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CLERK U S DISTRICT COURT
DISTRICT OF ARIZONA
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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

ANGELICA BARAJAS and GERARDO)
ARENIVAS,)
)
Plaintiffs,)
)
vs.)
)
PHP, et al.)
)
Defendants.)

No. CIV 97-0954 PHX RCB

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NATIONAL CLEARING HOUSE
FOR LEGAL SERVICES, INC.

Defendant PHP and Defendant Kevin Keller¹ have filed

¹Defendant Keller asserts that he has standing in this matter pursuant to Britton V. Coop, 4 F.3d 742 (9th Cir 1993). This case stands for the proposition that no individual has standing to assert the contractual right to compel arbitration unless one of three exceptions apply: (1) the individual is a third-party beneficiary to the contract; (2) the individual is a successor in interest to the contract; or (3) the individual is within a class of agents intended to benefit from the arbitration clause. Id. at 745-46.

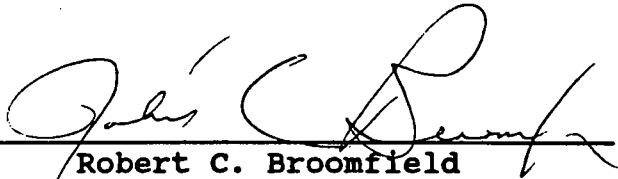
Essentially, Keller's claim is that Plaintiff's cause of action against him arose out of his role as an officer of PHP. Thus, he may rely upon the written arbitration clause for the same reasons that PHP can. From this argument, it is clear that Keller intends to rely on the third exception above.

In Britton the court analyzed the requirements to meet this exception. Not only must the individual be an agent of the signor company, but the alleged wrongdoing of the agent must stem

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Plaintiff's motion to stay).

DATED this 6 day of November, 1997.


Robert C. Broomfield
United States District Judge

Copies to counsel of record

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1 motions to stay this action pending an arbitration hearing in
2 San Diego, California. Plaintiff's oppose such a stay. The
3 matter is fully briefed, and oral argument was heard on
4 October 20, 1997 at which time the matter was taken under
5 advisement. The court is now prepared to rule.

6 BACKGROUND

7 Plaintiffs Angelica Barajas and Gerardo Arenivas are
8 native Spanish-speaking individuals. Barajas and Arenivas
9 were contacted separately by agents of Defendant PHP about
10 home purchasing assistance. Seeking to obtain help financing
11 homes, both Plaintiffs entered into contracts with PHP. The
12 negotiations occurred mostly in Spanish, but the contracts are
13 written entirely in English.

14 Plaintiffs each paid PHP \$2000 when they signed the
15 contract. PHP claimed that it was a school, and entitled its
16 form contract as a "Student Enrollment Agreement." (Defendant
17 PHP's exhibit B). However, Plaintiff's were never given any

18 from the contract containing the arbitration clause. Id. at 727.
19 Thus, the court found that the actions of the individual
20 Defendant to attempt to dissuade Plaintiff's from pursuing their
21 rights and remedies did not allow him to compel arbitration
because the acts were unrelated to the underlying contracts. Id.
at 747-48.

22 The present situation differs from the situation in Britton.
23 Plaintiffs alleged in their complaint that Defendant Keller
24 exercises day-to-day control of PHP as principal shareholder and
25 an officer and that Keller took actions to assure Plaintiffs that
26 they would receive assistance in purchasing a home. The latter
allegation relates directly to the context of the contract signed
by both Plaintiffs. Thus, although Britton denied standing to
the individual Defendant actually involved in the case, its
reasoning suggests that standing would in fact be proper in the
present situation.

1 suspect and are invalid if they do not comport to the parties'
2 reasonable expectation or if they are unconscionable. Bos
3 Material Handling, Inc. v. Crown Controls Corp., 186 Cal.
4 Rptr. 740, 744 (Cal. Ct. App. 1983).

5 As discussed above, it is clear that the arbitration
6 clause did not comport to the parties' reasonable
7 expectations. Moreover, both contracts are one sided and the
8 procedure under which they were executed is highly
9 questionable. Furthermore, there is some question as to
10 whether the Plaintiffs were even aware that they were entering
11 into contracts when they signed the agreements. The contracts
12 were form contracts; the parties were given no opportunity to
13 bargain; the contracts were not clearly explained to the
14 Plaintiffs; the contracts were written in a language foreign
15 to the Plaintiffs; and the terms of the contract were highly
16 questionable. As such, under the facts alleged, the
17 arbitration agreement is likely invalid under California law
18 as well. Therefore, the court will deny the motion to stay.

19 IT IS ORDERED denying Defendant PHP's motion to stay
20 pending arbitration.

21 IT IS FURTHER ORDERED denying Defendant Kevin Keller's
22 motion to stay pending arbitration. The clerk should note and
23 correct the docketing error on this motion (labeling it as

24 . . .

1 home-purchasing education or assistance, never received any
2 books or educational material, and never received any
3 instruction of any kind.

4 Plaintiffs claim that they were told by agents of PHP
5 that the money they put down when signing the contracts was to
6 be used for down payments on homes. However, it appears that
7 PHP may not rely on its home-purchasing assistance program to
8 satisfy its "students." Allegedly, the most significant
9 portion of PHP's business is to recruit individuals to enter
10 into the contracts, and encourage the individuals to
11 subsequently recruit others. Successful recruiters receive a
12 portion of the subsequent recruits' tuition. PHP allegedly is
13 nothing more than a well-disguised pyramid scheme. In fact,
14 it appears from Plaintiff's response that Plaintiffs were
15 recruited by individuals who had previously entered into the
16 same type of contracts. These individuals also served as
17 interpreters for Plaintiffs during the enrollment process.

18 Not surprisingly, Plaintiffs now claim that they never
19 received any home purchase assistance, and that Defendants
20 have refused to refund their tuition. Plaintiff brought suit
21 in this court, alleging several different causes of action in
22 their complaint.

23 Defendants now ask this court to stay this proceeding
24 pending arbitration. The contracts signed by both Plaintiffs
25 contain an arbitration clause, and a clause requiring any
26 factfinder to interpret the contract under California law.

1 clause, or even that such a clause existed in either contract.
2 Moreover, it is unreasonable to assume that the Plaintiffs,
3 two individuals new to this country, should go to an entirely
4 different state to settle any disputes that arise under the
5 contracts. Furthermore, the clause requiring such travel
6 benefits only PHP. Accordingly, the court must find the
7 arbitration agreements invalid under Arizona law based on the
8 facts alleged.

9 However, this court will consider California law as well.
10 It is clear that California law results in the same decision.
11 Under California law it is the duty of the court to determine
12 whether grounds exist to invalidate the arbitration agreement
13 or whether allegations of illegality go to the heart of the
14 contract, such that the entire contract would never have
15 existed.³ See Moncharsh v. Heily & Blase, 832 P.2d 899, 916-
16 17 (Cal. 1992); Bianco v. Superior Court, 71 Cal. Rptr. 322
17 (Cal. Ct. App. 1968); California State Council of Carpenters
18 v. Superior Court, 89 Cal. Rptr. 625, 633 (Cal. Ct. App.
19 1970). Adhesion contracts in California, like Arizona, are

20
21 ³The key here is the illegality of the entire contract. That
22 is, if the entire contract is illegal or against public policy,
23 the contract, including the arbitration clause, may be held
24 invalid. When dealing with potentially illegal contracts, "[i]f a
25 contract includes an arbitration agreement, and grounds exist to
26 revoke the entire contract, such grounds would also vitiate the
arbitration agreement." Moncharsh, 832 P.2d at 917. This
situation differs from fraud in the inducement on the underlying
contract. Id. at 917 n.13. Some act of fraud in procuring the
contract is not enough to prevent arbitration, unless the fraud
is directed at the arbitration clause. Fraud in the inducement
alone may be decided by an arbitrator.

1 However, Plaintiffs allege that neither clause was explained
2 to them and that agents of PHP, who translated the contract,
3 fraudulently hid the true nature of the contract.

4 DISCUSSION

5 The question before this court is whether the arbitration
6 clause in the contracts between PHP and Plaintiffs is
7 enforceable. The Plaintiffs claim that the clause was unknown
8 to them, that the contracts are unconscionable, and that PHP
9 fraudulently obtained their signatures on the agreements. The
10 Plaintiffs assert both fraud in the inducement and fraud in
11 the execution of the contract.

12 The existence of an agreement to arbitrate is a question
13 for the district court. Wagner v. Statton Oakmont, Inc., 83
14 F.3d 1046, 1048 (9th Cir. 1996). While there is a strong
15 policy favoring arbitration, courts must not ignore the
16 possibility that an agreement to arbitrate is invalid.
17 Stevens/Leinweber/Sullens, Inc. v. Holm Development and
18 Management, Inc., 795 P.2d 1308, 1313 (Ariz. Ct. App.
19 1990) (citing Mitsubishi Motors Corp. v. Soler Chrysler-
20 Plymouth, Inc., 473 U.S. 614 (1985)). In making this
21 threshold determination the court must apply state-law
22 principles of contract interpretation. Wagner, 83 F.3d at
23 1049.

24 Initially, the court must determine which state's law to
25 apply. The contract contains a clause invoking California
26 law, rather than the law of this forum. While Plaintiffs

1 its true purpose unclear. However, the evidence that
2 solidifies this court's decision is the evidence that shows
3 that the arbitration clause was included in an adhesion
4 contract, and that the clause was clearly not within the
5 reasonable expectations of the Plaintiffs, the weaker party.

6 The court in Broemmer refused to enforce an arbitration
7 agreement when the patient had no opportunity to negotiate the
8 terms of the agreement, and when it was offered on a take-it
9 or leave-it basis. Moreover, the terms of the agreement
10 favored the stronger party, the medical center that prepared
11 the agreement. See Broemmer, 840 P.2d 1013. The court found
12 that the agreement was not within the expectations of the
13 parties, regardless of the fact that the arbitration provision
14 was boldly titled and explicitly written. Id.

15 Similarly, the nature of the contracts in the present
16 case is suspect. The agreements are adhesion contracts. Both
17 Plaintiffs signed identical contracts, both contracts were
18 standard contracts used by Defendant. The Plaintiffs, even if
19 they had spoken English and understood the nature of the
20 transaction, were provided prepared form documents and didn't
21 bargain over the terms of the contract. As an adhesion
22 contract, the contract itself is outside the reasonable
23 expectation of the Plaintiffs, the weaker parties. In fact,
24 they were assured that the money they provided would go toward
25 their new homes, when the contracts provide no such guarantee.
26 They were not informed about the nature of the arbitration

1 argue that Arizona law should be applied, Defendants argue for
2 the enforcement of the clause.

3 In analyzing a conflict-of-law situation the district
4 court should apply the law of the forum state. Thus, this
5 court shall apply Arizona's conflict-of-law provisions.
6 Arizona follows the Restatement (Second) of Conflict of Laws.
7 Landi v. Arkules, 835 P.2d 458, 462 (Ariz. App. 1992) (citing
8 Burr v. Renewal Guaranty Corp., 468 P.2d 576, 577 (Ariz.
9 1970)).

10 "The legality and validity of a contract provision . . .
11 cannot be resolved by an explicit provision in the contract:
12 It is a question of law." Landi, 835 P.2d at 462 (citing
13 Restatement (Second) of Conflict of Laws §187 cmt.d). Arizona
14 courts generally apply the chosen law unless it is contrary to
15 the law of the state that has a "materially greater" interest
16 in the matter. Id. However, when a choice of law provision
17 is ineffective (judged initially by the chosen law), the law
18 of the forum with the "most significant relationship to the
19 transaction and to the parties" applies. Id. at 463.

20 Thus, whether this court applies California or Arizona
21 contract interpretation law to the present case turns on
22 whether the choice of law provision is effective, and, if it
23 is effective, whether California law is contrary to the law of
24 a state with a materially greater interest in the matter. The
25 court believes that, in reality, the law of California and the
26 law of Arizona are strikingly similar. See infra. However,

1 to the program receives a bonus for recruiting more
2 individuals to participate. The prominent feature of this
3 multi-level marketing program was the promise of recouping any
4 losses, in the form of money paid in without the ability to be
5 approved for a home loan, by bringing in other "students."
6 The same individuals in charge of recruiting the Plaintiffs
7 were the Plaintiff's only source of information or
8 translation. These individuals had a strong interest in
9 getting Plaintiffs to sign, but little interest in explaining
10 the risks to Plaintiff.

11 Plaintiffs claim not only fraud in the inducement of
12 these contracts, but also fraud in the execution. Plaintiffs
13 claim that they were misled as to the nature of the documents,
14 and that they believed they were signing documents relating to
15 the purchase of a home. They seem unaware that they were even
16 signing contracts. They understood their actions only to be
17 necessary to acquire financing for new homes, and were told to
18 initial each page if they wanted to purchase a home and wanted
19 assistance in doing so. The court concludes that Plaintiffs
20 did not knowingly agree to arbitrate, and their version of
21 events suggest that they didn't even knowingly enter into a
22 contract.

23 Therefore, the Plaintiffs have alleged sufficient facts
24 to determine that the arbitration clause was not explained to
25 them, that the clause was not clearly identified in the
26 contract, and that the contract was extremely one-sided and

1 the court will consider both separately. Initially, it is
2 important to observe that Arizona has a materially greater
3 interest in this matter than California.

4 These contracts were negotiated and signed in Arizona.
5 All activities resulting from the negotiation of the contracts
6 occurred in Arizona. Both Plaintiffs are citizens of Arizona.
7 The Defendant PHP conducts significant business in Arizona.
8 Thus, Arizona has a great interest in the resolution of this
9 matter according its own laws. Therefore, even if the
10 contracts' clause is effective, if California law is contrary
11 to the policies of Arizona, Arizona law will be applied
12 because Arizona has a materially greater interest in the
13 matter. Therefore, this court will initially consider this
14 matter under Arizona law.

15 Under Arizona law, the court must order arbitration
16 unless any legal or equitable grounds exist to invalidate the
17 arbitration provision contained in the contracts. A.R.S. §12-
18 1501; U.S. Insulation, Inc. v. Hilro Construction Co., 705
19 P.2d 490, 493 (Ariz. Ct. App. 1985); Holm Development, 795
20 P.2d at 1311. Such grounds may include fraud, lack of
21 capacity, or violation of public purpose. Holm Development,
22 795 P.2d at 1311; U.S. Insulation, 705 P.2d at 493. In
23 addition, adhesion contracts (form contracts presented on a
24 take-it or leave-it basis) are invalid if they are
25 unconscionable or if they do not conform to the weaker party's
26 reasonable expectations. Broemmer v. Abortion Serv. of

1 Phoenix, 840 P.2d 1013, 1016 (Ariz. 1992); Maxwell v.
2 Financial Services, Inc., 907 P.2d 51, 57 (Ariz. 1995) (citing
3 Broemmer and reviewing the grounds for invalidating a
4 contract). The validity of the arbitration agreement is the
5 focus of the initial inquiry, rather than the underlying
6 contract. Holm Development, 795 P.2d at 1313; U.S.
7 Insulation, 705 P.2d at 493-94.

8 In the present case the Plaintiffs speak little, if any,
9 English. The contracts were written entirely in English, and
10 contain a rather inconspicuous arbitration clause. The clause
11 is on page eight of a nine page document, in the second to
12 last numbered paragraph of a confusing document, in ordinary
13 print (only the word arbitration is underlined). The only
14 evidence to establish that the Plaintiffs "understood" what
15 they were signing is the presence of their initials next to a
16 simplistic check sheet also written in English. The
17 Plaintiffs claim that they had no notice of the arbitration
18 clause, and the checklist certainly does not suggest
19 differently. The list is not in a language native to either
20 Plaintiff. Asserting that the initials on the form offer any
21 more than the signatures on the contracts stretches
22 credulity.²

23 In addition, the contracts provide that every subscriber
24

25 ²Had the checklist been written in Spanish it would change
26 the facts significantly. However, as things stand the list is no
more reliable than the tucked-away clause in the contract itself.