RECENT DEVELOPMENTS

ARBITRATION

COURT FINDS EARNEST MONEY CONTRACT LANGUAGE IS NOT SUFFICIENTLY "EXPRESS, PLAIN, CLEAR, AND CERTAIN" TO EVINCE THE AGREEMENT OF THE PARTIES TO DELEGATE TO ARBITRATORS THE POWER TO DECIDE DISPUTES BETWEEN THEM

Bates v. MTH Homes-Texas, L.P., ____ S.W.2d ____ (Tex.App.-Houston [1st Dist.] 2005).

FACTS: On January 26, 2004, Bates filed suit against Hammonds because of defects sustained during the construction of Bates' new home. On September 9, 2004, Hammonds filed a motion to compel arbitration based on a clause in an earnest-money contract addendum. On September 28, 2004, the trial court granted the motion to compel. Bates filed a petition for writ of mandamus complaining of the trial court's order.
HOLDING: Writ conditionally granted.
REASONING: When a trial court erroneously grants a party's motion to compel arbitration, the movant has no adequate remedy at law and is entitled to a writ of mandamus. *In re Am. Homestar of Lancaster, Inc.*, 50 S.W.3d 480, 483 (Tex. 2001). A trial court abuses its discretion when it errs in determining what the law is or in applying the law to the facts. *In re Masonite Corp.*, 997 S.W.2d 194, 197 (Tex. 1999). A party cannot be required to arbitrate unless it has agreed to do so and the parties' agreement to arbitrate must be clear. *Trico Marine Servs. V. Stewart & Stevenson Technical Servs. Inc.*, 73 S.W.3d 545, 548 (Tex.App.- Houston [1st Dist.] 2002). The Court may not expand upon the terms of a contract or tolerate a liberal interpretation of it by reading into it a voluntary, consensual agreement to arbitrate when one otherwise does not exist. *Seale v. Roy M. Mitchell Contracting Co.*, 321 S.W.2d 149, 151 (Tex.Civ.App. - Austin 1959). Under both the Texas Arbitration Act (TAA) and the Federal Arbitration Act (FAA), a party seeking to compel arbitration has the initial burden to establish the arbitration agreement's existence and to show that the claims asserted fall within the agreement's scope. *In re Kellogg Brown & Root*, 80 S.W.3d 611, 615 (Tex.App. - Houston [1st Dist.] 2002).

In its motion to compel arbitration, Hammonds relied on the following clause of the earnest money contract addendum to show the parties' intent to arbitrate:

> This contract is subject to Chapter 27 of the Texas property code. The provisions of that chapter may affect the purchaser's right to recover damages arising from the performance of this contract. If purchaser has a complaint concerning a construction defect arising from the performance of this contract and that defect has not been corrected through normal warranty service, the purchaser must provide notice regarding the defect to the builder by certified mail, return receipt requested, not later than the 60th day before the date the purchaser initiates a claim to recover damages in an arbitration proceeding. The notice must refer to chapter 27 of the Texas property code, and must describe the construction defect. If requested by the builder, the purchaser must provide the builder an opportunity to inspect and cure the defect as provided by Section 27.004 of the Texas Property Code.

Hammonds argued that this clause showed that the parties intended to waive the right to a trial and instead to resolve any disputes through binding arbitration. Hammonds contended that if the parties had intended something other than arbitration, they would have used language such as "court of law" instead of "arbitration proceeding."
The language in this clause is not sufficiently clear to show agreement that arbitration was agreed on between the parties. The clause in the earnest money contract addendum on which Hammonds relied is not a traditional arbitration clause, but rather is similar to the statutorily mandated disclosure statement in Section 27.007 of the Texas Property Code. The clause in the earnest money contract addendum referred to arbitration, but did not limit the parties' rights to arbitration only. The clause, a statutorily required disclosure statement, provided the notice procedures to follow if a party sought damages in an arbitration proceeding. The clause on which Hammonds relied is not sufficient to constitute an agreement to arbitrate because it does not clearly indicate intent to arbitrate. The parties thus did not expressly agree in writing in the clause to submit the dispute to arbitration.

ARBITRATION AGREEMENTS DO NOT HAVE TO BE SIGNED TO BE ENFORCEABLE IF THERE IS AN AGREEMENT TO ARBITRATE

ARBITRATION CLAUSE IS NOT UNCONSCIONABLE BECAUSE IT LACKED MUTUALITY

ADHESION CONTRACTS ARE NOT AUTOMATICALLY UNCONSCIONABLE

In re Advance PCS Health L.P., ____ S.W.3d ____ (Tex. 2005).

FACTS: Several pharmacies filed suit asserting that a pharmacy benefits management company had underpaid them for a decade. The management company submitted affidavits establishing that the pharmacies who joined its network received an enrollment package that contained a Provider Agreement and membership and network enrollments forms. Only the Provider Agreement contained an arbitration clause, and only the membership and network enrollment forms were signed by the pharmacies. The management company moved for arbitration under the Federal Arbitration Act ("FAA") after the suit was filed. The trial court denied the management company's motion to compel arbitration under the FAA. The court of appeals summarily denied mandamus relief.
HOLDING: Conditionally granted the writ of mandamus.
REASONING: The pharmacies contended that because they only signed the membership and network enrollment forms and not the Provider Agreement, which contained the arbitration

clause, then the arbitration clause was not valid. Neither the FAA nor Texas law requires that arbitration clauses be signed, so long as they are written and agreed to by the parties. 9 U.S.C. § 3; Tex. Civ. Prac. & Rem. Code § 171.001(a). Additionally, an arbitration agreement does not have to be included in each of the contract documents it purports to cover. *See In re Halliburton Co.,* 80 S.W.3d 566, 569 (Tex. 2002). The enrollment forms that the pharmacies signed explicitly referenced and agreed to the terms of the Provider Agreement. Therefore, the Court reasoned, so long as the parties agreed to arbitrate this dispute, it did not matter which document included that agreement.

The pharmacies also argued that the arbitration clause was substantively unconscionable because it lacked mutuality, and procedurally unconscionable because the pharmacies were forced to accept it. The court held that adhesion contracts are not automatically unconscionable, and there is nothing per se unconscionable about arbitration agreements. Under the FAA, an unequal bargaining power does not establish grounds for defeating an agreement to arbitrate absent a well-supported claim that the clause resulted from the sort of fraud or overwhelming economic power that would provide grounds for revocation of any contract. *Gilmer v. Interstate/Johnson Lane Corp.,* 500 U.S. 20, 33, 111 S.Ct. 1647, 114 L.Ed.2d 26 (1991). The pharmacies contended that the arbitration clause was disclosed only after they had joined network. A representative of the de la Rosa Pharmacy testified that the management company sent the Provider Agreement to him only after he had signed and returned the enrollment forms. The Court explained that since de la Rosa signed several of the enrollment forms seriatim; having received the Provider Agreement after the first, he was on notice of its terms for all the rest. Furthermore, nobody else testified that the Provider Agreement came only after they had joined, including several other employees and agents who often signed for the de la Rosa Pharmacy. Because neither affidavits nor testimony showed that any pharmacy joined the network without an opportunity to read the Provider Agreement, the Court held that the pharmacies did not carry their evidentiary burden.

NON-SIGNATORY BOUND BY ARBITRATION CLAUSE ONLY IF IT SEEKS TO DERIVE A DIRECT BENEFIT FROM THE CONTRACT CONTAINING THE ARBITRATION PROVISION

In re Kellogg Brown & Root, Inc., 166 S.W.3d 732 (Tex. 2005).

FACTS: In October 1999, MacGregor USA, Inc. ("MacGregor") contracted with Ingalls Shipbuilding, Inc. ("Ingalls") to build elevator trunks for two cruise ships. MacGregor assigned the contract to its sister company, Macgregor FIN. In August 2000, MacGregor subcontracted part of the job to Unidynamics, which agreed to produce a set of the elevator trunks for one of the ships. In June 2001, Unidynamics and KBR entered into a second tier subcontract, under which KBR agreed to furnish labor, equipment, and facilities to produce the elevator trunks. In the fabrication subcontract between MacGregor and Unidynamics, the parties agreed that "[a]ny disputes arising from the interpretation or application of [the] contract including any document pertaining thereto, shall be settled by arbitration in accordance with General Conditions." The second tier subcontract between Unidynamics and KBR did not contain an arbitration provision. After the ship buyer declared bankruptcy in November 2001, Ingalls directed MacGregor to cease work and notify its subcontractors to do the same. MacGregor directed Unidynamics to comply with "the same instructions that Ingalls gave MacGregor." Unidynamics conveyed those instructions to KBR. On or around November 5, 2001, KBR ceased work, stored the elevator trunks and other equipment, and sent Unidynamics invoices for unpaid fabrication services and storage costs. Because KBR had not been paid in full, it asserted liens on the elevator trunk fabrications, parts, and other materials ("the collateral").

KBR brought action against Unidynamics and MacGregor to recover damages on breach of contract and quantum meruit theories and requested a declaratory judgment on ownership of collateral and liens. MacGregor moved to abate suit or compel KBR to join arbitration with Unidynamics despite KBR's status as non-signatory. The district court denied the motion. The contractor appealed and sought writ of mandamus. The appeals court conditionally granted writ and ordered trial court to issue order compelling second tier subcontractor to arbitrate. The second tier subcontractor then petitioned for writ of mandamus.

HOLDING: Relief conditionally granted.

REASONING: MacGregor asserted that KBR was bound to arbitrate under the doctrine of "direct benefits estopppel", a type of equitable estoppel applied in the arbitration context. Under direct benefits estoppel, a non signatory plaintiff seeking the benefits of a contract is estopped from simultaneously attempting to avoid the contract's burdens, such as the obligation to arbitrate disputes. *R.J. Griffin & Co. v. Beach Club II Homeowners Ass'n*, 384 F.3d 157, 160 (4th Cir. 2004). A party may be estopped from asserting that the lack of his signature precludes enforcement of the contract's arbitration clause when he has consistently maintained that other provisions of the same contract should be enforced to benefit him. *Thomson-CSF, S.A. v. Am. Arbitration Ass'n*, 64 F.3d 773, 776 (2d Cir. 1995). Thus, a non signatory plaintiff may be compelled to arbitrate if it seeks to enforce terms of a contract containing an arbitration provision. Consistent with the federal doctrine of direct benefits estoppel, the Texas Supreme Court had previously held that a non signatory plaintiff may be compelled to arbitrate if its claims are based on a contract containing an agreement to arbitrate. *In re FirstMerit Bank*, 52 S.W.3d at 753, 753 (Tex. 2001). The court considered the issue as whether KBR sought to enforce terms of the contract based on quantum meruit or was seeking a declaration that it possessed valid liens.

A non signatory plaintiff may be compelled to arbitrate if it seeks to enforce terms of a contract containing an arbitration provision.

To advance its estoppel theory, MacGregor contended that KBR's quantum meruit claim was based on the fabrication subcontract in the sense that KBR's labor and services were linked to the subcontract. KBR was fabricating trunks that were at the contract's core, and, in performing the work, KBR relied on the

fabrication subcontract's specifications. However, under direct benefits estoppel, a non signatory plaintiff cannot be compelled to arbitrate on the sole ground that, but for the contract containing the arbitration provision, it would have no basis to sue. The work to be performed under a second tier subcontract will inherently be related to and defined by contracts higher in the chain. Thus, a non signatory should be compelled to arbitrate a claim only if it seeks, through the claim, to derive a direct benefit form the contract containing the arbitration provision.

In its quantum meruit claim against MacGregor, KBR sought payment for services rendered. KBR provided services pursuant to its contract with Unidynamics. KBR's asserted right to payment stems directly from the KBR Unidynamics contract, not the fabrication subcontract. The fabrication subcontract included no provision for paying KBR and it precluded KBR from asserting rights under that contract, which expressly provided that "approved use of any subcontractor creates no contractual relationship between the subcontractor and MacGregror. The court found that the court of appeals abused its discretion in compelling KBR to arbitrate its quantum meruit claim against MacGregor. With respect to KBR's lien validity claims, MacGregor's sole argument for compelling arbitration was that the claims required a determination of ownership, and thus, they were based on the Title Agreement within the fabrication subcontract. When the arbitration award resolved the ownership dispute, it eliminated the only rationale that MacGregor asserts for arbitrating the liens' validity. There may have been other arguments to compel KBR to arbitrate the validity of its liens but the court deferred those matters to the trial court.

MISCELLANEOUS

STATE LAWS PROHIBITING DIRECT PURCHASE OF WINE FROM OUT-OF-STATE VINEYARDS VIOLATE COMMERCE CLAUSE

Granholm v. Heald, 125 S. Ct. 1885 (2005).

FACTS: In Michigan, in-state wineries were allowed to ship their wine directly to consumers and by-pass the wholesaler, while out-of-state wineries must ship their wine to an in-state wholesaler to be distributed to the retailers and then to the consumers. An out-of-state winery and state residents brought action challenging Michigan laws governing distribution of alcohol as violative of the commerce clause, alleging that state thereby discriminated against out-of-state wineries by preventing them from shipping wine directly to Michigan consumers. The plaintiffs contended that this system of channeling was an unnecessary added cost of the wine for the end consumer. The United States District Court for the Eastern District of Michigan granted summary judgment in favor of the state and the Sixth Circuit reversed, finding violation of the dormant Commerce Clause.

States may not enact laws that burden out-of-state producers or shippers simply to give a competitive advantage to in-state businesses.

In New York, an out-of-state winery may ship directly to New York consumers only if it became a licensed New York winery. Proprietors of out-of-state wineries and in-state wine consumers brought action challenging constitutionality of New York State's laws governing direct shipment to in-state consumers of out-of-state wine. They also stated that this New York "branch" requirement also added unnecessary costs to the wine. The United States District Court for the Southern District of New York granted summary judgment in favor of the consumers and wine makers and the Second Circuit reversed, upholding the state's law.

The Supreme Court consolidated both cases and granted certiorari. Both cases involved states offering preferential treatment to in-state wineries and imposing additional costs on out-of-state wineries or a complete bar with regards to the distribution of wine to end consumers.

HOLDING: Affirmed as to judgment of the Sixth Circuit Court of Appeals; reversed and remanded as to judgment of the Second Circuit Court of Appeals.

REASONING: The court concluded that state laws violate the Commerce Clause if they mandate differential treatment of in-state and out-of-state economic interests that benefited the former and burden the latter. The court states that in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate 'differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.' The mere fact of non-residence should not foreclose a producer in one State from access to markets in other States. States may not enact laws that burden out-of-state producers or shippers simply to give a competitive advantage to in-state businesses.

The rule prohibiting state discrimination against interstate commerce follows from the principle that States should not be compelled to negotiate with each other regarding favored or disfavored status for their own citizens. States do not need, and may not attempt, to negotiate with other States regarding their mutual economic interests. Laws of this type deprive citizens of their right to have access to the markets of other States on equal terms. The Commerce Clause of the US Constitution was designed to avoid this type of discrimination.

LAWYER WHO FAILED TO EITHER INFORM A CLIENT THAT A SECURITY INTEREST USED AS COLLATERAL IN THE SALE OF A COMPANY NEEDED TO BE RENEWED OR RENEW IT HIMSELF MAY BE HELD LIABLE FOR LEGAL MALPRACTICE

Barnes v. Turner, 606 S.E.2d 849 (Ga. 2004).

FACTS: In late 1996, William Barnes Jr. sold his auto parts company, part of which was paid at closing, and the rest was