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Alternative Dispute Resolution: The Federal Arbitration Act and Resolving Disputes in Arbitration versus a Court Proceeding

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ALTERNATIVE DISPUTE RESOLUTION: THE FEDERAL ARBITRATION ACT AND RESOLVING DISPUTES IN ARBITRATION VERSUS A COURT PROCEEDING

INTRODUCTION

Almost everyone enters into an agreement to arbitrate, whether aware of it or not. Arbitration clauses are now the standard method for resolving disputes in many consumer contracts, such as insurance, medical, and broker contracts. Standard arbitration agreements pose the quintessential question: when a dispute arises, and a person's competency to enter into the contract as a whole is challenged, is the arbitration agreement embedded within the contract enforceable?

With the passage of the Federal Arbitration Act ("FAA" or "Act") in 1925,[1] along with the federal government's power and authority to enforce the FAA, comes an emergent issue of determining when arbitration, rather than a court proceeding, must be used to resolve a dispute.[2] Due to arbitration provisions becoming more common in consumer contracts, many contract disputes, and accordingly many court opinions, will be based on the enforceability of arbitration agreements in years to come.[3] In fact, conflicting court decisions resolving arbitration agreements have been abundant since the enactment of the Act, and courts are still trying to reach a consistent pattern of uniformity to enforce arbitration provisions.[4]

The FAA establishes in Title 9 of the United States Code, Section 2, that "[a] written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising . . . shall be valid, irrevocable, and enforce-

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1 United States Arbitration Act, ch. 213, § 1, 43 Stat. 883, 883-86 (1925) (currently codified at 9 U.S.C. §§ 1-16 (2000)). Congress later renamed the United States Arbitration Act the Federal Arbitration Act and enacted it into law on July 30, 1947, ch. 392, § 1, 61 Stat. 674.

2. *See* Steven Shavell, *Alternative Dispute Resolution: An Economic Analysis*, 24 J. LEGAL STUD. 1, 1-3 (1995) (discussing the widespread use of alternative dispute resolution ("ADR") in resolving contract disputes and problems that arise); *see also* Spahr v. Secco, 330 F.3d 1266, 1273 (10th Cir. 2003) (holding the plaintiff's mental incapacity invalidated the entire contract as well as the embedded arbitration clause); Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 406-07 (1967) (holding that a claim of fraud in the inducement of the entire contract is a matter for arbitration, and not the court, when the contract contains a valid arbitration clause).

3. *See* Maureen A. Weston, *Checks on Participant Conduct in Compulsory ADR: Reconciling the Tension in the Need for Good-Faith Participation, Autonomy, and Confidentiality*, 76 IND. L.J. 591, 593-97 (2001) (discussing the widespread use of arbitration clauses in consumer and employment contracts and the potential for misconduct and abuse in the ADR process because of the participants' lack of good faith and the absence of judicial oversight or regulation).

4. David P. Pierce, *The Federal Arbitration Act: Conflicting Interpretations of Its Scope*, 61 U. CIN. L. REV. 623, 623-24 (1992) (discussing conflicting interpretations of the FAA in various state decisions).

able, save upon such grounds as exist at law or in equity for the revocation of any contract."[5] Additionally, Section 4 states that if a contract with an arbitration provision has been entered into, and the "making" of the arbitration agreement is not at issue, the court shall order the parties to proceed to arbitration.[6] Thus, many issues arise when an arbitration provision is placed in a contract because the agreement to arbitrate is made "valid, irrevocable, and enforceable," by federal statute, which can only become unenforceable under the same theories as a contract may become unenforceable under contract law.[7] Since the adoption of the FAA, arbitration agreements are increasingly used in resolving disputes that arise out of the contract as a whole, which undoubtedly favors businesses over consumers.[8]

This survey paper[9] explores the Tenth Circuit Court of Appeals opinion in *Spahr v. Secco*,[10] where the court decided that a mental capacity claim challenging the validity of a contract containing an arbitration agreement should be resolved in a court proceeding instead of arbitration.[11] Prior to *Spahr*, the Tenth Circuit had not addressed this issue.[12] Other circuits, however, have decided cases similar to *Spahr*.[13] Although the outcome in *Spahr* is different from the outcome other circuits reached in similar cases,[14] the holding in *Spahr* is likely to have important implications on future court decisions because *Spahr* readily provides a logical, fair, and rational method of evaluating the enforceability of arbitration agreements.

If *Spahr* is appealed to the United States Supreme Court, however, the Tenth Circuit's holding in *Spahr* may be reversed because the Supreme Court will likely want to maintain uniformity in court decisions pursuant to the *Prima Paint* rationale.[15] In contrast, if the Court can find

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5. 9 U.S.C. § 2.
6. *Id.* § 4.
7. *Id.* § 2.
8. Edward A. Dauer, *Judicial Policing of Consumer Arbitration*, 1 PEPP. DISP. RESOL. L.J. 91, 94-96 (2000) (discussing the widespread use of ADR and the asymmetries of arbitration that favors businesses over consumers).
9. The survey period runs from September 1, 2002, to August 31, 2003.
10. 330 F.3d 1266 (10th Cir. 2003).
11. *Spahr*, 330 F.3d at 1273.
12. *Id.* at 1267-68.
13. *See* Primerica Life Ins. v. Brown, 304 F.3d 469, 472 (5th Cir. 2002) (finding that a mental capacity claim challenging a contract containing an arbitration clause should be decided in arbitration); Jeske v. Brooks, 875 F.2d 71, 75 (4th Cir. 1989) (concluding that claims of unconscionability and lack of consideration challenging a contract containing an arbitration clause should be decided in arbitration); Unionmutual Stock Life Ins. Co. of Am. v. Beneficial Life Ins., 774 F.2d 524, 529 (1st Cir. 1985) (concluding that claims of mutual mistake and frustration of purpose challenging a contract containing an arbitration clause should be decided in arbitration).
14. *See Spahr*, 330 F.3d at 1272-73.
15. *See* Southland Corp. v. Keating, 465 U.S. 1, 11-13 (1984); Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983). States are also overturning decisions to uphold the *Prima Paint* rationale and maintain consistent holdings. *See, e.g., Primerica Life Ins.*, 304 F.3d at 472 (concluding that a challenge to a contract containing an arbitration clause should be decided in arbitration in accordance with the *Prima Paint* rationale).

sufficient public policy reasons to support *Spahr*,[16] the Court may alter their *Prima Paint* decision and create a new standard for arbitration agreements that combine the *Prima Paint* and *Spahr* rationales. Should this occur, arbitration will undergo a change for the better because the decision in *Spahr* adds a logical and fair method of interpreting the FAA that gives arbitration agreements their intended effect.[17] Thus, combining the *Prima Paint* and *Spahr* rationale will provide an enhanced method of evaluating arbitration agreements that is both rational and maintains the national legislative goals of favoring arbitration.

Part I of this survey examines the background of the FAA by looking at its history and formation, as well as relevant FAA provisions. Part II of this survey analyzes the Tenth Circuit's recent decision in *Spahr v. U.S. Bancorp Investments, Inc.*, where the Tenth Circuit held the arbitration provision unenforceable. Part III of this survey examines other recent circuit court rulings in similar arbitration cases. Finally, this paper takes the position that *Spahr* properly held a mental capacity challenge to a contract containing an arbitration agreement goes to the "making" of the arbitration agreement, and thus should be determined in a court proceeding.[18]

I. BACKGROUND

A. History and Formation of the FAA

With the number of cases being litigated on the rise, Congress passed the FAA in 1925 to make arbitration an equitable alternative to litigation that would reduce the number of cases in the court system.[19] As a result of increasing national hostility towards arbitration and courts' refusal to enforce arbitration agreements in contracts, Congress codified the FAA in Title 9 of the United States Code in 1947 to underscore the fact that federal policy favors arbitration agreements.[20] This codification aimed to place arbitration provisions "'upon the same footing as other

16. *See* Weston, *supra* note 3, at 593-97; Dauer, *supra* note 8, at 95-96. Arguably public policy warrants changing the current rationale regarding consumer arbitration agreements because they asymmetrically favor businesses and do not provide a fair outcome for consumers; consumers are forced into arbitration agreements for which they have not bargained, and are denied their right to a jury trial.

17. *See* Larry J. Pittman, *The Federal Arbitration Act: The Supreme Court's Erroneous Statutory Interpretation, Stare Decisis, and a Proposal for Change*, 53 ALA. L. REV. 789, 791-92, 806-11, 889-90 (2002) (discussing the problems with the Court's current statutory interpretation of the FAA and how changing to an originalist mode of statutory interpretation would better suit legislative intent).

18. *Spahr*, 330 F.3d at 1273.

19. *See* Southland Corp. v. Keating, 465 U.S. 1, 13-16 (1984); *see also* Richard C. Reuben, *Public Justice: Toward a State Action Theory of Alternative Dispute Resolution*, 85 CAL. L. REV. 577, 601 (1997) (discussing the history of arbitration in the United States in the early twentieth century).

20. Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 24-25 (1991) (quoting Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983)).

contracts'" by allowing courts to invalidate arbitration agreements only for the same reasons that other contracts could be invalidated.[21]

Additionally, Congress intended the FAA to be applicable in federal courts and state courts, pursuant to the Supremacy Clause.[22] In *Southland Corp. v. Keating* and *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, the Supreme Court took the position that the FAA trumped state statutes regulating arbitration agreements, thereby invalidating conflicting state laws.[23] The Supreme Court, however, held that "state law may be applied '*if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally.'"[24]

The Supreme Court has often reversed state court decisions that failed to enforce arbitration provisions in the same manner other contract provisions are enforced. In doing so, the Supreme Court has emphasized that they favor arbitration, pursuant to the legislative intent behind the Act.[25] By allowing state law to govern contracts generally, arbitration agreements are given the same standing and enforceability as other contracts because arbitration agreements are enforceable on the same grounds as any other contract.[26]

Arbitration is not inferior to litigation, but is simply a different method of resolving a dispute arising as "'a matter of contract,'"[27] in which a party is not required to arbitrate any dispute to which he has not agreed.[28] The Supreme Court has invalidated decisions where individual states refused to enforce arbitration provisions to the extent necessary to give those arbitration provisions the same enforceability as other contracts.[29]

The leading decision on the arbitrability of claims is *Prima Paint Corp. v. Flood & Conklin Mfg.*[30] In *Prima Paint*, the Supreme Court held that a claim for fraud in the inducement of the contract, which can invalidate the entire contract, instead of just the arbitration clause itself, should be resolved in arbitration.[31] The Court explained that unless there is concern that the claim involves the "making" of the arbitration provi-

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21. Doctor's Assocs., Inc. v. Casarotto, 517 U.S. 681, 687 (1996) (quoting Scherk v. Alberto-Culver Co., 417 U.S. 506, 511 (1974) (citation omitted)).

22. *Southland*, 465 U.S. at 16.

23. *See id.*; *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24-25.

24. *Casarotto*, 517 U.S. at 686-87 (quoting Perry v. Thomas, 482 U.S. 483, 492 n.9 (1987)).

25. *See id.* at 687-88; *Gilmer*, 500 U.S. at 24-26; *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24-25.

26. *Casarotto*, 517 U.S. at 686-87.

27. AT&T Techs. Inc. v. Communications Workers of Am., 475 U.S. 643, 648 (1986) (quoting United Steelworkers of Am. v. Warrior & Gulf Navigation Co., 363 U.S. 574, 582 (1960)).

28. *See* Reuben, *supra* note 19, at 605-07.

29. *See Casarotto*, 517 U.S. at 687; Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 275 (1995).

30. 388 U.S. 395 (1967).

31. *Prima Paint*, 388 U.S. at 406-07.

sion, Section 4 of the Act mandates the claim should be resolved by arbitration.[32]

Prima Paint also established the "separability doctrine," which severs arbitration clauses from the rest of the contract.[33] Where a claim does not attack the arbitration clause itself, but rather the entire contract, that claim must be resolved through arbitration.[34] This holding in *Prima Paint* may seem counterintuitive because a claim challenging the entire contract, including the making of the arbitration agreement, is subject to arbitration while a claim challenging only the arbitration agreement and not the entire contract may be resolved by the courts.[35] Although it may seem counterintuitive, *Prima Paint* established a rational and consistent pattern to determine which cases must be resolved by arbitration instead of by a court proceeding. Nonetheless, the *Prima Paint* rationale has been questioned because the holding reached by the Court arguably strayed from the FAA's language and legislative intent.[36] In so doing, the Court extended the FAA beyond cases involving interstate commerce and made arbitration agreements separable from the rest of the contract.[37]

Spahr v. Secco is a case of first impression in the Tenth Circuit[38] and will likely have a significant impact in determining when to mandate the arbitration of claims because *Spahr* adds a logical and fair method of interpreting the Act, even though it departs from *Prima Paint*. In sum, arbitration plays an important role in the litigation of consumer contracts. Moreover, conforming to uniform interpretations of the FAA is of great importance in future cases because uniformity will provide courts and consumers guidance in deciding whether to enter into or enforce contracts that contain arbitration agreements.

B. Relevant FAA Provisions

The key statutory provisions in the Act are Title 9 of the United States Code, Sections 2 through 4. Section 2 of the Act establishes that an arbitration provision is valid, irrevocable, and enforceable, but contains a "saving clause" allowing for an arbitration provision to be invali-

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32. *Id.* at 403-04.

33. *Id.* at 402-04.

34. *Id.* at 403-04; *see also* Tanya J. Monestier, *"Nothing Comes of Nothing" . . . Or Does It??? A Critical Re-Examination of the Doctrine of Separability in American Arbitration*, 12 AM. REV. INT'L ARB. 223, 224-27 (2001) (discussing the consistency with which U.S. case law has applied the *Prima Paint* severability doctrine to differentiate between contracts that are void and contracts that are voidable); Alan Scott Rau, *"The Arbitrability Question Itself,"* 10 AM. REV. INT'L ARB. 287, 331-36 (1999) (discussing misapplications of the *Prima Paint* doctrine).

35. *Prima Paint*, 388 U.S. at 403-04; *see also* Donald E. Johnson, *Has* Allied-Bruce Terminix Cos. v. Dobson *Exterminated Alabama's Anti-Arbitration Rule?*, 47 ALA. L. REV. 577, 609-10 (1996) (noting that although the rule in *Prima Paint* seems counterintuitive, it comports with the FAA).

36. *Prima Paint*, 388 U.S. at 407-08 (Black, J., dissenting). For further information on the legislative history of the FAA see the dissenting opinion.

37. *Id.* at 409-11 (Black, J., dissenting).

38. Spahr v. Secco, 330 F.3d 1266, 1267-68 (10th Cir. 2003).

dated under the standard contract defenses,[39] such as duress, fraud and unconscionability.[40] Section 3 of the FAA establishes that a court shall stay proceedings where the issue should be resolved in arbitration,[41] thereby limiting the court's authority to resolve disputes where the contract contains an arbitration provision.[42] Section 4 of the Act dictates when a court shall resolve a claim rather than requiring arbitration. This depends on whether the court is satisfied that the "making" of the agreement is not at issue.[43]

Section 2 of the FAA has been expanded to apply to state substantive and procedural policies in order to comply with the national policy favoring arbitration.[44] The Supreme Court progressively broadened the scope of cases to which the FAA extends by including contracts with arbitration agreements that do not involve interstate commerce.[45] The Supreme Court likewise interpreted Section 4 of the FAA to require that claims be arbitrated if the making of the arbitration agreement is not at issue.[46]

Section 4 of the Act is the key provision in many federal circuit cases because it allows a court to compel arbitration.[47] Section 4 of the FAA gives courts an opportunity to decide whether the claim goes to the

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39. *See* 9 U.S.C. § 2. Section 2 states in relevant part: "A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." *Id.*

40. *See Casarotto*, 517 U.S. at 687.

41. 9 U.S.C. § 3. Section 3 states:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

Id.

42. *See, e.g.*, *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 26 (stating that both state and federal courts are obligated to stay litigation under Section 3).

43. 9 U.S.C. § 4. Section 4 in part states:

> A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction . . . for an order directing that such arbitration proceed in the manner provided for in such agreement. . . . The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. . . . If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof.

Id.

44. *Southland*, 465 U.S. at 10-16; *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24; *see Prima Paint*, 388 U.S. at 404-05.

45. *See Prima Paint*, 388 U.S. at 401.

46. *See id.* at 402-04.

47. *See Prima Paint*, 388 U.S. at 403; *Spahr*, 330 F.3d at 1270; Primerica Life Ins. v. Brown, 304 F.3d 469, 472 (5th Cir. 2002).

"making" of the arbitration agreement, and if so, that claim may be decided by the court instead of through arbitration.[48] By interpreting Section 4 of the FAA in a manner requiring arbitration of almost all claims brought under a contract containing an arbitration agreement, courts progressively broadened the scope of cases subject to the FAA. In doing so, these courts arguably exceeded the legislative intent because arbitration agreements have been given more influence and effect than other contracts.[49]

II. UNITED STATES COURTS OF APPEALS DECISIONS

A. The Tenth Circuit

1. *Spahr v. Secco*[50]

In a case of first impression, the Tenth Circuit decided in *Spahr* whether parties raising a mental capacity challenge to the validity of an entire contract should be required to arbitrate according to the contract, or instead go to a court proceeding.[51] This section of the paper discusses the Tenth Circuit Court of Appeals' decision in *Spahr*.

a. Facts

In *Spahr v. Secco*, Spahr, an elderly man affected by Alzheimer's and dementia opened an investment account with U.S. Bancorp Investments, Inc. (U.S. Bancorp), whereby Spahr signed an agreement "promising to submit any controversy arising out of the account to arbitration . . . ."[52] Secco was a female employee working for U.S. Bancorp as Spahr's broker, investment advisor, and trustee.[53] Secco allegedly exploited Spahr by using sex to finagle him "out of large sums of money and real estate."[54] When Spahr's estate filed claims against U.S. Bancorp and Secco to seek recovery, U.S. Bancorp filed a motion to compel arbitration, pursuant to the agreement Spahr signed.[55]

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48. *Prima Paint*, 388 U.S. at 403-04; *Spahr*, 330 F.3d at 1269-70; *Primerica Life Ins. Co.*, 304 F.3d at 472.

49. For a detailed examination of the legislative history of the FAA, see IAN R. MACNEIL, AMERICAN ARBITRATION LAW 83-121 (Oxford University Press 1992).

50. 330 F.3d 1266 (10th Cir. 2003).

51. *Spahr*, 330 F.3d at 1267-68.

52. *Id.* at 1268. The agreement in this case involves a Cash Account Agreement that stated:
I agree that any controversy arising out of or relating to my account, to transactions with or for me or to this agreement or the breach thereof, whether executed or to be executed within or outside of the United States, and whether asserted against broker-dealer and/or its present or former agents or employees, will be settled by arbitration before and in accordance with the then current rules of the National Association of Securities Dealers, Inc. [("NASD")].
Id.

53. *Id.*

54. *Id.*

55. *Id.*

The district court denied U.S. Bancorp's motion to compel arbitration, holding the agreement to arbitrate between Spahr and U.S. Bancorp was unenforceable because Spahr lacked the requisite mental capacity to comprehend the nature and effect of the contract.[56] U.S. Bancorp and Secco appealed the district court's decision, claiming Spahr's mental incompetence challenge to the agreement should never have been heard by the court and instead should have been resolved in arbitration.[57]

b. Decision

In *Spahr*, the Tenth Circuit Court of Appeals affirmed the district court's ruling that the agreement is not subject to the arbitration provision.[58] The Tenth Circuit explained that because Spahr lacked the mental capacity to contract, the claim was not subject to arbitration because the entire contract was void.[59]

The Tenth Circuit considered whether parties raising mental capacity claims challenging the validity of an entire contract should be required to arbitrate pursuant to the contract.[60] The court reviewed whether language in Section 4 of the FAA provides judicial relief to cases where the entire contract, including the arbitration agreement, is challenged.[61] In cases such as *Spahr*, where the making of the arbitration agreement is at issue, the court retains the power to determine whether the arbitration agreement is valid.[62] In reaching this decision, the Tenth Circuit appellate court distinguished other circuit decisions from *Spahr*,[63] therein providing a logical and useful analysis. *Spahr* reached a different outcome than other circuits have reached in similar cases because the Tenth Circuit interpreted Section 4 of the Act as distinguishing between contract claims that make a contract void, which should be heard by a court, and contract claims that make the contract voidable, which should be resolved in arbitration.[64] Therefore, if a contract claim would risk making the entire agreement void, including the arbitration agreement, a court should hear that claim; whereas a contract claim merely making the contract voidable that does not place the "making" of the arbitration agreement at issue should be resolved in arbitration.[65]

56. *Id.*
57. *Id.* at 1269.
58. *Id.* at 1267-68.
59. *Id.* at 1273.
60. *Id.* at 1272-73.
61. *Id.* at 1271.
62. *Id.* at 1269.
63. *Id.* at 1272-73.
64. *See id.*
65. *Id.*

c. Analysis of the Tenth Circuit's Holding in *Spahr v. Secco*

In *Spahr*, the Court began by applying Title 9 of the United States Code, Section 4, holding that "[i]t has long been a tenet of federal arbitration law that 'arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.'"[66] Thus, when a dispute arises that relates to the contract as a whole, and includes a broad arbitration agreement, there is not "the requisite clear and unmistakable evidence 'within the four corners of the . . . [a]greement that the parties intended to submit the question of whether an agreement to arbitrate exists to an arbitrator.'"[67]

Additionally, the Tenth Circuit held in *Spahr* that the *Prima Paint* holding did not apply to the facts in *Spahr* because "[u]nlike a claim of fraud in the inducement, which can be directed at individual provisions in a contract, a mental capacity challenge can logically be directed only at the entire contract" and thus goes to the making of the contract and should be decided in a court proceeding pursuant to Section 4.[68] The Tenth Circuit then applied Section 4, determining that a mental capacity claim does go to the making of the contract, and thus should be decided by a court rather than an arbitrator.[69]

The Tenth Circuit's decision in *Spahr*, that the mental capacity challenge goes to the "making" of the contract and thus should be decided by a court instead of an arbitrator, is likely to be criticized for departing from the position of the Supreme Court and other circuits in similar cases following *Prima Paint*.[70] The determination that a claim goes to the "making" of the contract and thus may be decided by a court pursuant to Section 4 will likely be used in rare circumstances because of the court's strong favor for arbitration, which is shown in court decisions that consistently uphold the FAA.[71] The Supreme Court is likely to hold that a case involving a mental capacity challenge is analogous to a claim of fraud in the inducement, in that both challenge the validity of the entire contract without questioning the "making" of the arbitration provision

66. *Id.* at 1269 (quoting AT&T Techs., Inc. v. Communications Workers of Am. 475 U.S. 643, 648 (1986)).

67. *Id.* at 1270 (quoting Riley Mfg. v. Anchor Glass Container Corp., 157 F.3d 775, 780 (10th Cir. 1998)).

68. *Id.* at 1273.

69. *Id.*

70. *See* Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 403-04 (1967); Primerica Life Ins. v. Brown, 304 F.3d 469, 471 (5th Cir. 2002); Jeske v. Brooks, 875 F.2d 71, 72 (4th Cir. 1989); Unionmutual Stock Life Ins. Co. of Am. v. Beneficial Life Ins., 774 F.2d 524, 528-29 (1st Cir. 1985).

71. *See Prima Paint*, 388 U.S. at 402; Doctor's Assocs. Inc. v. Casarotto, 517 U.S. 681, 683 (1996); Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 23-26 (1991); Southland Corp. v. Keating, 465 U.S. 1, 17 (1984).

itself, and therefore both should be submitted to arbitration according to the agreement.[72]

To maintain consistency in their decisions, the Court may decide to reverse the decision in *Spahr*.[73] This may occur because after the Supreme Court made its decision in *Prima Paint*, other courts have consistently upheld the *Prima Paint* rationale by reversing inconsistent cases and setting a uniform standard of review for courts on every level.[74] There are compelling public policy reasons, however, for the Supreme Court to alter its decision in *Prima Paint* by incorporating the *Spahr* holding in deciding the arbitrability of claims that challenge contracts containing arbitration agreements. The primary public policy reasons include the fact that *Prima Paint* favors businesses over consumers, forces consumers into agreements they have not bargained for, and denies individuals their constitutional right to a jury trial.[75]

Although legislative intent stresses a national policy favoring arbitration, Congress has not displayed such favor towards businesses.[76] Regardless, the outcome of many arbitration disputes resulted in decisions unquestionably favoring businesses, leaving consumers in a position for which they never bargained.[77] *Prima Paint* and other decisions following its rationale do this very thing by favoring businesses and their adhesive agreements that unfairly bind consumers.[78] The challenge of enforcing arbitration agreements while not overstepping legislative intent is an obstacle courts will face in years to come. Arguably this challenge could best be overcome by adopting *Spahr* because *Spahr* reasonably and logically applies the Act without enforcing adhesive contracts that favor businesses.

Additionally, the constitutional right to a jury trial should not be overcome by an arbitration provision within a contract, when a party is challenging the validity of that entire contract, as this deprives the individual of the right to a jury trial and contravenes the legislative intent.[79] With these public policy reasons in mind, the Supreme Court would be reasonable and correct in adopting the *Spahr* decision as part of the standard in determining whether a claim challenging a contract containing an arbitration agreement should be resolved in a court proceeding rather than arbitration.

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72. *See Prima Paint*, 388 U.S. at 402; *Casarotto*, 517 U.S. at 683; *Gilmer*, 500 U.S. at 23-26; *Southland*, 465 U.S. at 17.

73. *See Primerica Life Ins.*, 304 F.3d at 472.

74. *Id.*

75. *See* Dauer, *supra* note 8, 94-96; Weston, *supra* note 3, at 600-01.

76. 9 U.S.C. §§ 1-16.

77. *See supra* note 13; *Casarotto*, 517 U.S. at 683.

78. Arguably, enforcing arbitration agreements against consumers favors businesses. *See Prima Paint*, 388 U.S. at 400-06.

79. *See Prima Paint*, 388 U.S. at 407-12 (Black, J., dissenting); MACNEIL, *supra* note 49, 83-121.

The Tenth Circuit's opinion in *Spahr*, which holds that a mental capacity claim goes to the "making" of the contract and should be heard by a court instead of an arbitrator,[80] appears to subject contracts with or without arbitration provisions to the same requirements. The trend of federal courts to enforce arbitration provisions in the manner Congress intended[81] at times gives contracts containing arbitration provisions more obstacles than those without arbitration provisions.[82] Consumers entering into such agreements are experiencing outcomes they might not logically expect, especially in cases where an arbitrator, rather than a judge, decides if an arbitration provision within a contract is enforceable.[83] The issue raises a serious problem in consumer contracts, because if a party is fraudulently induced into entering a contract, and the subsequent claims are then subjected to arbitration, that party arguably never entered into any valid agreement, let alone an agreement to arbitrate.[84] This contradiction produces unpredictable and illogical outcomes because contracts without an arbitration clause are held to a different standard than contracts containing them.[85]

Although the Tenth Circuit's opinion in *Spahr* departs from the *Prima Paint* rationale,[86] *Spahr* is nonetheless logical, fair, and provides a rational method of evaluating arbitration agreements. The main distinction between *Spahr* and *Prima Paint* is how and where these two courts draw the line in determining whether the "making" of the agreement to arbitrate shall be resolved by a court rather than arbitration.

The *Prima Paint* rationale focused on whether the challenge to the agreement goes to the "making" of the entire contract, versus the "making" of the arbitration provision, to determine whether the dispute should be resolved in a court rather than arbitration.[87] *Prima Paint* held that if a contract defense challenges the contract as a whole, it should be resolved

80. *Spahr*, 330 F.3d at 1272-73.

81. *See Casarotto*, 517 U.S. at 682-89; *Southland*, 465 U.S. at 5-7.

82. *See Casarotto*, 517 U.S. at 681-86; *Gilmer*, 500 U.S. at 24-26; *Southland*, 465 U.S. at 5-6; *Prima Paint*, 388 U.S. at 402; *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529. *See generally* Edward A. Dauer, *Contracts of Adhesion in Light of the Bargain Hypothesis: An Introduction*, 5 AKRON L. REV. 1 (1972) (analyzing the pros and cons of arbitration provisions); Richard M. Alderman, *Pre-Dispute Mandatory Arbitration in Consumer Contracts: A Call for Reform*, 38 HOUS. L. REV. 1237 (2001) (discussing the shortcomings of arbitration provisions).

83. Rau, *supra* note 34, at 303-06; *see also* Alderman, *supra* note 82, at 1242.

84. *See* Pittman, *supra* note 17, at 790-93 (discussing adhesion contracts and the their negative effect on consumer contracts in stating, "there has been, and currently is, a legitimate concern over the use of adhesion contracts that force consumers to accept arbitration to resolve future disputes, including personal injury claims as well as contractual claims, arising out of their purchases of consumer goods.").

85. Rau, *supra* note 34, at 293.

86. *Compare Prima Paint*, 388 U.S. at 402-04, *with Spahr*, 330 F.3d at 1270-75.

87. *See Prima Paint*, 388 U.S. at 403-04.

in arbitration; whereas if the contract defense challenges the arbitration provision alone, a court should resolve the claim.[88]

Spahr, on the other hand, focused on what contract defenses challenge the "making" of the agreement to arbitrate, without limiting the defenses to those challenging the arbitration agreement itself.[89] *Spahr* determined contract defenses making the entire contract void should be resolved by a court instead of through arbitration.[90] Contract defenses making the contract voidable, however, do not specifically challenge the "making" of the arbitration agreement and should be resolved in arbitration.[91] The Tenth Circuit in *Spahr* did not contradict the *Prima Paint* rationale. Instead, *Spahr* chose a different method of analyzing the word "making," as set out in Section 4 of the Act.[92]

Overall, it appears that when a party is using a contract defense to invalidate a contract, the court's goal is to determine whether the "making of the agreement for arbitration . . . is not in issue" before compelling arbitration.[93] At this point the court will determine whether the contract defense should be reserved for courts to decide, which inevitably creates a potential conflict between Congress's intention to favor arbitration of claims, and an individual's right to not be obligated to arbitrate an agreement considered void pursuant to contract law. The courts then must decide which claims they will hear and which claims must proceed to arbitration, according to the agreement, in a realistic manner so that all claims alleging a contract defense will not end up in court. Giving every claim a court date would defeat the purpose of the FAA in trying to enforce arbitration provisions in order to reduce "costliness and delays of litigation."[94]

Both *Prima Paint* and *Spahr* attempt to find the appropriate place to draw the line in allowing certain cases to be heard by a court instead of requiring arbitration. Although *Prima Paint* and *Spahr* arrive at different outcomes in distinguishing between cases that must go to arbitration versus a court proceeding, both approaches are useful in trying to establish a workable rationale. Although *Prima Paint* and *Spahr* are not without their drawbacks in achieving logical and realistic outcomes,[95] a common

88. *Id.*
89. *See Spahr*, 330 F.3d at 1271-73.
90. *Id.* at 1273.
91. *See id.* at 1271-73.
92. *See id.*
93. 9 U.S.C. § 4.
94. Hai Jiang, *Do We Allow Contract Law to Administer Civil Rights Remedies?*, 2003 DETROIT COLL. L. MICH. ST. U. L. REV. 251, 273.
95. *See Prima Paint*, 388 U.S. at 395-407; *Spahr*, 330 F.3d at 1266-75. Arguably there are downfalls in the *Prima Paint* decision because although *Prima Paint* offers a reasonable analysis of when to send a case to arbitration instead of a court proceeding, subsequent outcomes achieved from *Prima Paint's* rationale at times do not seem logical and may not fully withstand the analytical scrutiny of other courts. Additionally in *Spahr*, there are downfalls as well because in separating out contract defenses that make a contract void, and then allowing those cases to be heard in court could

middle ground between the *Prima Paint* and *Spahr* opinions might allow arbitration provisions to receive the same "footing" as other contract provisions, yet loosen the adhesion many consumer arbitration provisions currently face.[96]

Other circuits have considered whether a contract defense invalidating an arbitration agreement should be resolved by arbitration rather than a court proceeding.[97] This paper now examines how these circuits resolve the arbitration dilemma.

B. Fifth Circuit

1. *Primerica Life Ins. v. Brown*[98]

a. Facts

Brown executed an agreement with CitiFinancial's affiliate, Primerica Life Insurance Co., which contained "an arbitration clause requiring arbitration of [Brown's] claims."[99] When a claim arose, Brown alleged he lacked the mental capacity to enter into the contract and therefore was not bound to the arbitration agreement because the contract was invalid.[100] The district court agreed, holding the arbitration provision unenforceable because Brown lacked the mental capacity to contract.[101]

b. Decision

In *Primerica*, the Fifth Circuit appellate court reversed the district court, holding that a mental capacity challenge to the entire contract must go to arbitration pursuant to the arbitration clause.[102] Relying on *Prima Paint*, the Fifth Circuit reasoned that pursuant to Section 4 of the FAA, federal courts may only consider "issues relating to the making and performance of the agreement to arbitrate."[103] The court explained that Brown's mental capacity claim challenged the entire contract without specifically challenging the arbitration clause, and thus issues relating to arbitration agreements were never disputed.[104] Without any issues relating to the arbitration agreement in controversy, the court determined it

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lead to the same problem that the FAA wanted to prevent; which includes reducing cases in the courts and not allowing the courts to give arbitration provisions less "footing" than other contract provisions.

96. *See, e.g., Prima Paint*, 388 U.S. at 423 (Black, J., dissenting) (recognizing the "purpose of the Act was to place arbitration agreements upon the same footing as other contracts" (internal quotations omitted)); *Casarotto*, 517 U.S. at 682 (recognizing and applying same principal); *Gilmer*, 500 U.S. at 24 (same); *Southland*, 465 U.S. at 15-16 (same).

97. *Spahr*, 330 F.3d at 1272.

98. 304 F.3d 469 (5th Cir. 2002).

99. *Primerica Life Ins.*, 304 F.3d at 470.

100. *Id.* at 471.

101. *Id.*

102. *Id.* at 472.

103. *Id.*

104. *Id.*

lacked authority to hear Brown's contract defense and submitted the claim to arbitration.[105]

C. Fourth Circuit

1. *Jeske v. Brooks*[106]

a. Facts

Jeske, an investor, sought investment advice from Brooks, an employee at an investment firm.[107] When Jeske entered into an investor relationship with Brooks, he signed an agreement that "contained an arbitration clause covering all disputes over matters relating to the agreement."[108] After suffering losses stemming from Brook's investment advice, Jeske filed claims against Brooks and Brooks' investment firm.[109] When Brooks asked the court to stay the proceedings and compel arbitration pursuant to the agreement, the district court compelled arbitration of the state law claims, but refused to require arbitration of the federal claims.[110]

b. Decision

In *Jeske*, the Fourth Circuit held that claims of unconscionability and lack of consideration challenge the entire contract's formation and as such should be decided by arbitration.[111] Relying on *Prima Paint*, the Fourth Circuit determined that when a claim challenges the validity of an entire contract, and the arbitration provision within the contract is not specifically challenged, the question regarding the contract's validity is within the scope of arbitration.[112] The court ignored the potential conflict that may exist when an entire contract is invalid as a matter of law, and thus the embedded arbitration clause is inapplicable, yet the claim must first go to arbitration to determine whether or not the contract is valid.[113]

105. *Id.*
106. 875 F.2d 71 (4th Cir. 1989).
107. *Jeske*, 875 F.2d at 72.
108. *Id.*
109. *Id.*
110. *Id.* at 72-73.
111. *Id.* at 75.
112. *Id.*
113. *See id.*

D. First Circuit

1. *Unionmutual Stock Life Ins. Co. of America v. Beneficial Life Ins.*[114]

a. Facts

Unionmutual and Beneficial, both insurance companies, entered into a "Portfolio Indemnification Reinsurance Agreement" which included an arbitration clause requiring any dispute arising from the indemnification agreement to be arbitrated in Portland, Maine.[115] After forming the agreement, Beneficial contacted Unionmutual to rescind the indemnification agreement, stating that the recent passage of the Deficit Reduction Tax Act "frustrated the purpose of the contract."[116] The district court granted Unionmutual's motion to compel arbitration of Beneficial's dispute.[117]

b. Decision

On appeal, the First Circuit appellate court affirmed, holding that claims of mutual mistake and frustration of purpose challenging the making of the entire contract should be decided by an arbitrator.[118] Relying on the severability doctrine discussed in *Prima Paint*, the court took the position that arbitration clauses "'are 'separable' from the contracts in which they are embedded, and that where no claim is made that fraud was directed at the arbitration clause itself, a broad arbitration clause will be held to encompass arbitration of the claim that the contract itself was induced by fraud.'"[119] The First Circuit court reasoned that Beneficial's attempt to invalidate the entire contract lacked an independent challenge to the validity of the arbitration agreement.[120] Without an independent challenge separating the arbitration agreement from the rest of the contract, the court determined arbitration was the appropriate forum to decide the validity of the contract.[121]

III. ANALYSIS

Several federal circuit courts of appeal reviewed cases involving contract defenses as applied to arbitration agreements.[122] Among the de-

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114. 774 F.2d 524 (1st Cir. 1985).
115. *Unionmutual Stock Life Ins.*, 774 F.2d at 525.
116. *Id.*
117. *Id.*
118. *Id.* at 529.
119. *Id.* at 528 (quoting Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 402 (1967)).
120. *Id.* at 529.
121. *Id.*
122. *See* Primerica Life Ins. v. Brown, 304 F.3d 469, 472 (5th Cir. 2002); Jeske v. Brooks, 875 F.2d 71, 75 (4th Cir. 1989); Unionmutual Stock Life Ins. Co. of Am. v. Beneficial Life Ins., 774 F.2d 524, 529 (1st Cir. 1985).

cisions discussed above, these courts all relied on the *Prima Paint* rationale in their decisions.[123] *Primerica*, *Jeske*, and *Unionmutual*, each held the contact claims in these cases were subject to arbitration, pursuant to the arbitration agreement in the contract, because the contract defenses challenged the overall contract and not the making of the arbitration agreement itself.[124] In each of these cases, the respective court applied the *Prima Paint* rationale in questioning whether the claim challenged the contract as a whole or just the arbitration agreement, to determine that each claim was subject to arbitration because each challenged the entire contract.[125]

The *Prima Paint* doctrine these circuits apply seems easily overcome if a party simply challenges the "making" of the arbitration agreement, in which case the party will receive a court hearing.[126] Otherwise, if the party challenges the contract as a whole, the party is subject to arbitration.[127] Therefore, to receive a court hearing and not be subject to arbitration, a party need only assert a claim challenging the arbitration agreement itself, instead of the entire contract.[128] This seems unreasonable and against the clear legislative intent behind the FAA.[129]

In *Spahr v. Secco*, the Tenth Circuit court interpreted Section 4 of the Act, holding that claims making a contract void, rather than voidable bring the "making" of the entire agreement, including the agreement to arbitrate, into issue and should be resolved in a court proceeding.[130] *Spahr* would likely reach a different outcome than the First, Fourth, and Fifth Circuits reached in similar cases because *Spahr* held contract defenses making the entire contract void also challenge the "making" of the arbitration agreement and should be resolved by a court.[131] *Spahr* draws the line between contract defenses challenging the "making" of an arbitration agreement, even if the defense challenges the entire contract as well, and contract defenses that do not.[132] According to *Spahr*, if a claim challenges the "making" of the arbitration agreement, a court should

123. *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529.

124. *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529.

125. *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529.

126. *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529.

127. Primerica Life Ins., 304 F.3d at 472; Jeske, 875 F.2d at 75; Unionmutual Stock Life Ins., 774 F.2d at 529.

128. *Primerica Life Ins.*, 304 F.3d at 472; *Jeske*, 875 F.2d at 75; *Unionmutual Stock Life Ins.*, 774 F.2d at 529.

129. Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395. 407-12 (1967) (Black, J., dissenting) (citing to specific legislative history for enacting the FAA); MACNEIL, *supra* note 49, at 83-121.

130. Spahr v. Secco, 330 F.3d 1266, 1267-68 (10th Cir. 2003).

131. *See Spahr*, 330 F.3d at 1267-68.

132. *See id.*

resolve that claim, regardless of the fact that the claim challenges the entire contract instead of just the arbitration agreement.[133] *Spahr's* reasoning not only takes into account whether the arbitration provision or the entire contract was being challenged, but whether the "making" of the arbitration agreement is at issue.[134]

The Tenth Circuit's decision in *Spahr* contributed to a split among the circuit courts[135] regarding different applications of Section 4 of the Act.[136] The Tenth Circuit explicitly disagreed with the Fifth Circuit in *Primerica Life Ins. v. Brown*,[137] holding that where a party claims a lack of mental capacity to enter into a contract, a court rather than an arbitrator should decide the claim.[138]

As *Spahr* reasoned, a person should not be subject to arbitration when he or she has not so agreed.[139] Therefore, when the "making" of a contract containing an arbitration agreement is at issue, it seems implicit that the person never agreed to arbitrate. The *Spahr* rationale takes into account the "tenet of federal arbitration law" in holding that regardless of whether the challenge goes to the "making" of the entire contract or the "making" of the arbitration agreement, a party should not be forced to submit a dispute to arbitration unless there was consent.[140] *Spahr* is different from *Prima Paint* because the latter distinguishes between whether the claim challenges the entire contract or the arbitration provision within the contract, and then resolves the claims that challenge the entire contract through arbitration.[141] Although the *Spahr* and *Prima Paint* rationales are not contradictory because they both apply similar interpretations of Section 4, their rationales do produce dissimilar results because of the different interpretations of the word "making."[142] As such, the Tenth Circuit's reasoning in *Spahr* is arguably the better approach in determining what cases should be heard by a court because the *Spahr* analysis truly questions whether the claim goes to the "making" of the agreement to arbitrate, rather than looking at whether the claim challenges the entire contract or the arbitration agreement alone.[143] *Spahr's* approach maintains a logical, fair, and rational method of evaluating arbitration agreements that gives them the same standing and enforceability as other contracts receive.

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133. *Id.*
134. *See id.*
135. *Id.*
136. *See* id.
137. 304 F.3d at 472 (holding a mental capacity defense that goes to the making of the entire contract must be arbitrated).
138. *Spahr*, 330 F.3d at 1272.
139. *Id.* at 1268.
140. *Id.* at 1269-75.
141. *See id.*; *Prima Paint*, 388 U.S. at 402-07.
142. *Prima Paint*, 388 U.S. at 402-07; *Spahr*, 330 F.3d at 1269-70.
143. *Spahr*, 330 F.3d at 1271-73.

Should the U.S. Supreme Court hear *Spahr*, its decision will affect not only the future of arbitration agreement enforceability, but also the fundamental procedural fairness for those entering into contracts containing them. Although *Spahr* reaches a different outcome from other circuit courts in cases with similar facts,[144] the Court will have the opportunity to create a fairer standard in arbitration agreement enforceability that is based on public policy concerns. The primary policy reasons for adopting *Spahr's* rationale is the promotion of fairness in the legal system by giving consumers the same treatment and protection businesses receive under the law, enforcing contracts consumers have freely bargained for, and affording individuals their constitutional right to a jury trial.[145] These are all important public policy reasons because the legal system is based in large measure on principles of equity, and currently the Court's stance on arbitration agreements strongly favors businesses, and unfairly binds consumers.[146] By adopting the Tenth Circuit's decision in *Spahr*, the Court better promote the goals of the Federal Arbitration Act .

CONCLUSION

With Congress passing the FAA in 1925 and the United States Supreme Court holding arbitration as a comparable means to litigation, deserving of the same "footing" as other contract provisions,[147] it is apparent the use of arbitration agreements will continue to grow consumer contracts. Arbitration is likely to play an important role in many future contract cases in the Tenth and other circuits, which is why it is so important to understand the opinion in *Spahr*.

When the Tenth Circuit in *Spahr* stated that a court should hear a case involving a mental capacity claim that challenges the validity of the entire contract,[148] it effectively established a new method of analyzing contract defenses that attack the validity of arbitration clauses. *Spahr* thus established a useful alternative to the *Prima Paint* rationale in determining whether a court shall hear a case or compel arbitration.[149] The rationale in *Spahr* may initially create confusion when compared to *Prima Paint* because *Spahr* seemingly reaches the opposite outcome from *Prima Paint* in cases with similar facts.[150] *Spahr*, however, does give an applicable interpretation of the word "making,"[151] as set forth in the Section 4 of the Act. This interpretation will likely aid courts in de-

144. *See supra* note 13.
145. *See* Dauer, *supra* note 8, 94-96; Weston, *supra* note 3, at 600-01.
146. *See* Dauer, *supra* note 8, 94-96; Weston, *supra* note 3, at 600-01.
147. *See* Doctor's Assocs. Inc. v. Casarotto, 517 U.S. 681, 687 (1996); Southland Corp. v. Keating, 465 U.S. 1, 7-18 (1984).
148. *See* Spahr v. Secco, 330 F.3d 1266, 1272 (10th Cir. 2003).
149. *Spahr*, 330 F.3d at 1272-75.
150. *See* Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 402 (1967); *Spahr*, 330 F.3d at 1272.
151. *See Spahr*, 330 F.3d at 1272.

ciding cases while sustaining the intended purpose of the FAA. Importantly, the *Spahr* holding is critical in achieving outcomes that truly place arbitration provisions on the same "footing" as other contract provisions.[152]

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152. *See Casarotto*, 517 U.S. at 681-86.

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