Journal of Dispute Resolution

Volume 1990 | Issue 1 Article 10

1990

Constitutionally Recognizing Court Mandated Arbitration: Paradise Found or Problems Abound - Firelock Inc. v. District Court

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CONSTITUTIONALLY RECOGNIZING COURT MANDATED ARBITRATION: PARADISE FOUND OR PROBLEMS ABOUND?

"It has become a truism that we are the most litigious people on earth, and that our machinery for processing all this litigation is sorely over-taxed. If we cannot learn to live together more harmoniously, we must find a means to disagree more efficiently."[1]

"Arbitration is recognized in Colorado as a desirable method of resolving disputes, and is to be fostered rather than discouraged."[2]

Firelock Inc. v. District Court[3]

I. THE PROBLEM

In 1988, McGhee Communications, Inc. brought an action against Firelock Incorporated claiming Firelock had not paid for advertising services which McGhee had performed.[4] Suit was filed in the Boulder County District Court.[5] McGhee certified that the probable recovery would not exceed $50,000, exclusive of interest and costs, and alleged that the case was not exempt from mandatory arbitration.[6]

In its answer, Firelock denied the claimed amount was owed, put forth several affirmative defenses, and demanded a jury trial.[7] Firelock also petitioned the court to prevent the case from being assigned to mandatory arbitration under Colorado's Mandatory Arbitration Act[8] (hereinafter the "Act"). In support of this motion, Firelock claimed the Act violated:

1. separation of powers (Art. III, Art. IV, sections 1 and 9 of the Colorado Constitution);

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1. Nejelski & Zeldin, *Court-Annexed Arbitration in the Federal Courts: The Philadelphia Story*, 42 MD. L. REV. 787 (1983).
2. Wales v. State Farm Mut. Auto. Ins. Co., 559 P.2d 255, 256 (Colo. Ct. App. 1976).
3. 776 P.2d 1090 (Colo. 1989).
4. *Id.* at 1092.
5. *Id.*
6. *Id.*
7. *Id.*
8. COLO. REV. STAT. §§ 13-22-401 to -409 (1987).

2. right of access to courts (Art. II, section 6);
3. right to trial by jury (Art. II, section 23);
4. express Colorado constitutional prohibition against mandatory arbitration (Art. XVIII, section 3); and
5. equal protection (Art. II, section 25 and the equal protection clause of the Fourteenth Amendment to the U.S. Constitution).[9]

The trial court denied Firelock's challenge. Firelock then petitioned the Colorado Supreme Court requesting the issuance of an order preventing the district court from referring the case to arbitration.[10] Also, Firelock urged the Colorado Supreme Court to declare the Mandatory Arbitration Act unconstitutional.[11]

In its holding, the Colorado Supreme Court ruled the Act did not violate the separation of powers doctrine, the right of access to courts, the right to trial by jury, the equal protection clause, or a provision of the Colorado Constitution giving the General Assembly authority over consensual arbitration.[12]

This Note will argue that notwithstanding any criticism of the court-annexed arbitration procedure, the Colorado Supreme Court is taking a leadership position in upholding and expanding the role for arbitration, by recognizing that this form of alternative dispute resolution is less expensive, saves judicial time, provides for confidentially, and most importantly, provides the parties with a sense of fairness in the outcome.

II. HISTORY AND BACKGROUND

A. *Arbitration*

Arbitration, one of the oldest forms of dispute resolution, can be traced back to the ancient Egyptian and Greek cultures.[13] Arbitration's "popularity as a method of resolving disagreements among parties has continued to wax and wane in response to different forces at various periods in Anglo-American legal history."[14] Arbitration's "modern era," however, did not really begin until after World War I when arbitration agreements were first considered legally valid and enforceable.[15]

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9. 776 P.2d at 1093.
10. *Id.* at 1092.
11. *Id.*
12. *Id.* at 1091.
13. *See* Nejelski & Zeldin, *supra* note 1, at 789 (citing Sarpy, *Arbitration as a Means of Reducing Court Congestion*, 41 NOTRE DAME L. REV. 182, 184 (1965)).
14. *Id.*
15. Red Cross Line v. Atlantic Fruit Co., 264 U.S. 109, 124 (1924) (requiring that a court action be stayed upon a showing that a valid contract provision mandates that the parties arbitrate their dispute).

By definition, arbitration is a process where parties to a dispute agree to present their cases before an neutral third party.[16] Historically, arbitration was perceived to have many advantages over traditional litigation. First, although the parties themselves compensate the arbitrator, arbitration is still seen as less expensive than traditional adjudication.[17] Second, arbitration almost always provides a time savings for the parties, as well as providing relief for otherwise overcrowded court dockets.[18] Third, although trial judges may be experts in the law, many parties would rather present their case in front of a recognized expert in the field of their dispute.[19] And finally, as most arbitration hearings are held in private, many potential litigants perceive this confidential setting as a significant legal and business advantage.[20]

B. *Court-annexed Arbitration*

In 1958, Chief Justice Earl Warren, in a speech to the American Bar Association, detailed the nearly 70,000 case backlog in the federal court system and discussed the problems resulting from such delays.[21] By 1970, the number of cases filed but not yet heard had increased to over 114,000[22] and by 1976 that figure grew to almost 160,000[23] cases.

In 1977, when Griffin Bell was appointed United States Attorney General by President Jimmy Carter, he recognized the need for judicial reform by creating an Office of Improvements in the Administration of Justice within the Justice Department.[24] This new office made several recommendations, including "a proposal for court-annexed arbitration of civil cases in the federal courts."[25]

Attorney General Bell's thoughts on the subject were not new. The viability (*i.e.*, constitutionality) of court-annexed arbitration has been tested many times in the past. Two cases from Pennsylvania are routinely discussed and cited for the proposition that mandatory arbitration statutes do not infringe on the constitutional right to a jury trial or the right of access to courts.[26]

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16. Norris, *National Trends in Mandatory Arbitration*, 17 COLO. LAW 1313 (1988).
17. *Id.* at 1314.
18. *Id.*
19. *Id.*
20. *Id.*
21. Address by Chief Justice Earl Warren, *The Problem of Delay: A Task for Bench and Bar Alike*, 44 A.B.A. J. 1043, 1044 (1958).
22. Management Statistics for the United States Courts--1975, at 126 (National Statistical Profile from 1970-75).
23. Management Statistics for the United States Courts--1980, at 129 (National Statistical Profile from 1975-80).
24. Nejelski, *Court Annexed Arbitration*, 14 FORUM 215 (1978).
25. *Id.*
26. Hoffman, *The Constitutionality of Mandatory Arbitration*, 18 COLO. LAW. 455 (1989).

In Re Smith[27] upheld a Pennsylvania statute which provides that "all cases which are at issue where the amount in controversy shall be one thousand dollars or less...shall first be submitted to and heard by a board of three members of the bar of the county for consideration and award."[28] While stating clearly that the Act would be unconstitutional if the arbitrators decision was unappealable, "there is no denial of the right of trial by jury if the statute preserves that right to each of the parties by the allowance of an appeal . . . the only purpose of the constitutional provision is to secure that the right of trial by jury . . . [is] finally determined."[29]

Similarly, in *Kimbrough v. Holiday Inn*,[30] the federal district court upheld a local rule establishing mandatory arbitration. The court held that compulsory arbitration with a right to demand trial *de novo* after an arbitration award did not violate the Seventh Amendment right of trial by jury and did not violate the constitutional guarantees of due process and equal protection.[31]

The Illinois Supreme Court, however, has used the right to jury trial ground for striking down an Illinois law requiring arbitration for minor automobile accident cases[32] and the separation of powers ground for disapproving the mandatory arbitration provisions in the Illinois tort reform legislation.[33]

With regard to the equal protection argument, the various states are also in conflict. An Ohio court in *Grayley v. Satayatham*[34] struck down an Ohio act on equal protection grounds, while the Arizona Supreme Court in *Eastin v. Broomfield*[35] upheld a similar statute. Some of the differences of opinion on these issues no doubt occur because of the specific language in each state constitution. Other variances perhaps take place as the states are still seeking true guidance and leadership in the court-annexed arbitration arena.

C. *The Colorado Mandatory Arbitration Act*

The Colorado Mandatory Arbitration Act was signed into law on May 28, 1987, and is designed to be effective from January 1, 1988 until July 1, 1990.[36] The Act is a self-described "pilot project" designed to apply to all civil cases, filed in eight selected judicial districts of Colorado,[37] which seek money damages of

27. 381 Pa. 223, 112 A.2d 625 (1955).
28. *Id.* at 227, 112 A.2d at 628.
29. *Id.* at 230-31, 112 A.2d at 629 (citations omitted).
30. 478 F. Supp. 566 (E.D. Pa. 1979).
31. *Id.*
32. Grace v. Howlett, 51 Ill. 2d 478, 283 N.E.2d 474 (1972).
33. Wright v. Central Du Page Hosp. Assoc., 63 Ill. 2d 313, 347 N.E.2d 736 (1976).
34. 74 Ohio App. 2d 316, 343 N.E.2d 832 (1976).
35. 116 Ariz. 576, 570 P.2d 744 (1977) (en banc).
36. COLO. REV. STAT. § 13-22-402(1) (1987).
37. The selected judicial districts are the first, third, sixth, seventh, eighth, fourteenth, eighteenth, and twentieth.

$50,000 or less.[38] Matters exempt from mandatory arbitration include controversies involving governmental entities or employees, persons meeting Colorado Supreme Court indigency guidelines, and cases where equitable relief is sought.[39]

A key feature of the new court-annexed procedure provides that a party appealing an arbitrator's award, and thereby requesting a trial *de novo*, will be assessed costs, of up to $1,000, if the trial court's judgment does not improve the appellant's position by more than ten percent.[40]

The Colorado Act makes the selection and compensation of the arbitrator the responsibility of the parties.[41] With regard to the arbitration hearing itself, it should be informal and is not required to conform to strict rules of evidence.[42] The parties may appear with or without counsel, however, failure to appear at all will constitute waiver of the right to a trial *de novo*.[43]

It is within these historical parameters regarding alternative dispute resolution and the current Colorado Mandatory Arbitration Act, that the action in *Firelock v. District Court* began.

III. THE INSTANT DECISION

As drafted, the Colorado Supreme Court decision is important because it examines five potential challenges to the Mandatory Arbitration Act, any of which could invalidate the entire Act. The court, after discussing each area, concludes however, that the Act "does not violate the Colorado Constitution or the United States Constitution."[44]

A. *Separation of Powers*

Firelock contended the Act violated the separation of powers provision of the Colorado Constitution, in that "the Act is an unconstitutional delegation of judicial power to unqualified private citizens because it allows arbitration to be conducted by persons who are not members of the judiciary, but indeed who do not even have to be licensed attorneys."[45] In response, the court notes that "the act does not vest judicial authority in another branch of government . . . because the arbitration panels do not perform a judicial function."[46] For their authority, the justices looked to previous decisions which held that the essence of a "court" is

38. COLO. REV. STAT. § 13-22-402(2) (1987).
39. COLO. REV. STAT. § 13-22-402(5-6) (1987).
40. *See* Hoffman, *supra* note 26, at 456.
41. COLO. REV. STAT. § 13-22-403(1-4) (1987).
42. *See* Littlefield, *Court-Annexed Arbitration Comes to Colorado*, 16 COLO. LAW. 1941, 1944 (1987).
43. *Id.*
44. 776 P.2d at 1100.
45. *Id.* at 1093.
46. *Id.* at 1095.

having the authority to apply a remedy.[47] "It is clear that, under the Act, the arbitrators' decision is not an exercise of the sovereign power of the state because the decision is non-binding, and the arbitrators do not perform a judicial function because they do not possess the final authority to render and enforce a judgment."[48] The Colorado Supreme Court follows the lead of many other states which also hold that arbitrators do not perform judicial functions.[49]

B. *Right of Access to Courts*

Firelock's next claim was the Act violates the parties' right to access to the court system by forcing potential litigants to arbitrate their claims before an arbitrator prior to going to trial.[50] The court disagrees, stating "[m]any other reasonable burdens similar to the one imposed by the Act are present within our system of justice."[51] Also, the decision looks to the fact that "because the Act provides for *de novo* review of the decision of the arbitration panel . . . [it] does not place an unreasonable burden on the right of access to the courts."[52]

C. *Right to a Jury Trial*

Firelock further contended that the Colorado Constitution "establishes a constitutional right to a jury trial in civil actions and the Act impermissibly infringes on this right."[53] In holding otherwise, the Colorado Supreme Court first considered *Edwards v. Elliott*[54] which states that "the United States Constitution's guarantee of a civil jury trial does not apply to the states."[55]

The court next examines the Colorado Constitution, article II, section 23 which provides that "[t]he right of trial by jury shall remain inviolate in criminal cases; but a jury in civil cases in all courts, or in criminal cases in courts not of record, may consist of less than twelve persons, as may be prescribed by law."[56] The Colorado Supreme Court has interpreted this provision as meaning "that trial

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47. *Id.* at 1094.

48. *Id. See* Attorney General v. Johnson, 282 Md. 274, 287, 385 A.2d 57, 65 (1978) (because either party can reject the decision of the arbitration panel and because the panel cannot enforce its decision even if the parties accept it, the panels do not exercise the judicial power of the state in the constitutional sense).

49. *See* DiAntonio v. Northampton-Accomack Memorial Hosp., 628 F.2d 287, 292 (4th Cir. 1980) (following Virginia law); Keyes v. Humana Hosp. Alaska, Inc., 750 P.2d 343, 356-57 (Alaska 1988); Lacy v. Green, 428 A.2d 1171, 1178 (Del. Super. Ct. 1981); Prendergast v. Nelson, 199 Neb. 97, 110, 256 N.W.2d 657, 666-67 (1977); State *ex rel.* Strykowski v. Wilkie, 81 Wis. 2d 491, 520-22, 261 N.W.2d 434, 448-49 (1978).

50. 776 P.2d at 1095.

51. *Id.* at 1096.

52. *Id.*

53. *Id.*

54. 88 U.S. 532 (1874).

55. *Id.* at 557.

56. 776 P.2d at 1096-97.

by a jury in a civil action is not a matter of right under the Colorado Constitution."[57] Additionally, as "the Act provides for *de novo* review by the district court, thereby giving either party the opportunity for a jury trial, and the provision for the payment of the costs of arbitration if the party does not increase its position by ten percent is not an unreasonable burden on the availability of a jury trial."[58]

D. *Equal Protection Clause*

Firelock also argued that as the Act creates two classifications of litigants, depending if the lawsuit is filed in a judicial district designated for the arbitration pilot program or not, the entire Act should be deemed unconstitutional as it violates the equal protection clauses of both the Colorado and United States Constitutions.[59] "In interpreting the equal protection guarantee under the Colorado Constitution, we (the Colorado Supreme Court) have followed the analytical mode developed by the United States Supreme Court in construing the equal protection clause of the Fourteenth Amendment."[60] "The equal protection clause guarantees that all persons who are similarly situated will receive like treatment by the law."[61]

In ruling the Act did not violate the equal protection clause of either constitution, the court opines that "the General Assembly's decision to examine the success or failure of the Act in eight pilot districts is not a violation of equal protection."[62]

> The Fourteenth Amendment does not prohibit legislation merely because it is special, or limited in its application to a particular geographical or political subdivision of the state. Rather, the Equal Protection Clause is offended only if the statute's classification 'rests on grounds wholly irrelevant to the achievement of that State's objective.'[63]

While the Colorado court recognizes that "administrative convenience is not a legitimate governmental purpose,"[64] the "General Assembly chose to examine the success or failure of the Act by implementing its provisions in several judicial districts for a limited period of time during which evidence could be gathered to determine whether the Act would be beneficial on a statewide basis."[65] As

57. *Id.* at 1097. *See* Setchell v. Dellacroce, 169 Colo. 212, 215, 454 P.2d 804, 806 (1969).
58. 776 P.2d at 1096-97.
59. *Id.*
60. *Id. See* Tassian v. People, 731 P.2d 672, 674 (Colo. 1987).
61. *Id. See* J.T. v. O'Rourke, 651 P.2d 407, 413 (Colo. 1982).
62. 776 P.2d at 1098.
63. Holt Civic Club v. City of Tuscaloosa, 439 U.S. 60, 70-71 (1978).
64. *Tassian*, 731 P.2d at 676.
65. 776 P.2d at 1098.

"arbitration is favored by the law in Colorado,"[66] "we hold that the Act does not violate the equal protection guarantee of the United States and Colorado Constitutions."[67]

When considering all these factors together, the rule of law handed down by the Colorado Supreme Court is one which examines the relevant constitutional issues and holds that court-annexed arbitration is legally sound and pending the results of this pilot program, could further open the door to expanded judicial recognition of other methods of alternative dispute resolution.

IV. COMMENT: THOUGHTS FOR THE FUTURE

To be fair, the accolades given to arbitration and the other substitutes for traditional litigation are not universally shared. In his article *Against Settlement*,[68] Yale University Law School Professor Owen Fiss delivers a stinging critique of the settlement (*i.e.*, alternative dispute resolution) process. Fiss argues:

> Consent is often coerced; the bargain may be struck someone without authority; the absence of a trial and judgment renders subsequent judicial involvement troublesome; and although dockets are trimmed, justice may not be done. Like plea bargaining, settlement is a capitulation to the conditions of mass society and should neither be encouraged nor praised.[69]

Conversely, in supporting arbitration and other forms of resolving conflicts, Professor Leo Kanowitz of the University of California, Hastings College of the Law, contends:

> The widespread use of settlement and alternative dispute resolution mechanisms appears, therefore, to respond to a felt need on the part of disputants. Whether their purpose is to avoid the cost, delay, complexity, uncertainty, or anxiety of adjudication, disputants commonly resolve their conflicts in ways other than a full-blown trial. Clearly, there are social as well as personal advantages in avoiding litigation. Were every potentially litigable dispute actually submitted to a full judicial trial, present adjudicatory resources--judges, courthouses, bailiffs, etc--would have to be augmented exponentially.[70]

Additional support for avoiding the traditional courtroom litigation process comes directly from "the . . . revision of Rule 16 of the Federal Rules of Civil

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66. *See* Dominion Ins. Co. v. Hart, 178 Colo. 451, 498 P.2d 1138 (1972).

67. 776 P.2d at 1099.

68. Fiss, *Against Settlement*, 93 YALE L.J. 1073 (1984).

69. *Id.* at 1075.

70. Kanowitz, *Alternative Dispute Resolution and the Public Interest: The Arbitration Experience*, 38 HASTINGS L.J. 239, 242 (1987).

Procedure, which encouraged pretrial consideration of and action on 'the possibility of settlement or the use of extra-judicial procedures to resolve the dispute.'"[71]

Similar to Colorado, other state court systems approve of the arbitration procedure. For example, in *Smith v. Zepp*,[72] the Montana Supreme Court recognized arbitration as "the most speedy and economical means available to parties for a binding resolution of their disputes."[73]

Make no mistake, full-scale adoption of court-annexed arbitration will not, and indeed, is not designed to make litigation a less plausible or obsolete form of lawyering. Arbitration has, however, "proven to be an efficient and equitable method of resolving claims."[74]

Specifically, with regard to constitutionally upholding the Mandatory Arbitration Act, the Colorado Supreme Court is working to make arbitration a viable, effective, and efficient substitute for litigation. The court correctly recognizes that the arbitration process is not a judicial tool that trades important constitutional rights for case expediency, but is a procedure which is respectful of the rights of the parties. The constitutional protections remain, only the parties are given an alternative forum in which they can resolve their differences before heading to the courts.

In the end, the issue of fairness will most likely determine if this program succeeds or fails. Another important factor will be the quality of the men and women selected to serve as arbitrators. If the potential litigants perceive that they were presented with an equal opportunity to put forth their complaint to a knowing and informed arbitrator, who, in turn, handed down a rational and reasonable decision, the Act can certainly succeed. The holding of the instant case is insightful and well reasoned to meet the changing needs of today's society. In sanctioning this court-annexed arbitration by ruling it constitutional, the Colorado Supreme Court validates the principle that this type of alternative dispute resolution is effective because it is administered by a neutral party who is an expert in the field of the dispute, is less expensive, results in a substantial savings of time, and provides a measure of confidentially for the parties.

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71. *Id.* at 243.
72. 173 Mont. 358, 567 P.2d 923 (1977).
73. *Id.* at 369, 567 P.2d at 929.
74. Testa, *Slimming the Docket--A View From the Bench*, 58 FLA. B.J. 60 (1984).