

Magnuson-Moss Warranty Act v. the Federal Arbitration Act

The Makings for a Battle

By Nathan White*

I. INTRODUCTION

In 1975 Congress passed the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act (“the Magnuson-Moss Act” or “the Act”)¹ to protect consumers from retailers and manufacturers that take advantage of consumers by placing misleading warranties on the products they sell. Although the Act gives consumers the right to enforce its provisions in state or federal court, under the Federal Arbitration Act (“FAA”) retailers and manufacturers can force consumers to submit to arguably unfair arbitration or other alternative dispute resolution methods. Typically, retailers and manufacturers slip binding arbitration clauses into warranty contracts, forcing consumers to sign the warranty contract in order to get the products they desire. Under these warranties, when a consumer purchases a defective product the consumer forfeits the right to sue in court for breach of warranty. Furthermore, the consumer must submit to arbitration set up by the warranty’s maker.

In arbitration, the warrantor usually chooses the arbitrator. If the arbitrators want repeat business, they have a huge incentive to provide favorable rulings for the warrantor. Consequently, arbitration may leave the consumer with an unfavorable ruling with no right to appeal.

This problem results from an imbalance in bargaining power between sellers and manufacturers on one hand and consumers on the other. Because retailers and manufacturers have more bargaining power than consumers the retailers and manufacturers force consumers to choose between two arguably unjust options. Either the consumer can enter into a contract with unfair terms or the consumer can refuse to enter into the contract and forgo the product it seeks. The FAA plays an integral part in making this scenario possible. This article examines the law as it relates to arbitration and warranties for consumer goods, focusing primarily on mobile homes.

II. MAGNUSON-MOSS ACT

A. Purpose

Congress enacted the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act of 1975 in response to merchants’ widespread misuse of express warranties and disclaimers.² Specifically, Congress passed the Act, “in order to improve the adequacy of information available to consumers, prevent deception, and improve competition in the marketing of consumer products.”³ The Act is based on the premise that suppliers of consumer goods vigorously use

written express warranties as advertising and merchandising devices.⁴ Congress chose to regulate these express warranties in order to protect consumers from abuse.

B. Who the Magnuson-Moss Act Applies To

The Magnuson-Moss Act applies to “warrantors” who are defined as “any supplier or other person who gives or offers to give a written warranty or who is or may be obligated under an implied warranty.”⁵ Essentially, anyone giving a consumer a warranty or anyone upon whom the law imposes an implied

warranty is defined as a warrantor.

C. What the Magnuson-Moss Act Does

The Magnuson-Moss Act primarily regulates written warranties. The Act sets out detailed requirements regarding disclosures, duties, and remedies associated with warranties on consumer products. The Act authorizes the Federal Trade Commission (“FTC”) to promulgate implementing rules⁶ and provides guidelines for the FTC to use in the adoption of those rules. The FTC has published many rules implementing the Act, including:

1. Rule 701, specifying the information that must appear in a written warranty on a consumer product;
2. Rule 702, detailing the obligations of sellers and warrantors to make warranty information available to consumers prior to purchase; and
3. Rule 703, specifying the minimum procedural standards for any internal dispute settlement mechanism ("IDSM"), which must be followed by any warrantor who wishes to incorporate an IDSM, through a prior resort requirement, into the terms of a written consumer product warranty.⁷

The rules go further (or are at least clearer) than the Act itself in protecting consumers from arbitration abuse by warrantors. The rules prohibit warrantors from representing in any warranty that the decision of the warrantor, service contractor, or any designated third party is binding or final in warranty disputes.⁸ Under the rules promulgated pursuant to the Magnuson-Moss Act, warrantors cannot force consumers to submit to binding arbitration. Thus, the Act and the FTC regulations implementing it undercut the pro-arbitration stance of the FAA.

However, the Magnuson-Moss Act does not apply to all warranties. The Act only governs warranties for consumer products.⁹ A "consumer product" is defined by the Act as "tangible personal property which is distributed in commerce and which is normally used for personal, family, or household purposes (including any such property intended to be attached to or installed in any real property without regard to whether it is so attached or installed)."¹⁰

D. Amount in Controversy

Federal courts have concurrent original jurisdiction along with state courts over disputes involving violations of the Magnuson-Moss Act.¹¹ In passing the Act, Congress attempted to protect consumers from unduly limited warranties. At the same time, Congress realized that it could not clog federal courts with small suits and that subjecting warrantors to increasing amounts of private litigation "does not represent an efficient or generally satisfactory

way to achieve proper performance under warranties."¹² To balance these interests, Congress built three key limitations into the Magnuson-Moss Act. First, to get into federal court the amount in controversy must be at least \$50,000, excluding interest and costs.¹³ Second, claims may be aggregated to establish federal jurisdiction if all individual claims are \$25 or more.¹⁴ Third, if the suit is brought as a class action, the Act requires at least 100 named plaintiffs.¹⁵ These limitations deny federal courts subject matter jurisdiction of potential suits in many cases while leaving the federal courts free to adjudicate relatively large warranty suits or class actions. Unfortunately, these limitations leave many consumers without any federal court protection.

E. Remedies

Finally, the Act provides that a consumer harmed by a warrantor or supplier's failure to comply with its provisions may recover damages.¹⁶ The consumer may also recover costs and expenses, including reasonable attorney's fees.¹⁷ The Act provides much needed standards for warrantors as well as remedies for wronged consumers.

III. FEDERAL ARBITRATION ACT

A. Purpose

Congress passed the FAA in order to promote arbitration as a speedy alternative to litigation as well as to reduce court docket loads. The FAA requires that where the parties to a contract have agreed to arbitration in writing, disputes relating to the contract must be submitted to binding arbitration.¹⁸ As a result, parties to a contract containing an arbitration clause will be compelled to submit to arbitration by a court of competent jurisdiction.

IV. INTERACTION BETWEEN MAGNUSON-MOSS AND THE FAA

On April 6, 2000, the Corpus Christi Court of Appeals decided a case that clarifies how the FAA and Magnuson-Moss Act interact in the context of mobile home warranties.¹⁹ The issue in the case was whether a warrantor could force a consumer into binding arbitration by including an arbitration clause in a

written warranty. Neither the Supreme Court of Texas nor the Fifth Circuit has considered this issue.

A. Facts

The Van Blarcums signed a retail installment contract security agreement in order to buy a mobile home from Nationwide Housing Systems, Inc. ("Nationwide"). The Van Blarcums also entered into an arbitration agreement ("the Agreement") with Nationwide. The Agreement stated that, "all claims or disputes arising out of the sale, purchase, or occupancy of the mobile home, including any claims under any warranties [would] be resolved by final and binding arbitration."²⁰ The Agreement also stated that it "inure[d]" to the benefit of the manufacturer and any lender providing financing for the purchase of the mobile home. At the time of purchase Nationwide provided the Van Blarcums with a retailer's written warranty. The Van Blarcums were also entitled to a second written warranty from the manufacturer, American Homestar of Lancaster, Inc. ("Homestar"), which they never received.

After the purchase, the Van Blarcums informed both Nationwide

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and Homestar of a number of defects in the mobile home's construction and installation. Nine months after the Van Blarcums made their first request for warranty repairs, they still had numerous problems with their mobile home. In January of 1998, the Van Blarcums filed suit in a county court at law. They sued Nationwide and Homestar ("Defendants") for breach of express and implied warranties and violations of the Texas Deceptive Trade Practices-Consumer Protection Act. The Van Blarcums sought damages and a stay of arbitration. In response, the Defendants filed a motion to compel binding arbitration. The Defendants argued

that the arbitration clause was enforceable under the Texas and Federal Arbitration Acts.²¹ The trial judge ordered the parties to arbitration. The Van Blarcums filed a motion for reconsideration, which the trial court denied after a hearing. After the denial, the Plaintiffs filed for a writ of mandamus,²² requesting the appellate court to direct the trial court to vacate its order compelling binding arbitration.

B. Reasoning

The court begins its analysis by discussing whether the FAA or Magnuson-Moss Act controls arbitration clauses in consumer goods warranties. The Van Blarcums argue “the trial court abused its discretion in compelling arbitration because under the Magnuson-Moss Act, a consumer cannot be compelled to submit a claim to binding arbitration when the consumer purchases a product covered by written manufacturer and retailer warranties.”²³ Nationwide and Homestar contend, to the contrary, that the FAA controls and authorizes binding arbitration.²⁴

The court notes that the United States Supreme Court in *Shearson/American Express, Inc. v. McMahon* pronounced that the FAA, as any other statute, may be overridden by a contrary statute.²⁵ Under the *McMahon* test for determining the enforceability of arbitration agreements involving statutory claims the court states that “for a statutory claim to not be arbitrable, the party opposing arbitration must demonstrate that an ‘inherent conflict’ exists between the FAA and the statute’s underlying purposes.”²⁶ The party opposing arbitration must show that Congress intended to disallow any waiver of the right to sue under the statutory rights at issue. Congressional intent can be found in three ways: 1) in the text of the statute, 2) its legislative history, or 3) from any natural conflict between the FAA’s support for arbitration and the competing statute’s principal purpose.²⁷

In analyzing the Magnuson-Moss Act, the court briefly states its purpose is “to improve the adequacy of information available to consumers and prevent deception.”²⁸ The court also reasons that under the Act, a consumer who is damaged by a warrantor’s failure to comply with a warranty can sue for damages and

other legal and equitable relief.²⁹ This would seem to be in direct opposition to the FAA, which permits warrantors to force binding arbitration. To resolve this conflict the court sets out a rule of statutory construction: “Where an irreconcilable inconsistency is encountered between statutory provisions, the more recently enacted and more specific statute covering a specific subject controls over the earlier and more general one, unless there is evidence of a clear legislative intent to the contrary.”³⁰ The Van Blarcums argue the legislative history, underlying purpose, and the Act itself indicate that Congress sought to preserve a consumer’s right to sue.³¹ Agreeing with the Van Blarcums, the court heavily relies on *Southern Energy Homes v. Lee*, an Alabama Supreme Court case.

Southern states “the general provisions of the FAA are superceded by the subsequent and specific provisions in the Magnuson-Moss Act by which Congress has prohibited the inclusion in written warranties of clauses calling for binding arbitration.”³² Relying on *Southern*, the court declares that the Magnuson-Moss Act supercedes the FAA. Thus, binding arbitration clauses in written warranties for consumer products are unenforceable.³³

Having determined that the Magnuson-Moss Act controls in a consumer transaction, the court next turns to the question of whether the specific transaction at hand falls under the Magnuson-Moss Act. Homestar and Nationwide argue that the Magnuson-Moss Act does not apply because mobile homes do not meet the Act’s requirement that the transaction involve a “consumer product.”³⁴ The court finds that a mobile home falls within the Act’s definition of “consumer product.” In making this determination, the court focuses on the fact that a mobile home is by definition a movable dwelling that is tangible personal property.³⁵

The court further holds that the clause in the contract provides for binding arbitration of all “claims under any warranties” in violation of the Magnuson-Moss Act.³⁶ As an illegal agreement is unenforceable,³⁷ the trial court may not compel the Van Blarcums to submit to binding arbitration for the resolution of their mobile home warranty disputes.

C. Recent Developments

Last June the Supreme Court of Alabama decided *Southern Energy Homes v. Ard*.³⁸ In this case the court overruled its own decision in *Southern Energy Homes v. Lee*, in which it held binding arbitration clauses enforceable under the Magnuson-Moss Act. The *Van Blarcum* decision was based largely upon *Southern Energy Homes v. Lee*.

On August 9, 2000, briefs for a writ of mandamus were filed with the Supreme Court of Texas in the *Van Blarcum* case. On October 27, 2000 the Supreme Court of Georgia granted certiorari in *Results Oriented, Inc. v. Crawford* to hear the same issue of whether the Magnuson-Moss Act overrules the FAA.³⁹ These courts are faced with ruling on a controversial subject with little guidance to aid them.

It is important to note that there is no federal case law on this issue outside of Alabama. Two cases out of the United States District Court for the Middle District of Alabama provide the earliest authority: *Wilson v. Waverlee Homes, Inc.*,⁴⁰ and *Boyd v. Homes of Legend, Inc.*⁴¹

In *Wilson v. Waverlee Homes, Inc.*, the court stated in dicta that a mobile home seller may enforce a binding arbitration provision in a warranty contract against the buyer.⁴² *Boyd v. Homes of Legend, Inc.*, follows *Wilson* and clarifies the issue.⁴³ *Boyd* holds that the Magnuson-Moss Act primarily governs written warranties, with the result that only written warranties are non-arbitrable.⁴⁴ However, the argument exists that the court limited its own holding in *Wilson* with its decision in *Boyd* because the court was not sure exactly how far to go in enforcing arbitration clauses in warranties.

Unfortunately, few states have addressed this issue. Although Alabama has a significant amount of case law on the subject, the Alabama courts consistently produce divided decisions and occasionally overrule previous decisions.⁴⁵ Moreover, the supreme courts of Texas and Georgia have little authority to follow in making their decisions. The difficult issue facing the courts is rooted in the disagreement as to whether Congress intended to preserve a judicial forum for consumers when it passed the Magnuson-Moss Act. Only

one thing is clear; any decision on the issue must address the highly subjective *McMahon* three-prong test.

VI. MCMAHON ANALYSIS

The best way to predict how the Texas and Georgia supreme courts will decide this issue is to apply the *McMahon* test.

A. Prong One: Text

Under *McMahon* one can show congressional intent to override the FAA by examining the text of the statute itself. 15 U.S.C. § 2310(d)(1)(A) of the Magnuson-Moss Act gives consumers the right to “bring suit for damages and other legal and equitable relief...in a court of competent jurisdiction.” Additionally, 15 U.S.C. § 2310(a) of the Act governs informal dispute resolution mechanisms. By dictating that consumers may be required to “resort to such procedure [informal dispute resolution] before pursuing any legal remedy,” these two provisions arguably allow parties to preserve the right to go to court.⁴⁶ The argument’s strengths are that the Act is clear and simple. The statute clearly states that parties can go to court.⁴⁷

Conversely, others will read these provisions of the Magnuson-Moss Act in light of *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, which held that “by agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial forum.”⁴⁸ Yet, the Act does not grant substantive rights to judicial relief. Only the procedural right to judicial relief exists. The United States Supreme Court followed this logic in enforcing arbitration, but it is less than clear how lower courts can universally apply this logic.⁴⁹ In addition, an argument may be made that because the Act does not directly address arbitration, one cannot read arbitration into it

B. Prong Two: Legislative History

Proponents of arbitration may argue that there is nothing in the Act’s legislative history to show Congress intended arbitration agreements to be unenforceable when it passed the Act. Specifically, the Act does not mention arbitration. On the other hand, one may cite a

House of Representatives’ report stating that a decision in an informal dispute settlement proceeding is not a bar to a civil action on a warranty.⁵⁰ However, the better position is that nothing in the legislative history discusses arbitration; therefore, congressional intent does not preclude arbitration.

C. Prong Three: Purpose

Finally, one may take the view expressed in *Boyd* that the Act was passed in order to rectify differences in bargaining power.⁵¹ If the Act allowed consumers to be forced into binding arbitration through adhesion contracts then it would not fulfill its main purpose of

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rectifying the power imbalance between consumers and retailers. Therefore, an inherent conflict exists between FAA-governed arbitration and the Magnuson-Moss Act’s underlying purposes. Under this analysis, the FAA passes the *McMahon* test.

Nevertheless, the Act contains purposes in its own text that do not conflict with the FAA.⁵² Historically, the Supreme Court has failed to find an inherent conflict when certain statutes addressed imbalances in bargaining power.⁵³ Consequently, one faces difficulty in predicting Alabama’s and Texas’ future decisions regarding the third prong.

VII. CONCLUSION

The Corpus Christi appellate court’s decision in *Van Blarcum* is encouraging for consumers, especially mobile home buyers. The court was faced with two statutes

which arguably had contrary and irreconcilable statutory commands. By siding with the Magnuson-Moss Act, the court clearly chose the pro-consumer statute. If the Supreme Court of Texas agrees that the Magnuson-Moss Act controls over the FAA, warranty agreements that meet the Act’s requirements will come under the umbrella of its protection. In addition, warrantors of consumer goods may no longer be able to rely on the FAA and force binding arbitration.

It is important to note that the battle over how the FAA and the Magnuson-Moss Act interact will be far from over even after Texas and Georgia courts rule. The fact remains that the federal circuits have yet to address this issue.⁵⁴ Alabama is currently the only state where both the federal and state courts have dealt with the issue. In Alabama, a plaintiff may win or lose depending on the court in which his case is heard. Complicating matters further is the possibility that the Alabama Supreme Court may flip-flop again because its membership has changed. Finally, litigation over warranties and arbitration is increasing very rapidly. Congress passed the Magnuson-Moss Act in 1975. For over twenty years there were no cases regarding the issue discussed in this paper. In the last six months there have been at least six cases, the last of which was decided on December 1, 2000.⁵⁵ All of these factors make it probable that more decisions will be forthcoming. Ultimately, the potential for disparate decisions in courts across America should bring this matter before the United States Supreme Court.

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¹ Magnuson-Moss Warranty-Federal Trade Commission Improvement Act of 1975, 15 U.S.C. §§ 2301-2312 (1994).

² Annotation, *Consumer Product Warranty Suits in Federal Court under Magnuson-Moss Warranty-Federal Trade Commission Improvement Act*, 59 A.L.R. Fed. 461 (1982) [hereinafter *Consumer Product*].

³ 15 U.S.C. § 2302(a).

⁴ *Consumer Product*, 59 A.L.R. Fed. 461 (1982).

- ⁵ 15 U.S.C. § 2301(5).
- ⁶ *Id.* § 2302(a), § 2312(c).
- ⁷ 16 C.F.R. § 701-703 (2000).
- ⁸ *Id.* § 700.8.
- ⁹ 15 U.S.C. § 2301(1).
- ¹⁰ *Id.*
- ¹¹ *Id.* § 2310(d).
- ¹² H.R. REP. NO. 93-1107 (1974), *reprinted in* 1974 U.S.C.C.A.N. 7702.
- ¹³ 15 U.S.C. § 2310(d)(3)(B).
- ¹⁴ *Id.* § 2310(d)(3)(A).
- ¹⁵ *Id.* § 2310(d)(3)(C).
- ¹⁶ *Id.* § 2310(d)(1).
- ¹⁷ *Id.* § 2310(d)(2).
- ¹⁸ Federal Arbitration Act, 9 U.S.C. § 2 (1994).
- ¹⁹ *In re Van Blarcum*, 19 S.W.3d 484 (Tex.App.-Corpus Christi 2000).
- ²⁰ *Id.* at 488.
- ²¹ *Id.* at 488 (citing 9 U.S.C. § 2).
- ²² *In re Van Blarcum*, 19 S.W.3d at 487.
- ²³ *Id.*
- ²⁴ *Id.* at 490
- ²⁵ *See* 482 U.S. 220, 226 (1987).
- ²⁶ *In re Van Blarcum*, 19 S.W.3d at 490 (citing *Knepp v. Credit Acceptance Corp.* (In re *Knepp*), 229 B.R. 821, 833 (Bankr.N.D.Ala.199)).
- ²⁷ *Shearson/American Express, Inc. v. McMahon*, 482 U.S. at 227.
- ²⁸ 15 U.S.C. § 2302(a).
- ²⁹ *Id.* § 2310(d)(1).
- ³⁰ *In re Van Blarcum*, 19 S.W.3d at 490 (citing *HCSC-Laundry v. United States*, 450 U.S. 1, 6 (1981); *Balfour Beatty Bahamas, Ltd. v. Bush*, 170 F.3d 1048, 1050 (11th Cir.1999); *ICC v. Southern Ry. Co.*, 543 F.2d 534, 539 (5th Cir.1976)).
- ³¹ *In re Van Blarcum*, 19 S.W.3d at 491.
- ³² *Southern Energy Homes, Inc. v. Lee*, 732 So.2d 994, 999-1000 (Ala. 1999), *overruled by* *Southern Energy Homes, Inc. v. Ard*, 772 So.2d 1131 (Ala. 2000).
- ³³ *Van Blarcum* 19 S.W.3d at 491.
- ³⁴ *Id.*
- ³⁵ *Id.* at 492.
- ³⁶ *Id.* at 496.
- ³⁷ *Id.* (citing *Palma v. Verex Assur., Inc.*, 79 F.3d 453, 462 (5th Cir.1996) (quoting *DiFrancesco v. Houston Gen. Ins. Co.*, 858 S.W.2d 595, 598 (Tex.App.—Texarkana 1993, no writ)); *Phillips v. Phillips*, 820 S.W.2d 785, 789 (Tex.1991)).
- ³⁸ 772 So.2d 1131. (Ala. 2000).
- ³⁹ *Results Oriented, Inc. v. Crawford*, 538 S.E.2d 73 (Ga.App. Jul 31, 2000) *certiorari granted* (Oct 27, 2000).
- ⁴⁰ *Wilson v. Waverlee Homes, Inc.*, 954 F.Supp. 1530, 1539 (M.D.Ala. 1997), *aff'd*, 127 F.3d 40 (11th Cir. 1997) (table).
- ⁴¹ *Boyd v. Homes of Legend, Inc.*, 981 F.Supp. 1423 (M.D. Ala 1997), *remanded on jurisdictional grounds by* 188 F.3d 1294, 1300 (11th Cir.1999) (instructions given to district court to vacate in part).
- ⁴² *Wilson*, 954 F.Supp. at 1539.
- ⁴³ *Boyd*, 981 F.Supp. at 1423.
- ⁴⁴ *Id.* at 1436.
- ⁴⁵ *See* *Southern Energy Homes, Inc. v. Lee*, 732 So.2d 994 (Ala. 1999); *overruled by* *Southern Energy Homes, Inc. v. Ard*, 772 So.2d 1131 (Ala. 2000).
- ⁴⁶ *Id.*; 15 U.S.C. § 2301(d)(1)(A).
- ⁴⁷ 15 U.S.C. § 2301(d)(1)(A).
- ⁴⁸ *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.* 473 U.S. 614, 628 (1985).
- ⁴⁹ *See McMahon*, 482 U.S. at 229; *see also Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 35 (holding that the Age Discrimination in Employment Act claims are arbitrable notwithstanding that 29 U.S.C.S. § 626(c)(1) provides for a judicial forum for relief); *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 485-86 (1989)(holding that Securities Act of 1933 claims are arbitrable notwithstanding that 15 U.S.C.S. §77v(a) provides a judicial forum for relief).
- ⁵⁰ H.R.REP. 93-1107 (1974), *reprinted in* 1974 U.S.C.C.A.N. 7702, 7723.
- ⁵¹ *Boyd*, 981 F.Supp. at 1440.
- ⁵² *See* 15 U.S.C. § 2302(a).
- ⁵³ *See McMahon*, 482 U.S. 220; *see also Gilmer*, 500 U.S. at 29; *Rodriguez de Quijas*, 490 U.S. 477 (1989).
- ⁵⁴ Note that the Eleventh Circuit decision affirmed *Wilson* without issuing an opinion. *See Wilson v. Waverlee Homes, Inc.*, 127 F.3d 40 (11th Cir.1997). Thus it is not binding precedent. *See DeShong v. Seaboard Coast Line R.R.*, 737 F.2d 1520, 1523-24 (11th Cir.1984).
- ⁵⁵ *Southern Energy Homes, Inc. v. McCrary*, No. 1991435, 2000 WL 1763365 (Ala. Dec. 1, 2000).