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Green v. Wolfe, 372 P.2d 427 (Mont. 1962)

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commission of the fraud. As previously noted, the general practice is to allow punitive damages where the defendant has assumed no risk in perpetrating the fraud.⁵¹

As a further inducement to the perpetration of fraud, the possibility of gain is provided. Practically speaking, the defrauded party may find the cost of bringing suit prohibitive. On the other hand, an insurance company generally retains a permanent legal staff and can well afford the cost of defending those suits which are prosecuted. As a consequence, many victims of fraud will not prosecute, thus permitting the wrongdoer to profit without the necessity of successfully defending a suit. It is submitted that, where punitive damages are a probable risk to a party, it might be found economically impractical to engaged in fraudulent activities. In order to circumvent the above problems, it seems that the plaintiff should properly have been allowed to proceed in tort and punitive damages should have been allowed.

For the foregoing reasons, it is urged upon the court that it reconsider the position taken in this case.

MYRON E. PITCH

CONTRACT CLAUSE PROVIDING FOR ARBITRATION OF FUTURE DISPUTES IS NOT ENFORCEABLE IN MONTANA.—Plaintiff entered into an agreement with defendant whereby plaintiff agreed to lease land from defendant and run steers on it for a period of four years. Defendant was to supply 600 steers per year and at the end of each year, the steers were to be sold and the proceeds divided. This was done without incident for two years, but during the third year, defendant placed on the land 120 heifers in addition to the steers. A dispute arose over whether the heifers were to be handled under the terms of the agreement. Finally defendant sold both the heifers and the steers without the knowledge or consent of the plaintiff and appropriated the proceeds. Plaintiff remained on the land until the termination of the lease but no more cattle were run under the agreement. After some futile discussion between the parties, plaintiff instituted this suit for his share of the disputed proceeds and the profit he would have made had they continued as the contract stipulated. One of the defenses asserted related to paragraph six of the contract which reads: "Any difference between the parties under this lease that cannot be settled after thorough discussion, shall be submitted for arbitration by a committee of three disinterested persons, one selected by each party here to and the third by the two thus selected, and their decision shall be accepted by both parties." Defendant contended that plaintiff had refused to arbitrate and was thus barred from proceeding with the suit. The court ruled against defendant on all counts and judgment was entered for the plaintiff. On appeal to the Montana Supreme Court, *held*, affirmed. The rights of parties to free access to the courts cannot be interfered with and any such interference is void as viola-

⁵¹1 Cal. App. 2d 736, 336 P.2d 534, 538 (1959).

tive of the Revised Codes of Montana, 1947, section 13-806.¹ *Green v. Wolfe*, 372 P.2d 427 (Mont. 1962).

This statute provides: "Every stipulation or condition in a contract by which any party thereto is restricted from enforcing his rights under the contract, by the usual proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights, is void." The statute is an enactment of the common law as it existed in 1895.² The common law dealing with arbitration clauses is predicated essentially on grounds of public policy³ which have undergone substantial change in the intervening period.⁴ Consequently this article will deal with an examination of: (1) the common law as it existed in 1895, (2) the changes that have occurred since that time, (3) the rationale behind those changes, and (4) the resulting need for new legislation.

The common law generally recognized four distinct types of arbitration clauses. They are: (1) agreements to arbitrate disputes existing at the time the agreement is entered into. These were held valid and enforceable at common law only after actually being arbitrated.⁵ (2) Agreements which make arbitration of disputes not in existence at the time the agreement is consummated a condition precedent to court litigation.⁶ (3) Agreements which limit the scope of arbitration of future disputes to specified factual areas,⁷ and (4) clauses, such as found in the instant case, which make every possible future dispute, factual or legal, the subject of arbitration and such arbitration is final. Clauses of this latter type, which are the subject of this article, were held unenforceable at common law.⁸

Apparently the problem first came to the attention of the English courts during a period when judges were dependent on a fixed fee per case as their means of livelihood.⁹ Consequently, as every case arbitrated deprived some judge of a fee he otherwise would have collected, judges looked with disfavor on this attempt to deprive them of their income.¹⁰ From this early judicial antagonism arose the doctrine that arbitration clauses were void as against public policy.¹¹ This was buttressed by the

¹Hereinafter REVISED CODES OF MONTANA will be cited at R.C.M.

²*Wortman v. Montana Cent. Ry.*, 22 Mont. 266, 278, 56 Pac. 316, 321 (1899).

³*Fidelity & Cas. Co. v. Eickhoff*, 63 Minn. 170, 65 N.W. 351 (1895); *Vynior's Case*, 4 Coke, Part VIII, 81b, 82a (1610).

⁴Notes 34 and 35 *infra*.

⁵*Vynior's Case*, *supra* note 3. All states with the exception of South Dakota and Oklahoma specifically provide for such arbitration by what are called submission statutes. Montana's submission statute is R.C.M. 1947, § 93-201-1.

⁶Prior to 1855, these clauses were not valid at common law. In that year, *Scott v. Avery*, 5 H.L. Cas. 811, 10 Eng. Rep. 1121 (1855) held this type of agreement valid. However, the case was almost immediately reversed so that the general common law holding was that such agreements were invalid. The same result was reached in this country in *W.H. Blodgett Co. v. Bebe Co.*, 190 Cal. App. 665, 214 Pac. 38 (1923).

⁷These clauses, sometimes called appraisal agreements, are generally considered valid and enforceable. *In re Lower Baraboo River Drainage Dist.*, 199 Wis. 230, 225 N.W. 331 (1929).

⁸*Thompson v. Charnock*, 8 T.R. 139, 101 Eng. Rep. 1310 (1799).

⁹Lord Campbell made this statement in discussing the unworthy beginnings of the rule, and used it as justification for its reversal. *Scott v. Avery*, *supra* note 6.

¹⁰*Ibid.*

¹¹This is Lord Campbell's final conclusion concerning the rule he was about to overrule. *Scott v. Avery*, *supra* note 6.

rationale that courts should not be ousted of their jurisdiction, nor parties to a contract deprived of their right of access to the courts.¹² The rule holding invalid clauses calling for arbitration of future disputes became well established at common law and was early brought to this country where it again found fertile soil.¹³ By 1895, it is doubtful that a single jurisdiction had held to the contrary.¹⁴ Perhaps the best summation of the rule was given by Justice Hunt who said:¹⁵

Every citizen is entitled to resort to all the courts of the country, and to invoke the protection which all the laws of all those courts may afford him. A man may not barter away his life or his freedom or his substantial rights.... He cannot bind himself in advance by an agreement which may be specifically enforced, whenever the case may be presented.

Soon after the turn of the century, courts began to question the concepts on which the common law concerning arbitration clauses was based.¹⁶ There were a variety of reasons responsible. Among these was the enactment of submission statutes which allowed arbitration of existing disputes.¹⁷ The Minnesota court reasoned that the passage of such statutes signaled an end to the public policy against arbitration of any kind.¹⁸ If the parties could agree to be bound by the results of an arbiter's¹⁹ decision as to existing disputes, it did not seem to be violative of any public policy to allow them to be bound as to a future dispute.²⁰ Further, an arbiter's decision is not self-enforcing, but requires a court order declaring it to be a judgment of the court before it can be enforced against the adverse party.²¹

¹²Myers v. Jenkins, 63 Ohio St. 101, 57 N.E. 1089 (1900).

¹³Tobey v. County of Bristol, 23 Fed. Cas. 1313, (No. 14065) (County Ct. of Mass. 1845).

¹⁴At least this writer's research has not discovered any. However, in Perkins v. United States Elec. Light Co., 16 Fed. 513 (S.D.N.Y. 1881), the court enforced an arbitration clause when it was a condition precedent.

¹⁵Home Ins. Co. v. Morse, 87 U.S. (20 Wall.) 445, 451 (1874). The court held that parties to a contract could not agree to try any dispute arising out of the contract in the state courts instead of Federal courts.

¹⁶Zindorf Constr. Co. v. Western Am. Co., 27 Wash. 31, 67 Pac. 374 (1901) (2 judges dissenting). Prior to this decision, Washington had held that failure to arbitrate an *existing dispute* was a bar to court action. Here they extend the doctrine to include *future disputes*. United States Asphalt Ref. Co. v. Trinidad Lake Petroleum Co., 222 Fed. 1006 (S.D.N.Y. 1915). Judge Hough reluctantly upheld the common law, feeling bound by earlier decisions of higher courts.

¹⁷Park Constr. Co. v. Independent School Dist., 209 Minn. 403, 296 N.W. 475 (1941) (2 judges dissenting). This case overruled several earlier Minnesota cases, reasoning that the passage of the Minnesota submission statute in 1939 showed that the public policy of Minnesota favored arbitration of *all* disputes.

¹⁸*Ibid.*

¹⁹The distinction between arbiter and arbitrator is no longer adhered to. RUSS. ARB. 112.

²⁰Ezell v. Rocky Mountain Bean and Elevator Co., 76 Colo. 409, 232 Pac. 680 (1925); Park Constr. Co. v. Independent School Dist., *supra* note 17. However, these courts were not faced with the problem of a statutory statement of public policy such as exists in Montana.

²¹In Montana, this is accomplished under the provisions of R.C.M. 1947, § 93-201-6 by filing the submission with the clerk of court in the county where one of the parties resides. After five days and a showing that both parties have received notice of the filing, the award must be entered in the judgment book *unless* one of the parties has asked for a stay of judgment to allow the court to review the judgment. After judgment has been entered, it has the force of any other court judgment.

This permits the courts to judicially review the arbitrator's decision.²² Under this rationale, the argument has been advanced that the court is not ousted of its jurisdiction.²³ Other courts have taken the position that arbitration clauses do not affect the court's jurisdiction, thus making the question of ouster unnecessary. To support this conclusion, courts have stated that arbitration clauses simply remove a controversy from the arena of litigation and are therefore in the same category as an out of court settlement or a covenant not to sue.²⁴ Further since the courts will enforce both an agreement to arbitrate an existing dispute and any arbitrator's decision voluntarily submitted to, even if arising out of a future dispute, some courts have thought it illogical to void an agreement to submit a future dispute to arbitration since in each instance the dispute is removed from the jurisdiction of the courts.²⁵ These various arguments are well summed up by Chief Justice Leslie, speaking for the Texas Court of Civil Appeals.²⁶

Formerly, no doubt, courts looked with jealousy upon arbitrations generally, and seemed to regard them as means or efforts to oust the courts of jurisdiction in matters of litigation. Such is not the attitude of courts at present. It is the view now that the 'more intelligent' judicial sentiment is strongly in favor of arbitration. It is said to be favored for the reason that it is speedier, less expensive, and a more amicable way, than is offered by litigation, for the settlement of differences.

Finally some courts have thought it anomalous to state that such clauses are invalid²⁷ but still legal.²⁸ This means that although a party can violate the clause and bring his grievance to court, the opposing litigant can sue for damages for the breach of the arbitration clause. Courts are generally agreed, however, that the only measure of damages would be the difference

²²As to the factor determinative of whether the award will be set aside, see *Alliance Constr. Co. v. United States*, 79 Ct. Cl. 730 (1934); In the *Matter of Arbitration between Exercycle Corp. and James Maratta*, 9 N.Y.S.2d 329, 174 N.E.2d 463 (1961).

²³Of course, if this is followed too strictly, the primary purpose of arbitration is somewhat emasculated. People usually arbitrate as a cheaper and easier method of adjudicating disputes. If the courts regularly overturn the arbitrator's decision simply because they would have reached a different conclusion, the parties are forced to use the courts and there is more expense and greater delay. If, on the other hand, the courts automatically uphold the arbitrator's decision, then to say that the courts are not ousted of jurisdiction because they can review the arbitrator's decision is to tread a precarious semantical line. For an excellent discussion of this problem, see Jalet, *Judicial Review of Arbitration: The Judicial Attitude*, 45 CORNELL L.Q. 519 (1960).

²⁴*Park Constr. Co. v. Independent School Dist.*, *supra* note 17. Both out of court settlements and covenants not to sue are common methods of settling disputes. The argument, however, would seem to lose some of its vitality when it is remembered that agreements to submit existing disputes to arbitration are universally held valid and the examples mentioned by the Minnesota court likewise refer to existing disputes. Thus to sustain the argument, it would seem that the court must show some connection between existing and future disputes.

²⁵*Kulukundis Shipping Co., S/A, v. Amtorg Trading Corp.* 126 F.2d 978 (2d Cir. 1942).

²⁶*Ferguson v. Ferguson*, 110 S.W.2d 1016, 1021 (Tex. Civ. App. 1937).

²⁷In most instances, the words "invalid" and "unenforceable" are used synonymously. However, the courts usually seem to mean unenforceable.

²⁸*United States Asphalt Ref. Co. v. Trinidad Lake Petroleum Co.*, *supra* note 16.

between the judgment of the court and what the arbiter would have given.⁸⁰ But since generally there has been no arbitration, this measure of damages is impossible to apply. Thus only nominal damages are given and the non-breaching party is left with a right violated for which there is no remedy.

For these reasons the common law regarding arbitration has been found to be unsatisfactory. Some have thought that the courts are not ousted of jurisdiction by a clause sending to arbitration all future disputes; others reason that even if there is an ouster, "it is surely a singular view of judicial sanctity which reasons, that, because the Legislature has made a court, therefor everybody must go to court."⁸¹ Thus judicial attitude has slowly shifted over the years to a position less antagonistic toward arbitration. In 1920, New York adopted an act⁸² stating that all agreements to arbitrate future disputes were valid, irrevocable, and enforceable.⁸³ Congress soon followed⁸⁴ as did many of the states.⁸⁵ A combination of statutory enactments and judicial decisions⁸⁶ shows that at least 20 of the states have reversed the common law and hold that agreements to arbitrate future disputes are enforceable and a good defense to an action brought by a party refusing arbitration.

The Montana court first considered a contract containing an arbitration clause in 1891.⁸⁷ There, the court held that such a clause would not operate to bar a party from proceeding in court if he did not arbitrate. This, as shown earlier, was the general common law ruling. While other jurisdictions have abrogated the common law antagonism toward arbitration of future disputes, the codification of the common law in 1895⁸⁸ has produced the opposite result in Montana. In *Cotter v. Grand Lodge A.O.U.W.*,⁸⁹ the court found the statute inapplicable because the contract was signed before its passage and held that since the clause provided for arbitration as a condition precedent to court action, it was valid and enforceable, at

⁸⁰*Munson v. Straits of Dover S.S. Co.*, 102 Fed. 926 (2d Cir. 1900); *Electrical Research Prod. v. Vitaphone Corp.*, 20 Del. Ch. 4017, 171 Atl. 738 (1943).

⁸¹*United States Asphalt Ref. Co. v. Trinidad Lake Petroleum Co.*, 222 Fed. 1006, 1009 (S.D.N.Y. 1915).

⁸²Laws of New York, 143d session, vol 2, ch. 275 at 803 (1920).

⁸³The common law was not codified in New York. Only Montana, Missouri, and South Dakota codified the common law in this respect.

⁸⁴9 U.S.C. § 2 (1952) (enacted first in 1925).

⁸⁵*Ariz. Rev. Stat. ch. 12, § 1509* (1956); *Cal. Code of Civ. Pro., § 1280* (West 1955); *Gen. Stat. Conn. ch. 52, § 408* (1958); *Rev. Laws of Hawaii ch 116, § 4170* (1935); *Rev. Stat. of La. ch. 9, § 4201* (1950); *Ann. Laws of Mass. ch. 251, § 14* (1956); *Comp. Laws of Mich. § 645.1* (1948); *Minn. Stat. 572.08* (1957); *N.H. Rev. Stat. Ann. 542.1* (1955); *N.J. Stat. Ann. 2A:24-1* (1952); *Ohio Rev. Code Ann. 274.101* (1953); *Or. Rev. Stat. ch. 33, § 220* (1961); *Penn. Stat. Ann. tit. 5, § 21* (1930); *Gen. Laws of R.I. ch. 10, § 3-2* (1957); *Wis. Stat. ch. 298, § 01* (1961).

⁸⁶*Zindorf Constr. Co. v. Western Am. Co.*, 27 Wash. 31, 67 Pac. 374 (1901); *United Ass'n of Journeymen and Apprentices v. Stine*, 76 Nev. 189, 351 P.2d 965 (1960); *Ezell v. Rocky Mountain Bean and Elevator Co.*, 76 Colo. 409, 232 Pac. 680 (1925); *Ferguson v. Ferguson*, *supra* note 26. This list does not include those states that first overruled the common law by judicial action and then codified the court's decision.

⁸⁷*Randall v. American Fire Ins. Co.*, 10 Mont. 340, 25 Pac. 953 (1891).

⁸⁸R.O.M. 1947, § 13-806.

⁸⁹23 Mont. 82, 57 Pac. 650 (1899).

least insofar as it concerned a voluntary mutual benefit society.³⁸ Judge Piggot had this to say about the rule in general:⁴⁰

The common-law doctrine that a provision in an ordinary contract requiring all differences between the parties touching their rights and liabilities thereunder to be submitted to arbiters, whose decision or award shall be conclusive and final, will not be allowed to bar the litigation of such differences in the courts of the land, is an anomaly, and inconsistent with the right freely to contract; and, if it were not so firmly and well-nigh universally established, we apprehend that it would be over-turned, as resting upon no solid foundation of reason. Its operation should not be extended by construction, nor should it ever be invoked to nullify or impair contractual provisions not clearly infected with the supposed evils intended to be cured or prevented.

Such a modern view however, could not last under the statute. In *Wortman v. Mont. Cent. Ry.*,⁴¹ also decided in 1899, the court held the statute applicable in a situation where an engineer was to be the sole arbiter of any dispute over the construction of the contract or performance under it. In 1936,⁴² the Montana court faced an identical problem as that faced in the *Cotter* case,⁴³ holding that a clause making arbitration a condition precedent to litigation violated the statute.⁴⁴ And finally, in the instant case,⁴⁵ the court held that an arbitration clause embracing all future disputes violated the statute.

The Montana court, however, has judiciously restricted the use of the statute, holding at various times that the statute does not apply where: (1) issues of ultimate liability are not concerned,⁴⁶ (2) the clause limits arbitration to a specific area,⁴⁷ or (3) arbitration has actually been entered into.⁴⁸ The court has stated:⁴⁹

It is the policy of the law to favor the settlement of disputes by arbitration and every reasonable intendment will be indulged to give effect to such proceedings. The decision by arbitration is the decision of a tribunal of the parties' own choice and election. It is a popular, cheap, convenient and domestic mode of trial, which the courts have always regarded with liberal indulgence.

It becomes clear then, that whenever the arbitration clause embraces the sum total of future disputes that can arise out of the contract, it is

³⁸*Supra* note 38. Because of the personal nature of such societies, the courts have often recognized this exception and held that arbitration clauses in their by-laws are not void as against public policy.

³⁹*Supra* note 38 at 89, 57 Pac. at 652.

⁴⁰22 Mont. 266, 56 Pac. 316 (1899).

⁴¹*Cacic v. Slovenska Narodna Podporna Jednota*, 102 Mont. 438, 59 P.2d 910 (1936).

⁴²*Supra* note 38.

⁴³*Supra* note 42.

⁴⁴Instant case at 433.

⁴⁵*Polley's Lbr. Co. v. United States*, 115 F.2d 751 (9th Cir. 1940).

⁴⁶*Clifton-Applegate-Toole v. Drainage Dist. No. 1*, 82 Mont. 322, 267 Pac. 207 (1928).

⁴⁷*Lee v. Providence Wash. Ins. Co.*, 82 Mont. 264, 266 Pac. 640 (1928).

⁴⁸This statement first appears in *Lee v. Providence Wash. Ins. Co.*, *supra* note 48 at 273, 266 Pac. at 643. It is quoted in *Clifton-Applegate-Toole v. Drainage Dist. No. 1*, *supra* note 47 at 329, 267 Pac. at 212, and was reiterated as recently as 1940 in *Polley's Lbr. Co. v. United States*, *supra* note 46 at 754.

necessary that R.C.M., 1947, section 13-806 be applied and the clause is not enforceable. It is equally clear that the courts favor arbitration. Thus by virtue of the statute, Montana finds itself clinging to a doctrine long since removed from the mainstream of legal thinking and pushed into the eddies and backwash of legal anachronisms. The legislature passed what appeared, in 1895, to be a suitable law. In retrospect, however, it seems that Montana codified what has come to be a poorly reasoned and heavily criticized common law policy. The Montana court finds itself in somewhat the same situation as did District Judge Hough in 1915, when he considered a motion to enforce an arbitration clause. He stated,⁶⁰ "Inferior courts may fail to find convincing reasons for it; but the rule must be obeyed and these motions be severally denied." It is submitted that the Montana statute reflects an antiquated and repudiated public policy. A rule is valid only so long as its underlying fundamentals are sound. When the erosions of time have dissipated these foundations, the rule itself must fall. The Montana Legislature should repeal this statute.

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⁶⁰United States Asphalt Ref. Co. v. Trinidad Lake Petroleum Co., 222 Fed. 1006 (S.D.N.Y. 1915).

