# ARIZONA ADR FORUM

FALL 2020

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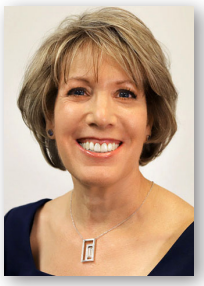
## FROM THE CHAIR

ALONA M. GOTTFRIED

The Board of the ADR Section of the Bar is hard at work to provide you with quality programming. The CLE Committee, with **Lee Blackman** as the chair, has already presented two virtual CLEs. On September 9, 2020, the Honorable Pamela Gates spoke about Maricopa County Superior Court's Certified Arbitrator and Fair Limits programs. On October 21, 2020, speakers Renee Gerstman and Rick Mahrle presented a CLE entitled *2020 ADR Case Law Update*. All of our speakers have been wonderful, and both CLEs were well-attended and well-received. We offered these CLEs at no cost to our members. Attending the ADR Section's CLEs is a nice way to maintain a feeling of community during these isolating times.

LEE BLACKMAN

HON. PAMELA GATES



RENEE GERSTMAN

RICK MAHRLE

The ADR Section's 2020 Convention Committee, chaired by Rick Mahrle, has planned two great programs for the convention:

- *Advanced Legal Negotiating Skills*
- *ADR Talks*

These programs will be presented (virtually) on December 2, 2020.

We would love to hear from you. Please feel free to contact me if you want to get more involved, have ideas for programs, or have news that may be of interest to our community.

*— Alona M. Gottfried*
*ADR Section Chair*
*480-998-1500*

STATE BAR OF ARIZONA


**EDITOR | JEREMY M. GOODMAN**

We welcome comments about this newsletter and invite you to suggest topics or submit an article for consideration. Email the Editor, Jeremy M. Goodman at jeremy@goodmanlawpllc.com.

# Attorney–Client Fee Arrangements and Unconscionability of Arbitration Provisions


BY RENEE B. GERSTMAN

On January 30, 2020, the Arizona Court of Appeals, Division One, addressed procedural and substantive unconscionability of an arbitration provision in *Rizzio v. Surpass Senior Living LLC*, 248 Ariz. 266, 459 P.3d 1201 (Ariz. Ct. App. Div. 1 2020). The opinion addresses the applicability of federal or state arbitration acts, procedural and substantive unconscionability, severing of unconscionable provisions, voids left by severing of unconscionable provisions, and whether an agreement to arbitrate a claim is substantively unconscionable where counsel for the party seeking to avoid arbitration has agreed to advance all arbitration costs. The Arizona Supreme Court has granted review and will consider the question of whether a plaintiff's retainer agreement under which her attorney will advance all costs of arbitration can be considered as part of plaintiff's individualized showing of her ability to financially bear the costs of arbitration.

## Federal Arbitration Act

The *Rizzio* opinion provides a primer on the applicability of the Federal Arbitration Act (FAA) and state arbitration acts such as the Uniform Arbitration Act (UAA) or the Revised Uniform Arbitration Act (RUAA)[1]. Although the nursing home was physically located in Arizona and the plaintiff was a resident of Arizona, the Court found that the FAA applied because the contract was between a nursing care facility owned and operated by a Texas LLC and an Arizona resident and therefore constituted interstate commerce for purposes of the FAA. Although the FAA applies, whether the contract is valid and enforceable is governed by state law.

## Background Information and Trial Court Ruling

Ms. Rizzio sued her nursing care facility in the trial court for injuries suffered when she attacked by another resident. The nursing care facility moved to compel arbitration.

The arbitration provision at issue was part of a nursing care facility contract signed by Ms. Rizzio's daughter on her behalf as her power of attorney. The arbitration provision encouraged the signer to obtain legal advice before signing the arbitration agreement and admission to the facility was not contingent on execution of the arbitration provision. The facility contract contained a cost-shifting provision that made Rizzio responsible for all costs of arbitration and all legal costs and attorney's fees (both hers and the nursing care facility's) ***regardless of which party prevailed in the arbitration***.

The trial court held an evidentiary hearing on the nursing care facility's motion to compel arbitration and made the following factual findings: the contract was drafted by the nursing care facility and not the party opposing arbitration, Rizzio had little opportunity to review the contract, the arbitration terms were not verbally explained to Rizzio, Rizzio had no opportunity to bargain with the nursing care facility, and Rizzio would be unable to effectively vindicate her claim as the contract unfairly allocated all the costs of arbitration to Rizzio regardless of whether she prevailed at arbitration. Based on these factual findings the trial court concluded that the arbitration provision was procedurally and substantively unconscionable and violated Rizzio's reasonable expectations. The Court of Appeals reviewed the denial of the motion de novo and affirmed in part, reversed in part, and remanded to the trial court.

The *Rizzio* opinion is a good review of Arizona law on unconscionability of arbitration provisions and confirms that in Arizona either procedural or substantive unconscionability, not both, may be a defense to enforcement of an arbitration provision.

## Procedural Unconscionability

The Court of Appeals set forth the factors typically considered in determining whether a contract is procedurally unconscionable. They are: age, education, intelligence, business acumen and experience, relative bargaining power, who drafted the contract, whether the terms were explained to the weaker party, whether alteration in the printed terms was possible, and whether there were alternative sources of supply for the goods in question. Other factors that may be considered are: whether the arbitration provision was separate from other paperwork, the typeface used, and whether it was signed hurriedly and without explanation in emergency circumstances.

The Court of Appeals upon review of the trial court record concluded that the record did not support a finding of procedural unconscionability. The Court's ruling relies on the fact that Rizzio's daughter had herself limited the time to review the agreement, the contract in bold language recommended that she consult with an attorney, admission of her mother to the facility was not contingent upon her signing the agreement, and there was no evidence of emergency circumstances at the time of execution. The Court of Appeals, in reaching its result, noted that the factual findings of the trial court supported a conclusion that the contract was an adhesion contract but, under Arizona law adhesion contracts are not *per se* procedurally unconscionable. Rather, contracts of adhesion are only unenforceable where they are not within the reasonable expectations of the weaker party and the contract is unconscionable.

## Substantive Unconscionability

In analyzing whether the agreement was substantively unconscionable, the Court of Appeals looked at the relative fairness of the obligations undertaken by the parties in the contract. Are the terms of the contract so one-sided as to oppress or unfairly surprise an innocent party, is there an overall imbalance in the obligation and rights imposed by the bargain, or a significant cost-price disparity. Arbitration agreements that contain excessive fees and costs that deny a potential litigant the opportunity to vindicate his or her rights may be substantively unconscionable. The Court of Appeals agreed with the trial court that the shifting of all costs and fees to Rizzio, even if she prevails, was unusual, one-sided, and operated as a prospective penalty for any resident seeking to bring a meritorious claim and was therefore substantively unconscionable and not enforceable.

Despite finding the arbitration provision substantively unconscionable, the Court of Appeals reversed the trial court's conclusion that the arbitration provision was substantively unconscionable finding that the cost-shifting provision could be severed from the remainder of the agreement under the agreement's severability clause and, once severed, the arbitration provision was conscionable.

Rizzio argued to the Court of Appeals that: (1) severance of the cost-shifting provision would leave the agreement silent on allocation of costs and fees and therefore unconscionable; and (2) that even with the cost-shifting provision severed, she could not afford to pay arbitration costs so that she would be denied the opportunity to vindicate her claim. The Court of Appeals rejected Rizzio's argument because the arbitrator under the FAA[2] has discretion to award arbitration fees and costs such that silence on allocation of costs alone does not invalidate an arbitration agreement.

The Court of Appeals went on to analyze whether the arbitration provision without the unconscionable cost-shifting provision was substantively unconscionable. Here, the Court of Appeals distinguished *Clark v. Renaissance West, LLC*, 232 Ariz. 510, 307 P.3d 77 (Ariz. Ct. App. Div. 1 2013) and *Harrington v. Pulte Home Corp.*, 211 Ariz. 241, 119 P.3d 1044 (Ariz. Ct. App. Div. 1 2005) from Rizzo's situation because under Rizzio's fee agreement with her attorney, her attorney and not Rizzio, assumed responsibility for advancing all costs and repayment by Rizzio of those costs was only to occur out of the proceeds of any recovery. Because Rizzio would only pay arbitration costs if she prevailed and received a monetary award and the arbitrator declines to allocate all costs to the nursing care facility, the Court found that because Rizzio was not responsible for upfront costs of arbitration, such costs would not be an impediment to arbitration and the provision without the now severed cost-shifting provisions was not substantively unconscionable.

The Court of Appeals does not discuss, and it is not clear, how the Court's reliance on the post-hoc agreement between Rizzio and her attorney is relevant to the inquiry of unconscionability under Arizona law given that Arizona law provides that unconscionability is determined at the time the parties entered into the contract. See *Nelson v. Rice*, 198 Ariz. 563, 12 P.3d 238 (Ariz. Ct. App. 2000). Is the Court of Appeals suggesting that the post-hoc agreement between a plaintiff and its attorney can cure an otherwise substantively unconscionable contract? Would the Court's decision be different if the fee agreement required Rizzio to bear some or all of the upfront costs of arbitration or if Rizzio would be required to reimburse the attorney for arbitration costs regardless of the outcome? What if Rizzio wanted to change counsel in the middle of the arbitration and the new attorney does not agree to cover the same costs as prior counsel? Would the Court of Appeals based on this decision adopt the position of other courts[3] that have allowed substantively unconscionable provisions to be cured by post-hoc offers of the defendant to cover arbitration expenses? Based on this opinion does an attorney commit malpractice if their client must pursue their claim in arbitration rather than in court based on the wording of their fee agreement?

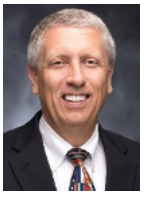
The Arizona Supreme Court accepted review of the Rizzio case on the issue of whether a plaintiff's retainer agreement under which her attorney will advance all costs of arbitration can be considered as part of the plaintiff's individualized showing of her ability to financially bear the costs of arbitration. Oral argument was scheduled for November 17, 2020. Stay tuned for further updates.

### ENDNOTES

1. Codified in Arizona at A.R.S. § 12-3001 *et seq.*
2. The RUAA has a similar provision, found at A.R.S. § 12-3021(D)
3. See, *Plummer v. McSweeney*, 941 F.3d 341 (8th Cir. 2019)

# The Unintended Consequences of Statutes of Limitations in Arbitration

**BY DAVE TIERNEY & GREG GILLIS**



**DAVE TIERNEY** and **GREG GILLIS** are members of the American Arbitration Association's Construction and Commercial Panel of Neutrals. Both practice construction law, commercial litigation and alternative dispute resolution with the Scottsdale firm of Sacks Tierney P.A

Nearly 60 years ago in a trial court in Connecticut, the purchaser of a ten-year old air conditioner sued the supplier of the system. On appeal, the Connecticut Court of Appeals boldly stated, "Arbitration is not a common-law action and the institution of arbitration proceedings is not the bringing of an action under any of our statutes of limitations." *Skidmore, Owings & Merrill v. Connecticut General Life Ins. Co.*, 197 A.2nd 83, 85 (Conn. 1963). Declaring that statutes of limitations did not control arbitration proceedings, the Court noted, however, that the facts were such that any applicable statute of limitations would not have expired, so its ruling on the inapplicability of statute of limitations in arbitration was *dicta*.

One decade ago, in the State of Washington, a broker's customer sued the broker and his firm. In *Broom v. Morgan Stanley D.W. Inc.*, 236 P.3d. 182 (Wash. 2010) the plaintiff was contesting the arbitrator's outright dismissal of several claims on statute of limitations' grounds. First, the Supreme Court of Washington agreed to address "facial legal error" and review the arbitrator's ruling. Second, it declared that an arbitration is not an "action" and that, accordingly, statute of limitations were not controlling. State statute of limitations simply did not apply in arbitrations, unless some contract clause or some state statute expressly made them applicable. Washington noted that when its legislature adopted the RUAA it carefully denominated the arbitration proceedings "something distinct from civil actions or judicial proceedings." The Court stated that the parties, if they wish, may agree contractually to the applicability of statutes of limitations, in which case they will control.

As if whether a statute of limitations applies in arbitration is not enough of a concern, another potential problem exists regarding which state's statute of limitations applies. This may not be a problem in Arizona construction cases because A.R.S. § 32-1129.05 requires Arizona law and venue apply to Arizona construction projects. However, in non-construction cases this issue could be fatal. Many courts, including Arizona, have found that statute of limitations are procedural rather than substantive law. As a result, the choice of law provision in the parties' contract may not control the statute of limitations.

For example, the statute of limitations to enforce a breach of a written contract is six years in Arizona, four years in Texas. There is little to no guidance for an arbitrator in making this choice of law analysis. Presumably the arbitrator, like a federal judge, would apply diversity jurisdiction and look to the law of the forum state.

Selecting the forum state does not end the inquiry. Parties frequently chose, for convenience and other reasons, to hold the arbitration hearing in a different forum. Therefore, using the example, if a party initiates a demand for arbitration in Texas four years and a day after the breach and the written contract requires Texas law to apply, the claim is subject to dismissal. However, if for convenience, the parties elected to conduct the arbitration in Arizona, the breach of a written contract claim remains a viable claim in arbitration for two more years. The converse would also be true. Counsel and parties should carefully consider whether transferring the hearing locale as a mere convenience to the parties and counsel has any unintended statute of limitations consequences.

The careful drafter of an arbitration clause will avoid these potential landmines by including a statement in their arbitration clause that statutes of limitations apply to these proceedings. For example:

> A demand for arbitration shall be made no earlier than concurrently with the filing of a request for mediation, but in no event shall it be made after the date when the institution of legal or equitable proceedings based on the Claim would be barred by the statute of limitations, which statues are hereby made applicable to the arbitrable Claims. For statute of limitations purposes, receipt of a written demand for arbitration by the person or entity administering the arbitration shall constitute the institution of legal or equitable proceedings based on the Claim.