

Negligence Law Section

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Predispute Arbitration Clauses: A Conflict of Rights

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Can an attorney include an arbitration clause in a client engagement agreement? Does an arbitration agreement in an employment contract allow an employer to compel arbitration of claims of sexual assault by an employee? As these important questions have been presented to the Michigan Supreme Court recently, we take a deeper dive into the current status of predispute arbitration agreements under Michigan law as well as the arguments for and against such agreements.

Arbitration agreements: a contract

Michigan favors Alternative Dispute Resolution (ADR). One form of ADR is arbitration. The process is binding and can result in entry of an enforceable judgment. Arbitration is ADR in the extremity. The parties waive their rights to trial. These agreements typically affect evidence and control venue. A decision to arbitrate is significant. It may be the correct decision in a given case, but there is no question that the decision can materially affect not only the cost of litigation but the result as well.

Arbitration can be agreed to before or after a dispute arises. Predispute arbitration clauses are ubiquitous and are imposed upon a party who signed a contract before there is a reason to litigate. These clauses are increasingly found in contracts with insurance companies, cell phone providers and car companies. In fact, eighty-one (81) of the one hundred (100) largest companies in the U.S. require their customers to arbitrate any claims of wrongdoing.¹ These types of agreements are not typically negotiated. Instead, they are usually a “form” document that happens to have been drafted by counsel for the party creating the form. Many consumers may not understand or even recognize the significance of a contract that preemptively waves jury trial, submits to venue and perhaps even limits the amount of damages that can be recovered.

Postdispute arbitration agreements, on the other hand, are entered into after a dispute has arisen, and sometimes even in the course of litigation. Usually, both parties have an opportunity to obtain the advice of counsel, engage in meaningful negotiations, and execute an informed waiver of substantive rights. The parties have the ability to negotiate decisions on legal issues, whether

there will be limitations on damages, and whether to use three neutral arbitrators (one appointed by each party with a single neutral) or a single arbitrator.

In 2013, the Michigan Uniform Arbitration Act (UAA) became effective.ⁱⁱ Pursuant to the UAA, an agreement to arbitrate any “existing or subsequent controversy” is valid, enforceable, and irrevocable, except on a ground that exists at law or in equity for the revocation of a contract.ⁱⁱⁱ

In 2016, in *Altobelli v Hartmann*, the Michigan Supreme Court reiterated that arbitration is a matter of contract.^{iv} Accordingly, when interpreting an arbitration agreement, the same legal principles that govern contract interpretation apply.^v A court must ascertain the intent of the parties at the time they entered into the agreement, by examining the language of the agreement according to its plain and ordinary meaning.^{vi} Importantly, a party cannot be required to arbitrate an issue which it has not agreed to submit to arbitration.^{vii}

Under Michigan law, the elements of a valid contract are: (1) parties competent to enter into a contract; (2) a proper subject matter; (3) legal consideration; (4) mutuality of agreement; and (5) mutuality of obligation.^{viii}

As with any contract, an agreement to arbitrate is subject to challenge. Defenses to an arbitration agreement are the same as the defenses available to contract formation, *i.e.* public policy, capacity, fraud, duress, unconscionability, lack of consideration, and waiver, among others.

Constitutional right to trial by jury

The Seventh Amendment of the U.S. Constitution states: “In Suits at common law . . . the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law.”^{ix} The Michigan Constitution states that the right to civil trial by jury shall remain.^x Thus, when parties agree to arbitrate, they are waiving their constitutional right to a trial by jury.

Attorney-client engagement agreements

In *Tinsley v Yatooma*, the Michigan Court of Appeals held that an attorney may include a predispute arbitration clause in a client engagement agreement.^{xi} The court determined that an arbitration provision in an attorney’s engagement agreement does not violate MRPC 1.8(h)(1) (which prohibits a lawyer from making an agreement prospectively limiting the lawyer’s liability to a client for malpractice), provided that the client consult with independent counsel.^{xii} As an aside, the Court noted that MRPC 1.8(h)(1) may not even apply to attorney-client arbitration provisions that do not limit an attorney’s liability for malpractice.^{xiii}

Application for leave to appeal in *Tinsley* has been filed in the Michigan Supreme Court. The Negligence Section of the State Bar of Michigan submitted an amicus brief on March 9, 2021. The Negligence Section argued that the mandatory arbitration provision at issue did prospectively limit the lawyer’s liability to his client for malpractice because the provision: (1) eliminated appellate reviewability of substantive and procedural errors of a single arbitrator; (2) eliminated traditional discovery rights (discovery was limited to 60 days and the client was limited to one deposition, but the attorney’s ability to take depositions was unlimited); and (3) placed responsibility for all of the costs and expenses of the arbitration on the client exclusively. The Negligence Section also pointed out that there is a conflict in the case law that should be

addressed by the Michigan Supreme Court- namely whether a fee agreement which violates the Michigan Rules of Professional Conduct is enforceable. On March 24, 2021, the Supreme Court denied the application for leave to appeal.

Employment contracts

In 1999, in *Rembert v Ryan's Family Steakhouse*,^{xiv} the Michigan Court of Appeals determined that as long as no rights or remedies accorded by statute are waived, and as long as the procedure is fair, employers may enter into predispute agreements with their employees to arbitrate statutory civil rights claims.^{xv} The *Rembert* Court struck a balance between the right to contract and the protection of substantive rights created by statute, stating:

While our decision upholds the principle of freedom of contract and advances the public policy that strongly favors arbitration, it does so subject to two conditions generally accepted in the common law: that the agreement waives no substantive rights, and that the agreement affords fair procedures. These conditions are rooted in two critically important bases: (1) our Supreme Court's decision in [*Renny v. Port Huron Hosp.*, 427 Mich. 415, 398 N.W.2d 327 \(1986\)](#), which held that agreements to arbitrate employment claims must have fair procedures, and (2) Michigan and federal decisions (which generally have been held to be persuasive authority in Michigan employment discrimination cases) that uniformly hold that these arbitration agreements may not waive any substantive rights or remedies provided by the statute and must provide for fair procedures...^{xvi}

As a result, predispute arbitration clauses cannot waive substantive rights provided by statute and the process must be fair.^{xvii}

In *Lichon v Morse*, the court of appeals held that a predispute arbitration agreement in the employment contract there did not allow an employer to compel arbitration of claims of sexual assault by an employee.^{xviii} The court reasoned that such claims were not subject to arbitration because the arbitration agreement applied to claims “relative to” employment, and sexual assault and battery of an employee at the hands of a superior is not conduct “related to” employment for purposes of the arbitration agreement.^{xix} Specifically, the court held that “under no circumstances could sexual assault be a foreseeable consequence of employment in a law firm.”^{xx} The court also ruled that enforcing an arbitration agreement in a case of sexual assault would “effectively perpetuate a culture that silences victims of sexual assault and allows abusers to quietly settle these claims behind an arbitrator’s closed door,” which would be against public policy.^{xxi}

The Michigan Supreme Court granted leave in *Lichon* to address whether the claims set forth in the plaintiffs’ complaints are subject to arbitration. Oral argument was held on October 8, 2020.^{xxii}

Exception: Minors and legally incapacitated individuals

It has been the common law in the state of Michigan for more than a century that a parent cannot bind a minor child to a contract.^{xxiii} As an arbitration agreement is a contract, a parent cannot bind a minor child to an arbitration agreement.^{xxiv} In 2010, the Michigan Supreme Court in *Woodman v. Kera LLC*,^{xxv} expressly recognized that “the freedom to contract does not permit

contracting parties to impose obligations upon and waive the rights of third parties in the absence of legally cognizable authority to do so.”^{xxvi}

Pursuant to MCL 700.5407, a conservator has the power to enter into a contract on behalf of a legally incapacitated individual.^{xxvii} However, there are limitations on a conservator’s authority, including the fact that a conservator must bring a proposed settlement before the court for approval.^{xxviii} In addition, although a conservator has authority to settle a claim by or against the protected individual by arbitration, a conservator cannot release a claim belonging to the estate unless the claim is uncollectable.^{xxix}

Unlike a conservator, a guardian does not have the statutory authority to enter into a contract, unless there is a protective arrangement authorized by a court for specifically enumerated reasons, none of which include waiver of a constitutional right.^{xxx} Moreover, the Supreme Court analogized the role of a parent to that of a legal guardian when it determined that a parent cannot waive the rights of a child.^{xxxi} Therefore, there is no authority that would allow a guardian to waive constitutional rights on behalf of a legally incapacitated individual.

Whether a power of attorney has authority to enter into a contract and agree to arbitration on behalf of an agent will likely depend largely on the language of the power of attorney. In *Kindred Nursing Centers Ltd. Partnership v Clark*, the United States Supreme Court reviewed two cases from the Supreme Court of Kentucky, where agents holding powers of attorney signed arbitration agreements when their principals were admitted into a nursing facility.^{xxxii} The United States Supreme Court determined that one of the powers of attorney gave the agent authority to sign an arbitration agreement, but remanded the other case back to the Kentucky Supreme Court for decision.^{xxxiii} On remand, the Kentucky Supreme Court determined that the power of attorney was not broad enough to give the agent authority to sign an arbitration agreement.^{xxxiv} Similarly, the Supreme Court of South Carolina recently reviewed a power of attorney and determined that the language of the power of attorney was not broad enough to allow an agent to waive a principal’s constitutional rights.^{xxxv}

Exception: Long-term care facilities

Although arbitration agreements are generally enforceable, there are some limitations on the ability of long-term care facilities to use these agreements. In 2016, CMS issued a final rule prohibiting nursing homes from including predispute arbitration clauses in their admission agreements.^{xxxvi}

Just three years later, however, in 2019, CMS issued a new final rule, which allows nursing homes to include predispute arbitration clauses in their admission agreements, but prohibits nursing homes from requiring that they be signed as a condition of admission and gives residents a 30 day window to rescind the agreement.^{xxxvii}

Michigan Consumer Protection Act

The Michigan Consumer Protection Act (MCPA) is generally intended to protect Michigan consumers from fraud and unfair dealing in consumer contracts.^{xxxviii} There is no prohibition against arbitration in the MCPA.

Forced Arbitration Injustice Repeal (FAIR) Act

In 2019, the U.S. House of Representatives passed the Forced Arbitration Injustice Repeal (FAIR) Act,^{xxxix} but it was not taken up by the Senate. This Act would prohibit predispute arbitration agreements from being valid or enforceable if they require arbitration of an employment, consumer, antitrust, or civil rights dispute. The FAIR Act was recently revived in Washington in February 2021.

Point-counterpoint

Predispute arbitration clauses should not be enforceable

By Donna MacKenzie

Predispute arbitration clauses are typically buried in the fine print of a contract or agreement. These hidden clauses not only deny individuals their constitutional right to have a dispute heard by an impartial judge or jury, but also include additional restrictions of rights, such as provisions that require the dispute be kept secret, limit the amount of the consumer's recovery, limit the number of arbitrators and/or who can serve as an arbitrator, limit discovery, limit the appealability of the arbitrator's decisions, and/or limit the ability to bring class action litigation. These restrictions typically favor the companies who draft the clauses over the individuals who are forced to sign them. Moreover, arbitration can be far more costly than judicial process but this fact is rarely, if ever, clearly referenced within these clauses.

There are numerous reasons why predispute arbitration agreements should not be enforced. First, it must be determined whether the person signing the agreement had the capacity and/or authority to sign the agreement. In addition, when arbitration agreements are hidden in the fine print and there is no indication that the provision was ever discussed or that the signor had knowledge that an arbitration clause was in the agreement, it cannot be said that the party intended to, or knowingly, waived their constitutional rights.^{xi} Likewise, where there is no mutual assent on all essential terms, the contract should be unenforceable.^{xii}

Moreover, individuals are typically forced into signing these clauses on a "take it or leave it" basis, without any ability to object to or negotiate the terms of the agreement, rendering such agreements procedurally unconscionable.^{xiii} In situations where the arbitration clause not only contains a waiver of the right to trial by jury, but also includes additional, unreasonable limitations, such as those identified above, the agreement may be rendered substantively unconscionable.^{xiii} Where an agreement is both procedurally and substantively unconscionable, it is not enforceable.^{xiv}

Arbitration clauses may also lack consideration or be illusory where there is no mutuality of promise.^{xiv} For example, if the agreement is one-sided, where the individual gives up the right to a jury trial, but the company preserves its constitutional right to have disputes heard by a judge or jury, there is arguably no mutual promise and the clause should fail.

Notably, the UAA does not validate predispute arbitration agreements, only agreements to arbitrate an existing or subsequent controversy. Moreover, to the extent that substantive rights created by statute are waived or that the process of arbitration is unfair, such an agreement can be challenged under *Rembert*. Finally, similar to *Lichon*, public policy may preclude certain matters from being subject to arbitration.

Postdispute arbitration agreements, on the other hand, typically do not present the myriad of problems posed by predispute arbitration agreements. For starters, a postdispute arbitration agreement is entered into when the parties know for sure that a dispute has arisen and it is more likely that the parties are intentionally and knowingly entering into the agreement. Moreover, at the point of a postdispute arbitration agreement, both parties are likely represented by counsel and the terms of the agreement are extensively negotiated. Indeed, postdispute arbitration agreements, when entered into voluntarily and at arms-length, can be a very useful resolution tool for disputes.

Parties should be free to enter into contractual agreements to arbitrate their disputes
By John Whitman

The root issue is whether or not an otherwise competent adult can enter into a contract. Do we need to be protected from ourselves? Is it the role of the court or the legislature, to impede the right of people to enter into contracts “for their own good”? I think not.

Obviously, this is not a universal statement. Minors and MIPs should be and are, in fact, protected from doing this. We regulate certain contracts, such as insurance policies, consumer installment contracts and others, already. While there may be a reason, in any given instance, to protect a vulnerable people, to broadly sweep away the ability to enter into a contract is dangerous.

To permit the Court or legislature this sweeping “gate keeper” role is a slippery slope. Does this mean that I cannot release statutory, substantive rights post loss? Or that I cannot agree to limit damages as part of a post loss negotiation?

A decision that a competent adult is not permitted to waive substantive rights, release a claim or agree to a process which may significantly impact their claim, undermines not only the process of negotiation at the heart of the civil justice system, it undermines the fundamental freedom of contract.

Our statutes already provide that such a “pre-dispute” or “pre-controversy” arbitration clause is enforceable “...except on a ground that exists at law or in equity for the revocation of a contract.”^{xlvi} We have a long and rich history of protecting both the right of contract and the right to challenge the validity of a contract. From my perspective, if it is “not broken, don’t fix it.”

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ⁱ Abrams, A (2019, February). 81 of the Largest U.S. Companies Won't Let You Take Them to Court. *Time*. <https://time.com/5538028/consumer-arbitration-agreements/>.

ⁱⁱ [MCL 691.1681 et seq.](#)

ⁱⁱⁱ Under the UAA, it is the responsibility of the court to decide whether an agreement to arbitrate exists or a controversy is subject to an agreement to arbitrate. [MCL 691.1686\(2\)](#). An arbitrator has authority to decide whether a condition precedent to arbitrability has been fulfilled and whether a contract containing a valid agreement to arbitrate is enforceable. [MCL 691.1686\(3\)](#).

^{iv} [Altobelli v Hartmann](#), 499 Mich 284; 884 NW2d 537 (2016).

^v *Id.*

^{vi} *Id.*

^{vii} *Id.*

^{viii} [Thomas v. Leja](#), 187 Mich App 418; 468 NW2d 58 (1991).

^{ix} [US Const. Amend. 7.](#); <https://www.archives.gov/founding-docs/bill-of-rights-transcript>

^x [M.I. Const. art. I, § 14.](#)

^{xi} [Tinsley v Yatooma](#), __ Mich App __; __ NW2d __, 2020 Mich. App. LEXIS 5297 (Ct. App. Aug. 13, 2020)

^{xii} *Id.*

^{xiii} *Id.*

^{xiv} [Rembert v. Ryan's Family Steak Houses, Inc.](#), 235 Mich App 118; 596 NW2d 208 (1999).

^{xv} The employment discrimination claims at issue arose under the Michigan Civil Rights Act (CRA), [MCL 37.2101 et seq.](#), and the Persons With Disabilities Civil Rights Act (PWDCRA), [MCL 37.1101 et seq.](#)

^{xvi} *Id.* at 124.

^{xvii} Another example arises in the context of Michigan No-Fault Statute, which creates a statutory right to recover interest, [MCL 500.3142](#), as well as fees [MCL 500.3148](#). Those substantive rights are routinely waived in some postdispute arbitration agreements, but pursuant to *Rembert*, such waivers could not be imposed on individuals by predispute arbitration provisions in the no-fault policy.

^{xviii} [Lichon v Morse](#), 327 Mich App 375; 933 NW2d 506 (2019).

^{xix} *Id.*

^{xx} *Id.*

^{xxi} *Id.*

^{xxii} <https://www.youtube.com/watch?v=qruAdPfu0Pg>.

^{xxiii} See [Woodman v. Kera LLC](#), 486 Mich 228; 785 NW2d 1 (2010) (holding that a parental preinjury waiver is not enforceable).

^{xxiv} [McKinstry v. Valley Obstetrics-Gynecology Clinic, P.C.](#), 428 Mich 167; 405 NW2d 88 (1987) (recognizing that under common law a parent does not have authority to bind a child to an arbitration agreement). In addition, under Michigan law, a parent is not permitted to settle a case on behalf of a minor, unless the parent has been appointed as next friend, guardian or conservator, and the settlement is approved by the court. MCR 2.420. Furthermore, a parent is only allowed to receive payment on behalf of a minor if the minor will receive payments of less than \$5,000 in a single year; otherwise, a conservator must be appointed. [MCL 700.5102](#).

^{xxv} [Woodman](#), *supra*.

^{xxvi} *Id.*

^{xxvii} [MCL 700.5407](#).

^{xxviii} [MCR 2.420\(B\)](#).

^{xxix} [MCL 700.5423\(2\)\(u\)](#).

^{xxx} [MCL 700.5408](#). This statute provides that “If it is established in a proper proceeding that a basis exists as described in section 5401 for affecting an individual’s property and business affairs, the court, without appointing a conservator, may authorize, direct, or ratify a transaction necessary or desirable to achieve a security, service, or care arrangement meeting the protected individual’s foreseeable needs. Protective arrangements include, but are not limited to, payment, delivery, deposit, or retention of money or property; sale, mortgage, lease, or other transfer of property; entry into an annuity contract, contract for life care, deposit contract, or contract for training and education; or an addition to or establishment of a suitable trust.” This statute, however, does not give a guardian authority to waive constitutional rights.

^{xxxi} [Woodman](#), *supra*.

^{xxxii} [Kindred Nursing Centers Ltd. Partnership v Clark](#), 137 S Ct 1421 (2017).

^{xxxiii} *Id.*

^{xxxiv} [Kindred Centers Ltd. Partnership v Wellner](#), 533 SW3d 189 (Ky 2017).

^{xxxv} [Arredondo v SNH SE Ashley River Tenant, LLC et al](#), South Carolina Supreme Court Opinion No. 28011 (March 10, 2021).

xxxvi [“Medicare and Medicaid Programs; Reform of Requirements for Long-Term Care Facilities.” Federal Register 81:192 \(October 4, 2016\) p. 68688.](#)

xxxvii [“Medicare and Medicaid Programs; Revision of Requirements for Long-Term Care Facilities: Arbitration Agreements.” Federal Register 84:138 \(July 18, 2019\) p. 34718.](#)

xxxviii [MCL 445.901 et seq.](#)

xxxix Forced Arbitration Injustice Repeal (FAIR) Act, <https://www.congress.gov/bill/116th-congress/house-bill/1423/text>.

xl [Morrison v. Circuit City Stores, Inc.](#), 317 F3d 646 (6th Cir 2003). *Morrison* discussed the four-part inquiry that is to be applied when determining whether a plaintiff knowingly and voluntarily waived her right to a trial by jury: (1) plaintiff’s experience, background and education; (2) the amount of time the plaintiff had to consider whether to sign the waiver, including the opportunity to consult a lawyer; (3) the clarity of the waiver; (4) consideration for the waiver and (5) the totality of the circumstances.

xli [Kloian v. Domino’s Pizza, LLC](#), 273 Mich App 449, 453; 733 NW2d 766 (2006). The party seeking to enforce the contract has the burden of proving that the contract is valid. *Id.*

xlii A contract or contract provision is procedurally unconscionable where the weaker party had no realistic alternative to acceptance of the terms. [Allen v Michigan Bell Tel Co](#), 18 Mich App 632, 637; 171 NW2d 689 (1969).

xliii A contract or contract provision is substantively unconscionable where the inequity of the term is so extreme as to shock the conscience. [Clark v DaimlerChrysler Corp.](#), 268 Mich App 138, 143-44; 706 NW2d 471 (2005).

xliv [Clark v. DaimlerChrysler Corp.](#), 268 Mich App 138, 143; 706 NW2d 471 (2005).

xlv [General Motors Corp. v. Dept’ of Treasury, Revenue Div.](#), 466 Mich 231, 238; 644 NW2d 734 (2002); [Mastaw v Naiukow](#), 105 Mich App 25; 306 NW2d 378 (1981). See also [Floss v Ryan’s Family Steak Houses, Inc.](#), 211 F3d 306 (CA 6, 2000) (striking an arbitration clause as illusory because defendants’ promised nothing in exchange for their promise to arbitrate all disputes)

xlvi [MCL 691.1686.](#)