

ARBITRATION – COMPELLING ARBITRATION: ORDERS
COMPELLING ARBITRATION AND DISMISSING
UNDERLYING ACTION ARE APPEALABLE AND WHETHER
OR NOT A CONTRACT WAS FORMED IS NECESSARY

Melaas v. Diamond Resorts U.S. Collection Dev., LLC, 2021 ND 1, 953
N.W.2d 623.

ABSTRACT

In *Melaas v. Diamond Resorts U.S. Collection Dev., LLC*, the North Dakota Supreme Court issued an opinion on matters of first impression impacting the ability to appeal from an order compelling arbitration and dismissing the underlying action. In *Melaas*, Kathleen Melaas met with a Diamond Resorts representative to discuss timeshare packages. The meeting lasted five hours, despite Melaas requesting to leave numerous times. Diamond Resorts did not let Melaas leave until she signed the timeshare agreement. Melaas was a vulnerable adult due to her diabetes leading her to experience fatigue and confusion during this long meeting. Melaas asserted she lacked the capacity to enter into the agreement. Additionally, she argued Diamond Resorts used high-pressure, abusive sales tactics and its knowledge of her medical condition to unduly influence and coerce her into signing the agreement. Last, she said her consent was obtained by duress and menace. Melaas sued Diamond Resorts and requested the district court declare her timeshare agreement with Diamond Resorts to be invalid and not binding. Diamond Resorts moved to compel arbitration and dismiss the complaint because the agreement requires arbitration of any and all claims stemming from the contract. Melaas opposed the motion, arguing the agreement and its arbitration clause are unenforceable due to being obtained by undue influence. The district court granted Diamond Resorts' motion to compel arbitration and dismissed Melaas' complaint. On appeal, the North Dakota Supreme Court reversed and *held* an order compelling arbitration and dismissing the underlying action is appealable, which overruled previous case law. The court also *held* the court must decide whether a contract was formed before ordering arbitration if a party challenges the existence of the contract containing the arbitration agreement by alleging she lacked the capacity to consent. The court examined case law and statutes from other jurisdictions, finding they were persuasive in deciding the issues of first impression. *Melaas* provides guidance to North Dakota practitioners about the opportunity to appeal motions to compel arbitration and dismiss the underlying action.

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|--|-----|
| I. FACTS..... | 150 |
| II. LEGAL BACKGROUND..... | 151 |
| A. APPEALABILITY OF ORDERS COMPELLING ARBITRATION..... | 151 |
| B. CAPACITY TO CONSENT TO A CONTRACT..... | 152 |
| III. ANALYSIS..... | 154 |
| A. ORDERS COMPELLING ARBITRATION ARE FINAL DECISIONS | 155 |
| B. FORMATION OF A CONTRACT..... | 155 |
| IV. IMPACT..... | 156 |
| V. CONCLUSION..... | 158 |

I. FACTS

Kathleen Melaas appealed from a district court order granting a motion to compel arbitration and dismissing her complaint against Diamond Resorts U.S. Collection Development, LLC (“Diamond Resorts”).¹ In August 2019, Melaas sued Diamond Resorts for undue influence, lack of capacity to consent, and unlawful practices and asked the district court to find the timeshare agreement she entered with Diamond Resorts invalid.²

Melaas met with a Diamond Resorts sales representative to discuss vacation and timeshare packages.³ She claimed the sales meeting lasted for five hours and Diamond Resorts refused to let her leave, even though they “knew she was a diabetic and suffered fatigue and confusion[.]”⁴ Melaas asked to leave the meeting at least once and Diamond Resorts ignored her request until after the timeshare agreement was signed.⁵

Melaas asserted the agreement was invalid because “she lacked the capacity to enter into the agreement” and “Diamond Resorts used high-pressure and abusive sales tactics and knowledge of her medical condition to unduly influence and coerce her into signing the agreement[.]”⁶ Melaas asserted any purported consent was obtained through menace and duress.⁷

1. Melaas v. Diamond Resorts U.S. Collection Dev., LLC, 2021 ND 1, 953 N.W.2d 623.

2. *Id.* ¶ 2.

3. *Id.*

4. *Id.*

5. *Id.*

6. *Id.*

7. *Id.*

Diamond Resorts moved to compel arbitration and dismiss the complaint or alternatively stay proceedings.⁸ They claimed the agreement required arbitration of all claims coming from the contract.⁹ Further, Diamond Resorts said the arbitration provision was valid, the agreement requires arbitration of all claims in Nevada, arbitration should be ordered, and the action should be dismissed.¹⁰ The district court granted Diamond Resorts' motion to compel arbitration and Melaas' complaint was dismissed.¹¹ On appeal, the North Dakota Supreme Court concluded the district court erred by ordering arbitration without deciding Melaas' capacity to consent challenge to the formation of the contract first.¹² The district court's order of dismissal and order compelling arbitration were reversed and remanded.¹³

II. LEGAL BACKGROUND

Writing for the court, Justice McEvers discussed areas of concern when addressing issues concerning arbitration provisions stemming from contractual agreements.¹⁴ She addressed four issues: 1) whether an order compelling arbitration is immediately appealable, 2) if the court must decide whether a contract was formed prior to ordering arbitration when a party challenges existence of the contract due to lack of capacity to consent, 3) the court's pre-requisite evidentiary requirements to ordering arbitration, and 4) whether challenges to the validity of an agreement should be decided by an arbitrator.¹⁵ Relevant portions of the Federal Arbitration Act ("FAA") were also discussed, specifically that an appeal may be taken from a final decision with respect to an arbitration.¹⁶

A. APPEALABILITY OF ORDERS COMPELLING ARBITRATION

Many states adopted either the Uniform Arbitration Act ("UAA") or the Revised Uniform Arbitration Act.¹⁷ The North Dakota Legislature adopted the UAA in 1987 and recodified it in the North Dakota Century Code in 2003.¹⁸ Section 32-29.3-28(1), in relevant part, authorizes appeals in arbitration cases, but does not "explicitly authorize an appeal from an order granting

8. *Id.* ¶ 3.

9. *Id.*

10. *Id.*

11. *Id.* ¶ 4.

12. *Id.* ¶ 1.

13. *Id.* ¶ 41.

14. *Id.* ¶ 15.

15. *Id.* ¶¶ 8, 21, 29.

16. *Id.* ¶ 7.

17. *Id.* ¶ 6.

18. *Id.*

a motion to compel arbitration” and dismissing the action.¹⁹ The North Dakota Supreme Court addressed the appealability of an order compelling arbitration in *Superpumper Inc. v. Nerland Oil, Inc.*²⁰ The court said orders compelling arbitration are not listed as appealable under the UAA and jurisdictions that adopted the uniform act are divided about whether the orders are appealable.²¹ The Court acknowledged that some jurisdictions have held orders compelling arbitration are appealable as a final order.²²

Melaas argued that *Superpumper* changed the FAA’s appealability so the order in this case should be appealable.²³ Recently, the United States Supreme Court held an order compelling arbitration and dismissing a party’s underlying claims is appealable because it is a “final decision with respect to an arbitration.”²⁴ The United States Supreme Court explained an order compelling arbitration and dismissing a party’s underlying claims disposes of the entire case on the merits, which is consistent with the interpretation of a “final decision.”²⁵

The North Dakota Supreme Court next considered how other states have handled this issue.²⁶ The court agreed with the analysis of many state courts.²⁷ The court wished “to remain consistent with other states that have adopted the uniform act” and concluded “an appeal from an order compelling arbitration and dismissing the underlying action is appealable.”²⁸ Therefore, the court overruled *Superpumper* to the extent it conflicted with their decision in Melaas’ case.²⁹

B. CAPACITY TO CONSENT TO A CONTRACT

Next, a discussion of the capacity to consent to a contract is relevant. Melaas argued the timeshare agreement, including the arbitration agreement and forum selection clauses, were unenforceable because she lacked the ability to consent, and her consent was obtained through undue influence, duress, menace, or fraud by Diamond Resort.³⁰ Melaas also contended “the court was required to decide whether a valid contract existed before it could compel

19. *Id.* ¶ 7 (citing N.D. CENT. CODE 32-29.3-28(1)).

20. 1998 ND 144, 582 N.W.2d 647.

21. *Id.*; *Melaas*, 2021 ND 1, ¶ 8, 953 N.W.2d 623.

22. *Id.*

23. *Id.* ¶ 9.

24. *Id.* ¶ 10 (citing *Green Tree Fin. Corp.-Ala. v. Randolph*, 531 U.S. 79, 86 (2000); *Lamps Plus, Inc. v. Varela*, 139 S.Ct. 1407, 1414 (2019)).

25. *Id.* (citing *Green Tree*, 531 U.S. at 86).

26. *Id.* ¶ 12.

27. *Id.* ¶ 13.

28. *Id.*

29. *Id.*

30. *Id.* ¶ 19.

arbitration.”³¹ Previously, the North Dakota Supreme Court “considered whether a challenge to the validity of a contract should be determined by the court or the arbitrator under . . . the UAA.”³² In *26th St. Hosp., LLP v. Real Builders, Inc.*,³³ the court identified two types of validity challenges.³⁴ The first type challenges the validity of the agreement to arbitrate and the second type challenges the validity of the contract.³⁵ However, in the court’s analysis of whether an arbitration agreement is enforceable, only the first type, a challenge to the validity of the agreement to arbitrate, is relevant.³⁶ “An arbitration agreement is severable from the remainder of the contract, and therefore a party’s challenge to the contract as a whole does not prevent a court from enforcing a specific agreement to arbitrate.”³⁷

The United States Supreme Court also addressed this issue.³⁸ “The [United States Supreme Court] said courts should order arbitration of a dispute only where the court is satisfied neither the formation of the arbitration agreement nor its enforceability or applicability to the dispute is in issue, and if either is in issue then the court must resolve the disagreement.”³⁹

The federal appeals courts that have discussed a capacity to contract challenge disagree on whether a court or an arbitrator is required to determine the existence of a contract.⁴⁰ However, “[s]tate courts that have decided the issue have generally held a party’s capacity to consent to a contract and therefore whether a contract was ever formed is an issue for the court to decide.”⁴¹

When a party moves to compel arbitration, the district court must look for an arbitration agreement that requires arbitration of the dispute.⁴² “If there is an arbitration agreement applicable to the dispute, the court must then decide any challenges to the making of the arbitration agreement[.]”⁴³ Then the court is to decide “any challenges to the validity of the arbitration agreement itself and any claims that the contract containing the arbitration agreement

31. *Id.*

32. *Id.* ¶ 20.

33. 2016 ND 95, 879 N.W.2d 437.

34. *Id.* ¶ 17.

35. *Melaas*, 2021 ND 1, ¶ 20, 953 N.W.2d 62 (citing *Real Builders*, 2016 ND 95, ¶ 12, 879 N.W.2d 437).

36. *Id.*

37. *Id.*

38. *Id.* ¶ 21.

39. *Id.* ¶ 23 (citing *Granite Rock Co. v. Int’l Bhd. Of Teamsters*, 561 U.S. 287, 296, 130 S.Ct. 2847, 177 L.Ed.2d 567 (2010)).

40. *Id.* ¶ 24.

41. *Id.* ¶ 26.

42. *Id.* ¶ 29.

43. *Id.*

was never formed because one party did not have the capacity to consent to the agreement.”⁴⁴

The court decided “[b]ecause Melaas claimed she lacked the capacity to consent to the timeshare agreement at the time it was executed, and provided an affidavit supporting her argument . . . the district court erred in ordering arbitration without holding an evidentiary hearing and deciding whether a contract exists.”⁴⁵ “However, Melaas’ claims about fraud, duress, menace, and undue influence are arguments about the validity of the entire contract, which . . . do not challenge the existence of the contract.”⁴⁶ “[T]hese claims challenge the validity of the entire timeshare agreement and do not challenge the validity of the arbitration agreement itself, [therefore] they are issues for the arbitrator to decide if the district court determines that a contract exists and arbitration is appropriate.”⁴⁷ Here, the court concluded the district court erred because it did not decide whether a contract containing an arbitration agreement was formed before granting the motion to compel arbitration.⁴⁸

Next, the court addressed the forum selection clause, an issue separate from arbitration.⁴⁹ A forum selection clause’s application provides separate grounds for dismissal which can be argued in a motion to dismiss for improper venue, which Diamond Resorts did not do here.⁵⁰ The court ordered “[o]n remand, if any of the parties argue the case must be dismissed under the forum selection clause, the district court must first determine whether a contract exists.”⁵¹ A court may consider the forum selection clause issue if a contract is determined to exist.⁵²

III. ANALYSIS

The court unanimously held an order compelling arbitration and dismissing the underlying action is appealable, overruling *Superpumper*.⁵³ It also held before ordering arbitration, a court must decide whether a contract was formed requiring arbitration if a party alleged lack of capacity to consent.⁵⁴

44. *Id.*

45. *Id.* ¶ 30.

46. *Id.* ¶ 31 (citing *Real Builders*, 2016 ND 95, ¶¶ 17-19, 879 N.W.2d 437).

47. *Id.*

48. *Id.* ¶ 32.

49. *Id.* ¶ 38.

50. *Id.*

51. *Id.* ¶ 40.

52. *Id.*

53. *Id.* ¶¶ 41-42.

54. *Id.* ¶ 40.

A. ORDERS COMPELLING ARBITRATION ARE FINAL DECISIONS

The court's reasoning in holding an order compelling arbitration and dismissing the underlying action is appealable was based on the premise that the dismissal is a "final decision with respect to arbitration."⁵⁵ "[A]n order compelling arbitration and dismissing a party's underlying claims disposes of the entire case on the merits and leaves no part of it pending before the court, which is consistent with the longstanding interpretation of a 'final decision.'"⁵⁶ "[A]n order compelling arbitration [] disposes of all the issues before the trial court or orders the entire controversy to be arbitrated is a final decision . . . " which is appealable because of the way it dismisses of an action entirely.⁵⁷ The court agreed with many similar holdings among state courts that considered this issue in recent years.⁵⁸ Therefore, the holding in *Superpumper* is overturned as it relates to the appealability of orders compelling arbitration and dismissing the underlying action.⁵⁹

B. FORMATION OF A CONTRACT

Whether a contract has been formed is important to consider. The court held, on a motion to compel arbitration, it must decide whether a contract was formed before ordering arbitration if a party challenges the existence of a contract containing an arbitration agreement by alleging lack of capacity to consent.⁶⁰ The court reasoned, while taking case law from other states into account, that when a party moves to compel arbitration, the district court must first determine if there is a valid arbitration agreement requiring arbitration of the dispute between the parties.⁶¹ If there is an arbitration agreement applicable to the dispute, the court must then decide any challenges to the making of the agreement, including any validity challenges and any claims that the contract containing the arbitration agreement was never formed because one party did not have the capacity to consent to the agreement.⁶² After resolving any challenges to the making of the arbitration agreement, the court must order arbitration if the court has determined a valid arbitration agreement exists requiring arbitration of the dispute.⁶³ Here, Melaas claimed she could not enter into the timeshare agreement because she could not form the

55. *Id.* ¶ 10 (citing 9 U.S.C. § 16(a)(3)).

56. *Id.*

57. *Id.* ¶ 12.

58. *Id.*

59. *Id.* ¶ 13.

60. *Id.*

61. *Id.* ¶ 29.

62. *Id.*

63. *Id.*

required consent.⁶⁴ “She alleged she ha[d] multiple medical conditions, which impacted her decision making capabilities[.]”⁶⁵ Her daughter “filed an affidavit in support of Melaas’ argument that she did not have capacity to consent to the timeshare agreement.”⁶⁶

Here, the North Dakota Supreme Court held the district court erred in ordering arbitration without holding an evidentiary hearing and deciding whether a contract existed.⁶⁷ It reasoned “Melaas claimed she lacked the capacity to consent to the timeshare agreement at the time it was executed and provided an affidavit supporting her argument.”⁶⁸ Therefore, the North Dakota Supreme Court concluded the district court erred by granting Diamond Resorts’ motion to compel arbitration before deciding whether a contract containing an arbitration agreement was formed.⁶⁹ On remand the North Dakota Supreme Court ordered the district court to an evidentiary hearing and decide whether a contract containing an arbitration agreement exists.⁷⁰

IV. IMPACT

As discussed, *Melaas* overturned the precedent established in *Superpumper*, therefore this case impacted North Dakota practitioners. *Melaas* overruled *Superpumper* to the extent it dealt with the appealability of an order compelling arbitration and dismissing the underlying action.⁷¹ Prior to *Melaas*, an order compelling arbitration and dismissing the underlying action was not appealable.⁷² *Melaas* changed prior case law to remain consistent with other states that have adopted the uniform act.⁷³ North Dakota practitioners will need to familiarize themselves with the holdings in *Melaas* to effectively represent their clients, specifically those dealing with issues relating to compelling arbitration through arbitration agreements. With the increased usage of arbitration agreements, North Dakota practitioners could be seeing this issue more often.

The issue of compelling arbitration has come up in many instances across many different states.⁷⁴ Whether the state has adopted the Uniform Arbitration Act or the Revised Uniform Arbitration Act impacts how states

64. *Id.* ¶ 30.

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.*

69. *Id.* ¶ 32.

70. *Id.*

71. *Id.* ¶ 13.

72. *Id.* ¶ 8.

73. *Id.* ¶ 13.

74. *See id.* ¶¶ 6, 12.

decipher issues regarding compelling arbitration.⁷⁵ North Dakota adopted the Uniform Arbitration Act in 1987 and recodified it in the Century Code in 2003.⁷⁶ The Uniform Arbitration Act does not “explicitly authorize an appeal from an order granting a motion to compel arbitration and dismissing the action.”⁷⁷ As mentioned previously in this article, the North Dakota Supreme Court first addressed the appealability of an order compelling arbitration in *Superpumper*, where the court decided “orders compelling arbitration are not listed as appealable under the [Uniform Arbitration Act].”⁷⁸ The court noted “jurisdictions that adopted the uniform act are divided about whether [such] orders are appealable.”⁷⁹ When overruling the decision in *Superpumper*, the court was “persuaded by the wisdom of the decisions interpreting and applying the procedural requirements of the [uniform act] in deciding whether an order compelling arbitration is appealable.”⁸⁰

The North Dakota Supreme Court’s decision was also “guided by the federal courts’ interpretation of similar appealability provisions.”⁸¹ In *Lamps*, “the Supreme Court held an order compelling arbitration and dismissing a party’s underlying claims is appealable” because it is a “final decision with respect to arbitration.”⁸² “The court explained an order compelling arbitration and dismissing a party’s underlying claims disposes of the entire case on the merits . . . which is consistent with the longstanding interpretation of a ‘final decision.’”⁸³ The court noted “the order compelling arbitration would not have been appealable if the district court had entered a stay instead of dismissing the underlying action.”⁸⁴

State courts have also “considered this issue in recent years [most holding] a party may appeal from an order compelling arbitration and dismissing the underlying action.”⁸⁵ In *Kottschade*, the court held an “order compelling arbitration and dismissing the case was appealable as an appeal from a final judgment under state rules of civil appellate procedure.”⁸⁶ Similarly in *Sawyers*, the court held “an order compelling arbitration which disposes of all the

75. *See id.*

76. *Id.* ¶ 6.

77. *Id.* ¶ 8.

78. *Id.*

79. *Id.*

80. *Superpumper, Inc. v. Nerland Oil, Inc.*, 1998 ND 144, ¶ 17, 582 N.W.2d 647.

81. *Melaas v. Diamond Resorts U.S. Collection Dev., LLC*, 2021 ND 1, ¶ 9, 953 N.W.2d 625.

82. *Id.* ¶ 10 (citing *Green Tree Fin. Corp.-Alabama v. Randolph*, 531 U.S. 79, 86 (2000)).

83. *Id.* (citing *Green Tree*, 531 U.S. at 86).

84. *Id.*

85. *Id.* ¶ 12.

86. *Id.* (citing *City of Rochester v. Kottschade*, 896 N.W.2d 541, 547-58 (Minn. 2017)).

issues before the trial court or orders the entire controversy to be arbitrated is a final decision and is immediately appealable.”⁸⁷

Understanding how the North Dakota Supreme Court came to its decision in *Melaas* is important and impactful because it shows the reasoning that went into the decision of overturning prior caselaw in *Superpumper*. The court’s analysis and discussion of caselaw in other states shows how it came to its decision in *Melaas*. It is important for practitioners to understand this analysis and the impact this case could have on other courts that do not allow orders compelling arbitration to be appealed in the future. *Melaas* creates persuasive authority on the appealability of arbitration orders. Other courts may be influenced by North Dakota caselaw to reconsider the appealability of arbitration orders.

It is also important for legal practitioners to understand the court’s reasoning as to why they held a court must first decide whether a contract was formed if a party challenges the existence of a contract containing an arbitration agreement by alleging lack of capacity to consent. The court looked at how other courts have analyzed this issue.⁸⁸ It is the opinion of many state courts that a party’s capacity to consent to a contract and whether a contract was ever formed is a decision for the court.⁸⁹ Other types of challenges to the formation or existence of a contract, and not the contract’s validity, are also decisions for the court before arbitration can be ordered.⁹⁰ The North Dakota Supreme Court found these arguments to be persuasive, holding “the court must decide whether a contract was formed before ordering arbitration if a party challenges the existence of the contract containing the arbitration agreement by alleging she lacked the capacity to consent.”⁹¹ North Dakota practitioners should keep this analysis in mind when they deal with cases regarding contracts containing arbitration agreements.

V. CONCLUSION

In *Melaas*, the North Dakota Supreme Court held orders compelling arbitration and dismissing the underlying action are appealable and courts must decide whether a contract was formed before ordering arbitration if a party challenges the existence of a contract containing an arbitration agreement by alleging a lack of capacity to consent.⁹² *Melaas* was a case of first impression and overruled precedent set by *Superpumper*.⁹³ North Dakota citizens and

87. *Id.* (citing *Sawyers v. Herrin-Gear Chevrolet Co., Inc.*, 26 So.3d 1026, 1034 (Miss. 2010)).

88. *Id.* ¶ 26.

89. *Id.*

90. *Id.* ¶ 27.

91. *Id.* ¶ 28.

92. *Id.* ¶ 13.

93. *Id.*

practitioners should be aware of the impact *Melaas* has on future cases dealing with compelling arbitration.

Rainey Selvig*

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