary of the contract between the trustee and the contracting party and, therefore, is bound by the terms of an arbitration agreement contained in the contract. This rationale was used by the Court of Appeals in Arizona in *Shahan v. Staley*.⁶⁷ *Shahan* is an interesting case in that it arose when the trust beneficiary was attempting to compel the trust's securities broker to arbitrate.⁶⁸ The broker resisted, arguing that the beneficiary was not his customer.⁶⁹ The court concluded that the beneficiary was entitled as a third-party beneficiary to the arbitration he sought.⁷⁰

Some courts, however, have declined to use the third-party beneficiary doctrine to enforce arbitration clauses against a trust beneficiary. In *Morgan*

58. 70 P.3d 168 (Wash. Ct. App. 2003).

59. *Id.*

60. *Id.* at 169.

61. *Id.* at 170. The Texas Court of Appeals reached a similar conclusion in *Merrill Lynch v. Eddings*. The *Eddings* court noted "[i]f the settlor and beneficiaries of a trust could bring suit independently of the trustee and thereby avoid the arbitration agreement, the strong state policy favoring arbitration would be effectively thwarted." *Eddings*, 838 S.W.2d at 879. In *Eddings*, the trial court had denied the motion to compel arbitration. *Id.* at 876.

62. 57 P.3d 95 (Okla. Civ. App. 2002).

63. *Id.*

64. *Id.* at 99.

65. *Id.*

66. *Id.*

67. 932 P.2d 1345 (Ariz. Ct. App. 1996).

68. *Id.* at 1347.

69. *Id.*

70. *Id.* at 1348.

Stanley DW Inc. v. Halliday,⁷¹ a Florida appeals court considered a suit by a trust beneficiary against a trustee and a brokerage firm with which the trustee had contracted.⁷² The beneficiary alleged mismanagement of the trust assets.⁷³ When the trustee placed trust assets with Morgan Stanley, the trustee signed a customer agreement that included a binding pre-dispute arbitration provision.⁷⁴ After the beneficiary filed suit, Morgan Stanley moved to compel arbitration on the theory that the beneficiary was a third-party beneficiary of the agreement between the trustee and Morgan Stanley that contained the arbitration provision and that the beneficiary was bound under agency theory.⁷⁵ Rejecting the third-party beneficiary theory, the court held simply that the beneficiary was not an intended beneficiary of the customer agreement, nor was she, in particular, an intended beneficiary of the arbitration provision.⁷⁶ Citing the often-used statement that incidental or consequential benefit is insufficient to render one a third-party beneficiary, the court affirmed the trial court's denial of Morgan Stanley's motion.⁷⁷ Further, the court noted that Morgan Stanley also seemed to be arguing that the trustee was an agent of the beneficiary who could bind the beneficiary to the arbitration agreement.⁷⁸ The court rejected this argument as well, stating that the trustee is a fiduciary of, not an agent for, the beneficiary.⁷⁹ In conclusion, the court cogently stated:

As for arbitration agreements, which involve a waiver of a person's right of access to the courts, binding a non-signatory to arbitrate under the theory of third party beneficiary is fraught with miscalculation and unfairness. For one thing, unless a manifestation of intent by the third party beneficiary to the arbitration clause is clear and indisputable, the non-party's right of access may be lost by the unilateral decision of another without knowledge or consent. For another, it is difficult to understand how, as a general matter, the usual arbitration agreement is designed specifically to benefit a non-party. In this instance, any general doubt as to benefit is displaced by its specific absence, as the trial Judge found. Arbitration in this case—involving the alleged mismanagement by both Morgan Stanley and the Trustees of the Trust assets—will not shorten the

71. 873 So. 2d 400 (Fla. Dist. Ct. App. 2004).

72. *Id.* at 402.

73. *Id.*

74. *Id.*

75. *Id.* As further evidence of the creative lengths to which parties seeking to arbitrate will go, Morgan Stanley argued that the fact that the beneficiary had a personal account covered by an agreement containing a binding pre-dispute clause suggested that she should be bound by the similar clause in the agreement between the trustee and Morgan Stanley. The court rejected this argument. *Id.* at 402 n.1 (citing *Shearson Lehman Hutton Inc. v. Lifshutz*, 595 So. 2d 996 (Fla. Dist. Ct. App. 1992)).

76. *Halliday*, 873 So. 2d at 403.

77. *Id.* (citing *Metro. Life Ins. Co. v. McCarson*, 467 So. 2d 277 (Fla. 1985); *Caretta Trucking Inc. v. Cheoy Lee Shipyards, Ltd.*, 647 So. 2d 1028 (Fla. Dist. Ct. App. 1994)).

78. *Id.*

79. *Id.* ("That the Trustees may engage the services of an expert in managing Trust assets to assist them in the performance of their fiduciary responsibilities hardly makes them agents of the Trust beneficiary in order to bind her personally to their hiring of that assistance or to their purported waiver of her right of access to a court to seek redress for loss occasioned thereby.").

dispute at all because the litigation will proceed against the Trustees anyway.⁸⁰

If the court decides that this sort of claim must be submitted to arbitration, an interesting question arises: who is the proper party to the arbitration, the trustee or the beneficiary? The New York case of *In re Blumenkrantz*⁸¹ is one of the very few cases addressing this issue.⁸² Typically, the trustee is the only person with authority to act on behalf of the trust.⁸³ In a case in which the beneficiary is suing both the trustee and the contracting third party, however, the trustee is squarely in a conflict of interest position.⁸⁴ In these situations, courts allow the beneficiary to sue on a theory analogous to the derivative suit in the corporate setting.⁸⁵ This rationale, however, also makes the beneficiary subject to the arbitration agreement entered into by the original trustee.⁸⁶

c. Trends

As the case law illustrates, arbitration issues involving trustees are somewhat different from other arbitration cases in the sense that the settlor, who is presumably competent and acting knowingly and voluntarily, is agreeing on behalf of the trust beneficiaries to arbitrate possible future disputes between the beneficiaries and the trustee. The element of vulnerability, if present, would be in the beneficiary standing on the receiving end of one of the most respected fiduciary duties in the legal spectrum.

As the case law further illustrates, some courts have difficulty applying traditional contract law rules governing the enforceability of agreements to arbitrate in the trust setting.⁸⁷

There is no question that using arbitration in the trust context has a number of possible advantages over litigation. If a trust dispute is between family members, having the matter resolved more quickly than it would be through litigation improves the chance that the family's relations will improve after the dispute. There may also be a desired privacy in the arbitration process that would not be present in a litigation context.⁸⁸

80. *Id.* at 404.

81. 824 N.Y.S.2d 884 (N.Y. Surr. Ct. 2006).

82. *Id.* at 887-88.

83. *Id.* at 888.

84. *Id.* ("The trustee cannot be held liable for failure to oversee management of the funds absent a determination by the arbitrator that Wachovia Securities is liable to the trust for the loss incurred. It is not in the interest of the trustee to pursue a claim against Wachovia Securities. A finding of misfeasance against Wachovia could result in a finding of liability against the trustee for failure to properly monitor the delegee . . .").

85. *See id.* at 889 (holding that the proper procedure is to grant the beneficiary limited trusteeship for the purposes of proceeding against the contracting party).

86. *Id.*

87. *See* Michael P. Bruyere & Meghan D. Marino, *Mandatory Arbitration Provisions: A Powerful Tool to Prevent Contentious and Costly Trust Litigation, But Are They Enforceable?*, 42 REAL PROP. PROB. & TR. J. 351, 361-64 (2007) (discussing courts' difficulties in applying contract law to the enforceability of arbitration clauses in trust settings).

88. *See* Jonathan G. Blattmachr, *Reducing Estate and Trust Litigation Through Disclosure, In Terrorem Clauses, Mediation and Arbitration*, 9 CARDOZO J. CONFLICT RESOL. 237, 261 (2008) (noting

On the other hand, those who suffer breaches of a fiduciary duty owed to them have traditionally had recourse to the courts. Forcing a trust beneficiary to arbitrate against either a trustee or one with whom the trustee has contracted is antithetical to this idea.

With respect to arbitration based on a contract between the trustee and a third party, the Florida Court deciding *Halliday* may have summed it up best: “Perhaps the whole idea of trying to bind a nonparty trust beneficiary to an arbitration agreement entered into by the Trustees with a securities portfolio manager is really what is wrong here.”⁸⁹ The court went on to discuss that it seems wrong to allow a fiduciary to delegate an important aspect of its duty to the trust and its beneficiaries to a third party, and then have the third party attempt to force the beneficiary into arbitration while the trustee stands by.⁹⁰

With respect to arbitration between a trustee and beneficiary, the argument seems even stronger. One who owes a fiduciary duty to another should not be able to force the other party to arbitrate. In taking that position, nothing would prevent the beneficiary and trustee from agreeing to arbitrate after a dispute has arisen. Rather, the difficulty is with arbitration clauses that mandate arbitration before a dispute has arisen.

III. ANALYSIS

The growing number of courts addressing pre-dispute binding arbitration agreements suggests two things. First, an increasing number of challenges are being made to such agreements. Second, some courts seem to be struggling to find ways to refuse to enforce such agreements, suggesting a growing discomfort with the agreements themselves.

In response to the first point, some make the argument that the issue stems from an excess of lawyers pursuing frivolous lawsuits. These individuals see the entire issue as emanating from the greed of plaintiff-side trial lawyers.

It is not surprising that so many of these challenges arise in situations involving vulnerable individuals. If there are concerns in the context of consumer versus entity,⁹¹ those concerns would be magnified when an element of vulnerability is added.⁹²

The trust situation may present the strongest example of situational vulnerability. The trust beneficiary may be a capable, intelligent, strong individual. However, that same individual may be vulnerable with regards to the trust. The vulnerability in that setting comes from the fact that the beneficiary is owed one of

that litigation often leads to adverse publicity among families). Attorney Blattmachr suggests an interesting twist to a traditional mandatory arbitration clause: combine the clause with an in terrorem model to state that the beneficiary who refuses to mediate or arbitrate in good faith forfeits his interest. *Id.* at 260-61.

89. *Halliday*, 873 So. 2d at 403.

90. *Id.* at 404.

91. See Sternlight, *Creeping Mandatory Arbitration*, *supra* note 3, at 1640-42 (describing the unique features and concerns of consumer arbitration).

92. See *id.* at 1641 (noting that “less educated” persons can be covered by arbitration, which means that fewer consumers understand the clauses to which they agree).

the strongest fiduciary duties in law: that of trustee to beneficiary.⁹³

In response to the second point, the lengths to which some courts will go to find a way to refuse to enforce an arbitration clause suggests to this author that courts are increasingly uncomfortable with enforcing mandatory pre-dispute arbitration agreements in the consumer context. It makes sense that this discomfort would be at its greatest when one of the parties to the arbitration is in a vulnerable position.

The best example of this may be the courts that have used contractual unconscionability as a way to refuse to compel arbitration. Unconscionability is viewed by many as a safety valve in the law of contracts.⁹⁴ It can be used by courts when faced with an otherwise valid contract that the court does not think should be enforced.

To this author, unconscionability is seldom desirable as a theory for deciding a case. Based as it is on whether the issue at hand shocks the conscience of the court, use of the doctrine leads to divergent results in situations involving substantially similar facts.

Further, it is important to note that even though most of the recent decisions uphold the arbitration agreement, many of the decisions reverse trial courts that refused to compel arbitration.⁹⁵ This suggests a discomfort at the trial court level about compelling arbitration in these cases.

The Supreme Court has recognized that the Federal Arbitration Act was enacted “to overrule the judiciary’s longstanding refusal to enforce agreements to arbitrate.”⁹⁶ Although Supreme Court precedent suggests a willingness to accede to congressional intent, state courts seem more reluctant. The resulting patchwork of state court precedent has led to uncertainty and contradictory results in similar cases. Even if two courts enforce arbitration agreements, different reasoning underlying the enforcement can lead to uncertainty as to what theory will work in the next case.

CONCLUSION

The time has come for an intense consideration of whether binding pre-dispute arbitration involving consumers is desirable. In light of the sweeping coverage of the Federal Arbitration Act as interpreted by the Supreme Court, the optimal vehicle for altering the enforceability of binding pre-dispute arbitration agreements involving consumers is reconsideration of the Federal Arbitration Act by Congress. Commentators have called for precisely such action,⁹⁷ and this author adds her

93. See, e.g., 1 MARK L. ASCHER ET AL., SCOTT AND ASCHER ON TRUSTS § 2.1.5 (5th ed. 2006) (“[The characteristics of a fiduciary relationship] exist in a particularly intense way in the relationship between trustee and beneficiary.”).

94. See generally Charles L. Knapp, *Blowing the Whistle on Mandatory Arbitration: Unconscionability as a Signaling Device*, 46 SAN. DIEGO L. REV. 609 (2009) (discussing the intersection of unconscionability doctrine and arbitration).

95. See, e.g., *Eddings*, 838 S.W.2d at 876 (reversing the trial court’s order denying a motion to compel arbitration).

96. *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219-20 (1985).

97. See generally ARBITRATION LAW IN AMERICA, *supra* note 1 (providing a collection of essays by various scholars, which call for changes to American arbitration law).

voice to their chorus.