

**The Alternatives After *Grafton Partners*
For Drafting and Enforcing
Alternative Dispute Resolution Clauses**

**A Presentation for San José Bank Attorneys Association
November 18, 2005**

**Peter M. Rehon, Esq.
REHON & ROBERTS
A Professional Corporation
Ten Almaden Boulevard, Suite 550
San José, California 95113**

**Telephone: (408) 494-0900
Facsimile: (408) 494-0909
prehon@rehonroberts.com**

www.rehonroberts.com



© Copyright 2005, Rehon & Roberts, A Professional Corporation.

This material is designed to provide topical legal information of interest to attorneys, friends and clients of our firm. It is not intended to constitute, and should not be considered to be, legal advice. If you have any questions regarding the general or specific application of the legal principles described in this material, please consult an attorney.

**The Alternatives After *Grafton Partners*
For Drafting and Enforcing Alternative Dispute Resolution Clauses**

I. *Grafton Partners L.P. v. Superior Court* (2005) 36 Cal.4th 944.

A. The Law Governing Jury Trial Waivers.

1. California Constitution, Article I, section 16, which reads in pertinent part:

Trial by jury is an inviolate right and shall be secured to all, but in a civil cause three-fourths of the jury may render a verdict. A jury may be waived in a criminal cause by the consent of both parties expressed in open court by the defendant and the defendant's counsel. In a civil cause a jury may be waived by the consent of the parties expressed as prescribed by statute....

2. Code of Civil Procedure section 631, which reads in pertinent part:

- a) The right to a trial by jury as declared by Section 16 of Article I of the California Constitution shall be preserved to the parties inviolate. In civil cases, a jury may only be waived pursuant to subdivision (d).

.....

- (d) A party waives trial by jury in any of the following ways:
 - (1) By failing to appear at the trial.
 - (2) By written consent filed with the clerk or judge.
 - (3) By oral consent, in open court, entered in the minutes.
 - (4) By failing to announce that a jury is required, at the time the cause is first set for trial, if it is set upon notice or stipulation, or within five days after notice of setting if it is set without notice or stipulation.
 - (5) By failing to deposit with the clerk, or judge, advance jury fees as provided in subdivision (b).
 - (6) By failing to deposit with the clerk or judge, at the beginning of the second and each succeeding day's session, the sum provided in subdivision (c).

3. *Exline v. Smith* (1855) 5 Cal. 112.
4. *Trizec Properties, Inc. v. Superior Court* (1991) 229 Cal.App.3d 1616.

B. The Holding of *Grafton* and its Logic.

C. What's Left after *Grafton*? Drafting Alternatives:

1. Modified Jury Trial Waivers? Is there a legislative response on the horizon?
2. Binding Arbitration.
3. Judicial Reference.
4. Combination Clauses.

D. Does *Grafton* Apply in Federal Court?

1. *Simler v. Conner* (1963) 372 U.S. 221.
2. *Leasing Service Corp. v. Crane* (4th Cir. 1986) 804 F.2d 828.
3. *Medical Air Tech. Corp. v. Marwan Invest. Inc.* (1st Cir. 2002) 303 F.3d 11, 18.
4. *Okura & Co. (America) Inc. v. Careau Group* (C.D.Cal. 1991) 783 F.Supp.482, 488.
5. See Justice Chin's concurrence in *Grafton*: "As a practical matter, in a diversity action, a federal court will routinely enforce a knowing and voluntary predispute jury waiver as a matter of federal law." (36 Cal.4th 944, 969, citing *Okura, supra.*)
6. *Standard Wire & Cable Co. v. Ameritrust Corp.* (C.D.Cal. 1988) 697 F.Supp. 368.
7. *Paracor Finance Inc. v. General Electric Capital Corp.* (9th Cir. 1996) 96 F.3d 1151, 1166.
8. *K.M.C. v. Irving Trust Co.* (6th Cir. 1985) 757 F.2d 752.

II. Overview of the Law Governing Alternative Dispute Resolution (“ADR”) Provisions

A. Arbitration

1. The California Arbitration Act (Code of Civil Procedure sections 1280 - 1294.2); Rule 371, Cal. Rules of Court. *Cf.* Judicial Arbitration, Code of Civil Procedure sections 1141.10 - 1141.31, and Rules 1600 - 1618, Cal. Rules of Court.
2. The U.S. Arbitration Act, also known as the Federal Arbitration Act (9 U.S.C. section 1 - 16).
3. Statutes dealing with arbitration in specific types of contracts.
 - a. Home Construction Contracts (Business & Professions Code section 7191). See *Woolfs v. Superior Court* (2005) 127 Cal.App.4th 197.
 - b. Health Care Contracts dealing with Arbitration of Medical Malpractice Claims (Code of Civil Procedure sections 1295).
 - c. Health Care Service Plans (Health & Safety Code section 1363.1). See *Malek v. Blue Cross of Cal.* (2004) 121 Cal.App.4th 44.
 - d. Real Estate Sale or Lease Contracts (Code of Civil Procedure section 1298).
 - e. Attorney Engagement Letters (Business & Professions Code section 6201).
 - f. Common Interest Development By-laws, CC&R's or Agreements (Civil Code sections 1363.810 - 1363.850).
 - g. Public Construction Contracts (Code of Civil Procedure section 1296).
 - h. See also statutes summarized in W. Knight, *Cal. Practice Guide: Alternative Dispute Resolution* (2004) Appendix A.

4. Recent and / or Important Cases dealing with Arbitration Clauses.
 - a. *Discover Bank v. Superior Court* (2005) 36 Cal.4th 148.
 - b. *Boghos v. Certain Underwriters at Lloyd's of London* (2005) 36 Cal.4th 495.
 - c. *Aguilar v. Lerner* (2004) 32 Cal.4th 974.
 - d. *Cruz v. PacifCare Health Systems, Inc.* (2003) 30 Cal.4th 303.
 - e. *Little v. Auto Stiegler, Inc.* (2003) 29 Cal.4th 1064.
 - f. *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83.
 - g. *Engalla v. Permanente Medical Group, Inc.* (1997) 15 Cal.4th 951.
 - h. *Moncharsh v. Heily & Blase* (1992) 3 Cal.4th 1.
 - i. *Graham v. Scissor-Tail, Inc.* (1981) 28 Cal.3d 807.
 - j. *Ting v. AT&T* (9th Cir.2003) 319 F.3d 1126.
 - k. *Independent Assn. Of Mailbox Center Owners, Inc. V. Superior Court* (2005) 133 Cal.App.4th 396.
 - l. *Jones v. Humanscale Corp.* (2005) 130 Cal.App.4th 401.
 - m. *Garrison v. Superior Court* (2005) 132 Cal.App.4th 253.
 - n. *Greenbriar Homes Community v. Superior Court* (2004) 117 Cal.App.4th 337.
 - o. *Garcia v. DIRECTTV, Inc.* (2004) 115 Cal.App.4th 297.
 - p. *Abramson v. Juniper Networks, Inc.* (2004) 115 Cal.App.4th 638.

- q. *Fitz v. NCR Corp.* (2004)
118 Cal.App.4th 702.
- r. *Liska v. The Arns Law Firm* (2004) 117 Cal.App.4th 275
- s. *Hedges v. Carrigan* (2004) 117 Cal.App.4th 578
- t. *Martinez v. Master Protection Corp.* (2004)
118 Cal.App.4th 107.
- u. *Lopez v. Charles Schwab & Co., Inc.* (2004)
118 Cal.App.4th 1224.
- v. *Fitz v. NCR Corp.* (2004)
118 Cal.App.4th 702.
- w. *Omar v. Ralphs Grocery Co.* (2004)
118 Cal.App.4th 955.
- x. *Kalai v. Gray* (2003) 109 Cal.App.4th 768.
- y. *Jaramillo v. JH Real Estate Partners, Inc.* (2003) 111
Cal.App.4th 394.
- z. *Szetela v. Discover Bank* (2002) 97 Cal.App.4th 1094.
- aa. *Stirlen v. Supercuts, Inc.* (1997) 51 Cal.App.4th 1519.

B. Judicial Reference

- 1. Code of Civil Procedure section 638.
- 2. Important Cases dealing with Judicial Reference Clauses.
 - a. *Pardee Construction Co. v. Superior Court* (2002) 100
Cal.App.4th 1081.
 - b. *Woodside Homes of Cal., Inc. v. Superior Court* (2003)
107 Cal.App.4th 723.

- c. *Greenbriar Homes Community v. Superior Court* (2004) 117 Cal.App.4th 337.
- d. *Trend Homes, Inc. v. Superior Court* (2005) 131 Cal.App.4th 950.

C. Mediation

Civil Action Mediation Act (Code of Civil Procedure sections 1775 - 1775.15).

III. Questions to Ask When Evaluating Whether an ADR Provision Is Enforceable.

- A. Is there even an enforceable ADR agreement? See Code of Civil Procedure section 1281.2; *Lopez v. Charles Schwab & Co., Inc.* (2004) 118 Cal.App.4th 1224.
- B. Are there any specialized statutes which apply to this particular contract? See section II.A.3., above. If so, is the statute preempted by the Federal Arbitration Act? See *Cronus Investments, Inc. V. Concierge Services* (2005) 35 Cal.4th 376, 383; *Hedges v. Carrigan* (2004) 117 Cal.App.4th 578, 584; *Ovitz v. Schulman* (October 26, 2005) ___ Cal.App.4th ___ [35 Cal.Rptr.3d 117].
- C. Are the claims which are likely to arise under the contract actually arbitrable?
 - 1. Certain Injunctive relief claims are not arbitrable. *Cruz v. PacifCare Health Systems, Inc.* (2003) 30 Cal.4th 303.
 - 2. A purchaser or lessor of real property cannot be compelled to arbitrate a construction defect claim. Code of Civil Procedure section 1298.7; *Basura v. U.S. Home Corp.* (2002) 98 Cal.App.4th 1205; *Villa Milano Homeowners Assn.v. Il Davorge* (2000) 84 Cal.App.4th 819.
 - 3. Certain judicial remedies do not lend themselves to arbitration, such as actions for judicial foreclosure. See Code of Civil Procedure section 726.

- D. Is the ADR provision unconscionable?
1. Statutory authority: Civil Code section 1670.5. See also Civil Code section 1671 (enforceability of penalty and liquidated damages provisions).
 2. Important cases.
 - a. *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83.
 - b. *Little v. Auto Stiegler, Inc.* (2003) 29 Cal.4th 1064.
 - c. *Graham v. Scissor-Tail, Inc.* (1981) 28 Cal.3d 807.
 - d. *Abramson v. Juniper Networks, Inc.* (2004) 115 Cal.App.4th 638.
 - e. *Greenbriar Homes Community v. Superior Court* (2004) 117 Cal.App.4th 337.
 - f. *Jaramillo v. JH Real Estate Partners, Inc.* (2003) 111 Cal.App.4th 394.
 - g. *Fitz v. NCR Corp.* (2004) 118 Cal.App.4th 702.
 - h. *Stirlen v. Supercuts, Inc.* (1997) 51 Cal.App.4th 1519.
 3. Is the ADR provision substantively unconscionable?
 - a. Does the ADR provision seek to deprive a party of an important statutory or common law right? For instance, does the provision prohibit class treatment of arbitrable claims, does it restrict the remedies of the prevailing party, does it impair any specific statutory remedies? See *Armendariz, supra*; *Discover Bank, supra*; *Szetela, supra*.
 - b. Does the ADR clause have aspects which are one-sided (non-mutual) and which unfairly benefit one party at the expense of the other? See *Armendariz, supra*; *Jones, supra*.

- c. Does the ADR clause contain a provision which prohibits or severely limits discovery? See *Armendariz, supra*.
- d. Does the ADR clause have a venue clause which violates California's venue scheme, Code of Civil Procedure sections 392 - 97? See *Pinedo v. Premium Tobacco Stores, Inc.* (2000) 85 Cal.App.4th 774; *Alexander v. Superior Court* (2003) 114 Cal.App.4th 723 (non-ADR case).
- e. Does the ADR clause have a forum selection or choice-of-law clause which violates California public policy? *Discover Bank, supra*; *America Online, Inc. v. Superior Court* (2001) 90 Cal.App.4th 1 (non-ADR case); *Nedlloyd Lines B.V. v. Superior Court* (1992) 3 Cal.4th 459 (non-ADR case).
- f. Does the ADR clause provide for the selection of a neutral or neutrals whose qualifications might raise a question about true neutrality in the context of the agreement in question? See *Graham v. Scissor-Tail, Inc.* (1981) 28 Cal.3d 807.
- g. Does the ADR clause severely limit any applicable limitations period? See *Martinez, supra*; *Boelts v. City of Lake Forest* (2005) 127 Cal.App.4th 116, 121 n. 4.
- h. Does the ADR clause require the payment of an unreasonable fee as a precondition to the right to arbitrate? See *Armendariz, supra*; *Boghos, supra*.

IV. Other Considerations In Drafting The (Hopefully) Enforceable ADR Clause.

A. The Use of Factual Recitals.

1. See Evidence Code section 622.
2. *Plaza Freeway Limited Partnership v. First Mountain Bank* (2000) 81 Cal.App.4th 616.
3. *Miner v. Tustin Avenue Investors* (2004) 116 Cal.App.4th 264.

B. The Form and Placement of ADR Provisions.

1. See Commercial Code section 2316 regarding “conspicuousness”: print type, headings, placement.
2. Language choice: Is it clear and unambiguous?
3. Use of initials and specially prepared language (as opposed to a form agreement or “bill stuffer”). See Justice Johnson’s dissent in *Hicks v. Superior Court* (2004) 115 Cal.App.4th 77; *rev. granted and opinion superseded by* 13 Cal.Rptr.3d 300.
4. Avoid circumstances which create a contract of adhesion, considered by the courts to be “an element of procedural unconscionability.” See *Discover Bank v. Superior Court, supra* (amendment to cardholder agreement in the form of a bill stuffer); *Szetela, supra*.