Explaining Waiver of Court Trial in Arbitration Agreements

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When an agreement provides for arbitration, what language waiving access to the courts will be enforceable, particularly when one of the parties may be unsophisticated?

Recently, the Supreme Court of New Jersey issued an opinion in *Atalese v. U.S. Legal Services Group*, Nos. A-64 September Term 2012, 072314, 9/23/14, that will surprise those who have been drafting agreements compelling mandatory arbitration. It held that the arbitration provision was unenforceable because it did not contain specific language that the "plaintiff was waiving her statutory right to seek relief in a court of law."

The plaintiff, Patricia Atalese, had entered into a service contract for debt adjustment with U.S. Legal Services Group, but refused to pay, claiming misrepresentations with respect to its services and status as a licensed debt adjuster, as well as violations of the state's usury law.

USLSG moved to compel arbitration based upon the following provision: "In the event of any claim or dispute between client and the USLSG related to this agreement … the claim or dispute shall be submitted to binding arbitration upon the request of either party. … The parties shall agree on a single arbitrator to resolve the dispute. Any decision of the arbitrator shall be final and may be entered into any judgment in any court of competent jurisdiction."

The Appellate Division affirmed the trial court's decision compelling arbitration. It concluded that although the arbitration clause did not specifically state that Atalese was giving up her right to a court trial, it gave the parties "'reasonable notice of the requirement to arbitrate all claims under the contract' and that 'a reasonable person by signing the agreement [would have understood] that arbitration is the sole means of resolving contractual disputes.'"

On appeal, Atalese contended that New Jersey law required a specific statement that the party was waiving its right to court trial or that arbitration was the exclusive available remedy.

USLSG asserted, however, that any reasonable consumer would understand that arbitration is different from litigation, that the arbitration clause was sufficiently clear and that it adequately advised that the matter would be resolved in an arbitration forum. It further asserted that this result was mandated by the "liberal federal policy favoring arbitration" under the Federal Arbitration Act (FAA), and that arbitration agreements

should be placed "on an equal footing with other contracts" and enforced in accordance with their terms.

The court acknowledged that both the FAA and the New Jersey Arbitration Act were nearly identical and do "enunciate federal and state policies favoring arbitration."

It noted that "Section 2 of the FAA provides that [a] written provision in … a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction … shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."

While recognizing that arbitration agreements cannot be subjected to more burdensome requirements than other agreements, the court added that, "Arbitration's favored status does not mean that every arbitration clause, however phrased, will be enforceable. ... The FAA 'permits states to regulate … arbitration agreements under general contract principles' and a court may invalidate an arbitration clause 'upon such grounds as exist at law or in equity for the revocation of any contract.'" Otherwise stated, whether a valid agreement to arbitrate exists will generally be determined by state law.

The court continued that any contract, including an agreement to arbitrate, "must be the product of mutual assent, as determined under customary principles of contract law." Such mutual assent requires a full understanding of the terms of the agreement, and, where a waiver is involved, "full knowledge of his legal rights and intent to surrender those rights."

In the case of arbitration, which involves the waiver of a court trial, the court concluded that, "An average member of the public may not know—without some explanatory comment—that arbitration is a substitute for the right to have one's claim adjudicated in a court of law." Accordingly, particular care is taken to ensure that there is a "'knowing assent of both parties to arbitrate and a clear mutual understanding of the ramifications of that assent.'"

Moreover, such "particular care" is neither specific to nor does it impose an extra burden on arbitration clauses, as such is required in any contract containing a waiver of rights (citing, as examples, rights relating to mechanics' liens, certain evidentiary materials, and labor grievances). In all such cases, the waiver must be "'clearly and unmistakably established.'"

Finally, no specific "form of words" is required. To illustrate, the court provides varying language from other cases deemed sufficient to put a party on notice that arbitration is a waiver of a right to sue in court.

What deficiencies, then, were found by the court with respect to the USLSG arbitration provisions?

First, the court twice mentions that the arbitration clause appears on page nine of a 23-page contract. While not specifically identified as a defect, the court may have had some concern that a critical waiver-of-rights provision was buried in a lengthy contract without any indication of its significance.

More importantly, Atalese asserted that USLSG had violated two consumer protection statutes "both of which explicitly provide remedies in a court of law." The arbitration clause, however, neither mentioned nor explained "that plaintiff is waiving her right to seek relief in court for breach of her statutory rights."

The court recognizes that the agreement does provide that a single arbitrator will resolve the dispute, that the arbitrator's decision will be final and might be entered as a final judgment in any court of competent jurisdiction.

What the court finds missing, however, is an explanation of "what arbitration is" or how it differs from a proceeding in a court of law. "Nor is it written in plain language that would be clear and understandable to the average consumer that she is waiving statutory rights."

Although the court does not require reference to the specific constitutional or statutory right being waived, it held that there must be, at the very least, sufficiently broad or general language explaining that the plaintiff was giving up her right to a court or jury trial. In addition, while no specific words or prescribed formulae are required, the message they deliver must be clear and unambiguous, as they would be in any other agreement in which constitutional or statutory rights were being waived.

To further reflect the scope of its requirement of a clear and unambiguous waiver, the court, in footnote 2, specifically found the following language in another New Jersey Appellate Division case to be insufficient: "Any other unresolved dispute arising out of this agreement must be submitted to arbitration"; and, "The arbitrators would have exclusive jurisdiction over the entire matter in dispute, including any question as to arbitrability." (Interestingly, Atalese apparently argued that such exclusivity language would have satisfied the requirement.)

It would not appear that this decision of the New Jersey Supreme Court is consistent with federal precedent or that other jurisdictions are likely to conclude that such specificity is required in all arbitration agreements when one of the parties may be insufficiently knowledgeable about arbitration or understand the implicit waiver of court trial.

What is certain, however, is that parties resisting submission to arbitration in New Jersey and beyond will reference this decision. In addition, it will, in all likelihood, be relied upon not only in consumer cases but also in other disputes involving claims of individuals.

Accordingly, when drafting arbitration provisions, attention to the comments, acceptable illustrations and conclusions of the New Jersey Supreme Court would appear to reflect a wise precaution.