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New Jersey Supreme Court Rights Course of Arbitrability

By Robert E. Bartkus – August 07, 2019

On March 12, 2019, an ADR Committee article, "New Jersey Court Puts Brakes on Arbitration after Car Deals are Called Off," reported on the precedential Appellate Division opinion in *Goffe v. Foulke Management Corp.* 454 N.J. Super 260 (App. Div. 2018), declining to compel arbitration because the car purchases were said to have been "rescinded." When disputes arose regarding the transaction, and the customers returned the cars, the sales agreements were deemed to have been rescinded, either by their terms or based on a subsequent agreement rescinding the purchase. The Appellate Division held that the legal effect of the rescission was to "return [the parties] to square one—in legal terms, the status quo ante . . . ." As the article stated: "Just as the rescission nullified the parties' obligations concerning the car purchase, [the court held] 'there can be no doubt that the arbitration provisions [in the original contracts] were discarded in the process.'" The court also found that the dealer may have failed to comply with the Consumer Fraud Act requirement to provide a copy of the purchase agreement at the time of the transaction, in which case the purchase agreement would be unenforceable. It remanded to the trial court to require discovery and determine whether the allegations of fraud were substantiated and, based on those findings resolve the motion to compel arbitration anew. The broader implications of the *Goffe* decision were discussed in a May 24, 2018 article, "New Jersey Holds That Rescission Defeats Arbitration."

The New Jersey Supreme Court granted a petition for certification to review the decision which it reversed and remanded, thereby compelling arbitration of all issues. 238 N.J. 191, 2019 N.J. LEXIS 791 (Jun. 5, 2019).

The Supreme Court opinion began with a recitation of hornbook arbitration law—cases such as *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), and *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440 (2006), which the Appellate Division did not cite—holding that the arbitration clause within a contract is severable from the underlying contract. Thus, unless the parties are disputing whether the arbitration clause itself was procured by fraud, general allegations of fraud in connection with the formation of the contract as a whole must be decided in the arbitration. Likewise, under *Rent-A-Center, W., Inc. v. Jackson*, 561 U.S. 63 (2010), questions as to whether the parties have delegated questions of arbitrability to the arbitrator are severable from the arbitration clause; unless the delegation clause itself is challenged, arbitrability questions must be resolved by the arbitrator.

As the cases show, and the lower court decision proved, it often is easier to state the general rule than to know its parameters and how it is to be applied in a specific situation. Thus, after *Prima Paint* held that allegations of fraud in the inducement of the underlying contract were to be determined by the arbitrator, there was a thought to distinguish between whether contracts were void or voidable. But that did not hold sway for long. Third Circuit cases distinguished between fraud in the inducement and fraud in the execution, the latter of which is a gateway issue for the court. *See* *Connors v. Fawn Mining Corp.*, 30 F.3d 483 (3d Cir. 1994). Whether a

person had authority to execute the underlying agreement also is a formation, gateway issue for the court. *Par-Knit Mills, Inc. v. Stockbridge Fabrics Co.*, 636 F.2d 51 (3d Cir. 1980). And the Supreme Court has made iterative decisions regarding what is a formation issue for the court, and what goes to the arbitrator. *Buckeye* noted, for example, that a court may still be required to determine whether a contract was "concluded"— as opposed to whether the contract was "valid." 546 U.S. at 444 n.1. Giving *Sandvik AB v. Advent Int'l Corp.,* 220 F.3d 99 (3d Cir. 2000), as an example, it noted that courts still may be required to decide whether the contract was signed, and whether the signor had the authority or capacity to sign— without violating the severability principle. Whether the *Buckeye* contract was usurious, and thus not legal or enforceable under state law, was for the arbitrator. When the underlying contract was formed or ratified also can be for the court, as in *Granite Rock Co. v. Int'l Board of Teamsters*, 561 U.S. 287 (2010).

This is where *Goffe* adds to our understanding of severability—at least in New Jersey. Whereas the Appellate Division had said a court must determine whether a contract was rescinded, cancelled, or unenforceable because it failed to satisfy a requirement of the state's Consumer Fraud Act, the state Supreme Court disagreed. Arguments of a bait-and-switch fraud, or that the agreements were not "knowingly and voluntarily" signed and agreed to (in that context), addressed contract enforceability rather than formation. All of these defenses must be decided by the arbitrator, without the need for discovery and further consideration by the trial court.

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