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ARBITRATION

ARBITRATION CLAUSE IN CONTRACT MAY NOT BE AVOIDED BY PLEADING FRAUDULENT INDUCEMENT

In re Kaplan Higher Educ. Corp., 235 S.W.3d 206 (Tex. 2007).

FACTS: The plaintiffs were students enrolled in an electrician's program at San Antonio College of Medical and Dental Assistants-McAllen Branch ("The College"), a wholly owned subsidiary of Kaplan Higher Education Corporation ("Kaplan"). Each student signed an enrollment agreement detailing tuition, rules and graduation requirements. The agreement required them to arbitrate "[a]ny controversy or claim arising out of, or relating

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to this Agreement" pursuant to the Federal Arbitration Act ("FAA"). Nevertheless, the students sued the College, Kaplan, the College's president, and the College's admission director for false assurances that upon graduation the students would be eligible for licenses as journeymen or master electricians. They alleged negligence, negligence per se,

negligent misrepresentation, and violations of the Deceptive Trade Practices Act.

The defendants moved to compel arbitration pursuant to the FAA and the students dropped their claims against the College and College's president. However, they maintained their claims against the non-signatories, Kaplan and Ventura. The trial court refused to compel arbitration. Kaplan and Ventura petitioned the Thirteenth Court of Appeals for mandamus, which it denied without explanation. Kaplan and Ventura petitioned the Supreme Court of Texas for mandamus relief.

HOLDING: Remanded.

REASONING: The court held that the students could not avoid arbitration by bringing a fraudulent inducement claim. The court recognized that the arbitrability of a claim turns on the substance of the claim, not artful pleading.

The court stated that "claims must be brought on the contract and arbitrated if liability arises solely from the contract." Here, the court found that "although alleged in various forms, the substance of the students' claims was fraudulent inducement, as they [sought] refunds of tuition and other cost they would not have incurred had they not" enrolled in the College's electrician program. Because the allegations went to the students' "contract" with Kaplan, the court found that it was subject to arbitration under the arbitration clause of the enrollment agreement, which applied to any controversy or claim "arising out of, or relating to" the agreement.

The court stated that a fraudulent inducement claim generally arises from an obligation imposed by law, not the underlying contract. However, the court recognized a need "to place arbitration agreements on equal footing with other contracts," because "almost every contract claim against a corporation could be recast as a fraudulent inducement claim against the agent, or employee who took part in the negotiation" to avoid having to arbitrate.

TEXAS SUPREME COURT MANDATES ARBITRATION OF CONSUMER DISPUTE

In re U.S. Home Corp., 236 S.W.3d 761, (Tex. 2007).

FACTS: Two couples, representing a class of home buyers, brought suit against U.S. Home, Lennar Corporation and three U.S. Home employees for failure to include shower pans in their houses. They acknowledged that there was a binding arbitration clause in their agreement with builder, but raised seven contract defenses to arbitration. They alleged damages which included medical bills, mold remediation, repairs and mental anguish.

Defendants moved to compel arbitration. Plaintiffs moved for class certification. The district court found merit in five of the plaintiffs' contract arguments against arbitration: (1) that the arbitration clauses were contracts of adhesion, and thus procedurally unconscionable; (2) that the arbitration clauses were procured by fraud; (3) that the arbitration clauses were not supported by mutual consideration; (4) that arbitration would be unduly burdensome and costly; and (5) that a mediation clause was a condition precedent to arbitration. The district court denied defendants' motion to compel arbitration, and granted plaintiffs' motion for class certification. Defendants filed a petition for a writ of mandamus.

HOLDING: Writ conditionally granted.

REASONING: The court found all the arguments accepted by the trial judge, as well as additional arguments made by plaintiffs on appeal, to be without merit. In response to the adhesion argument, the court stated that there is nothing inherently unconscionable about arbitration agreements. It was not enough that the plaintiffs proved that U.S. Homes refused to contract with them unless they agreed to arbitration. The court found that the fraud allegation was based on the fact that the arbitration clause was on the back of the contract and this was insufficient to prove fraud. The court further stated that the finding of no mutual consideration was simply wrong because both parties agreed to arbitration. In response to the contention that arbitration would be too costly, the court noted that plaintiffs had simply provided a normal schedule of fees, and that this was not enough. Finally, the court found that while the parties had obviously contemplated mediation, it was not a requirement that precluded arbitration.

On appeal, plaintiffs raised two additional arguments. First, they argued that they were not required to arbitrate because one of the warranty agreements said that "either party 'may request' arbitration." The court rejected this argument, stating that it must consider all contracts as a whole, and not let them cancel each other out. It also noted that arbitration would still be binding at the request of either party.

Second, the plaintiffs argued that they did not have to arbitrate against the individual defendants because these defendants were not signatories to the original agreement. The court found this argument to be without merit as well. "[A] litigant who sues based on a contract subjects him or herself to the contract's terms." For these reasons, without hearing oral argument, the court conditionally granted the writ, stating it would issue the writ only if the trial court failed to follow their order to compel arbitration.

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CELL PHONE COMPANY CAN ARBITRATE COMMUNICATIONS ACT CLAIMS

Lozano v. AT & T Wireless Services, Inc., 504 F.3d 718 (9th Cir. 2007).

FACTS: Paul Lozano, a customer of AT & T Wireless Services, Inc. (“AWS”), brought a putative class action alleging that AWS did not fully disclose a billing practice to its customers. AWS contends that it made full disclosure of its billing practices in its Welcome Guide. The Welcome Guide also contained an agreement to arbitrate which included a class action waiver clause. Shortly after Lozano filed suit, AWS moved to compel arbitration. The district court initially granted the motion, but subsequently vacated its order. In vacating, the district court found that the class action waiver was unconscionable and unenforceable under California law.

Lozano then sought to certify a national class of AWS customers for claims brought pursuant to the Federal Communications Act (“FCA”). However, the district court refused to certify a national class on the basis that individual issues would predominate over class issues. The court reasoned that having class members nationwide would require individual determinations of whether the class action waiver was unenforceable under the law of a particular customer’s state. Lozano contended that this inquiry was extraneous because claims brought pursuant to the FCA were not subject to arbitration in the first place. Lozano asserted that it was Congress’s intent to preclude adjudication of FCA claims by arbitration. The district court rejected this contention and Lozano appealed.

HOLDING: Affirmed.

REASONING: Because of the Federal Arbitration Act’s policy of favoring arbitration, Lozano was required to show that Congress intended to preclude arbitration of FCA claims. If congressional

intent existed, it would have to be found in the text of the statute, the statute’s legislative history, or in “an inherent” conflict between arbitration and the FCA’s underlying purpose.

Section 207 of the FCA provides that consumers may bring FCA claims before the FCC or file suit in federal district court.

Inequality in bargaining power was not sufficient to hold arbitration agreements unenforceable.

Lozano argued that Congress, in § 207, intended to exclude the arbitral forum because important policy considerations are litigated in FCA claims. The court rejected this argument, citing multiple U.S. Supreme Court cases in which the Court found statutory claims were arbitrable in spite of important public policy concerns. Lozano also argued that FCA claims should not be arbitrable because of the inequality in bargaining power between consumers and communications companies. The court found that inequality in bargaining power was not sufficient to hold arbitration agreements unenforceable.

Lozano also argued that the FCA claims were not subject to mandatory arbitration pursuant to the court’s decision in *AT & T Corp. v. Coeur d’Alene Tribe*, 295 F.3d 899 (9th Cir. 2002). In *Coeur d’Alene Tribe*, the court held that tribal courts did not have jurisdiction to adjudicate FCA claims because Congress, by

limiting the jurisdiction of FCA claims in § 207, intended to leave no room for “adjudication in any other forum—be it state, tribal, or otherwise.” The court rejected Lozano’s contention that the arbitral forum was also excluded. The court reasoned that *Coeur d’Alene Tribe* did not determine whether § 207 barred the arbitral forum. This would have required a strong showing of congressional intent. The fact that Congress included the designation of fora for the adjudication of FCA claims does not, without more, establish congressional intent. The court also reasoned that the Sherman Act has jurisdictional language similar to that found in § 207 of the FCA, and the Supreme Court has held that claims under the Sherman Act are subject to arbitration.

CLASS WAIVER MAY BE UNENFORCEABLE IN OVERTIME CASE

Gentry v. Superior Court, 165 P.3d 556 (Cal. 2007).

FACTS: The plaintiff, Robert Gentry, was an employee of Circuit City. Gentry’s position within in the company allegedly should have entitled him to overtime time pay, but he and others were erroneously classified as exempt managerial employees. Gentry filed a class action lawsuit on behalf of salaried employees against the company claiming Circuit City had violated California’s Labor Code and Business and Professions Code.

When Gentry was hired, Circuit City had him sign a dispute resolution agreement, which included an arbitration clause. The terms for arbitration included: 1) a 30-day option to opt-out of the arbitration agreement; 2) a class arbitration waiver; 3) a suspension of any litigation once arbitration is chosen; and, 4) a limitation on damages, attorneys’ fees and statute of limitations.

The Superior Court of Los Angeles County stayed Gentry’s action and ordered him to arbitrate his claim individually. Gentry’s writ of mandate to the Court of Appeals was denied. The California Supreme Court granted Gentry’s petition for review.

HOLDING: Reversed and remanded.

REASONING: The court began by discussing the possibility that class action waivers in contracts of adhesion may be found substantively unconscionable. Specifically, if the waiver is found to exculpate a party contrary to public policy or if the waiver is found to be substantially favoring one side over the other, it may be unenforceable. The court stated that class action waivers are not per se unconscionable, but are dependent upon the facts of the case.

The present case concerned the statutory right to receive overtime pay, which is unwaivable. The court concluded that if a class arbitration waiver is found to “impermissibly interfere” with the ability to enforce an unwaivable statutory right, then the waiver may be unenforceable. The court explored examples of impermissible interference. First, because the amount of damages sought in overtime disputes are often small, it may be impractical to pursue individual litigation or arbitration. The court explained that proving overtime violations could be difficult and therefore cost prohibitive for an individual suit. And while the overtime statute entitles the successful plaintiff to attorneys’ fees, there is still the risk that the plaintiff will be unsuccessful.

Second, a current employee is at greater risk of retaliation pursuing an individual suit, than one who is simply

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represented in a class action or arbitration. Circuit City argued that California's anti-retaliation statute offers sufficient protection to current employees. The court agreed with Gentry that the fear of retaliation would often deter a current employee from pursuing individual litigation despite the statute.

Finally, an employee may not be aware that their employer has violated their statutory right to overtime pay. The court found that because Circuit City told their employees that they were not

eligible for overtime pay, there was a greater likelihood that these employees would be unaware their rights had been violated.

The court ordered the trial court on remand to consider the above three factors. If the trial court concludes that the class arbitration waiver interferes with employees' ability to enforce their unwaivable statutory rights, it must invalidate the waiver clause.

UNIFORM COMMERCIAL CODE

UNCERTIFIED CHECK IS MERELY CONDITIONAL PAYMENT

E.P. Towne Ctr. Partners, L.P. v. Chopsticks, Inc., ___ S.W.3d ___ (Tex. App.—El Paso 2007).

FACTS: E.P. Towne Center Partner, L.P. ("Towne Center") leased a restaurant in its shopping center to Chopsticks, Inc. Chopsticks sued Towne Center for violation of an exclusivity clause and Towne Center filed a counter suit for breach of contract alleging non-payments of rents. The disputes were resolved in mediation. The settlement agreement required Chopsticks to pay Towne Center a lump sum followed by four monthly payments. Chopsticks timely made the lump sum payment and tendered an uncertified check for the first monthly payment. When Towne Center attempted to deposit the check, it was returned for insufficient funds.

Towne Center contacted Chopsticks to secure an alternative payment. Chopsticks said to redeposit the check, but Towne Center no longer possessed it. There was a dispute as to whether Towne Center requested a cashier's check. Chopsticks subsequent monthly check was deposited without incident.

Pursuant to the terms of the settlement agreement, Towne Center filed a motion for entry of judgment. The trial court denied the motion concluding that the settlement agreement was incomplete and ambiguous and that Chopsticks had fulfilled its obligations. Towne Center appealed.

HOLDING: Reversed.

REASONING: Towne Center argued that Chopsticks breached

the agreement when the first monthly installment check was dishonored. The court stated that "[a]n uncertified check is merely a conditional payment for an obligation and payment is made absolute when the check is presented and honored." Because Chopsticks' check was returned for lack of funds, its obligation to make an installment payment was not performed. The court found Chopsticks' non-performance was a breach of the agreement entitling Towne Center to enforcement under the agreement.

Chopsticks argued Towne Center was estopped from denying that the terms of the agreement were satisfied by accepting the second monthly payment. It also argued that its previous and subsequent payments were substantial performance of its obligations. Finally, Chopsticks argued that since only one payment was untimely, its breach was immaterial.

Because Chopsticks proffered no support for its estoppel argument, this argument was rejected. The court found that the payments were essential to the performance of the agreement, so the doctrine of substantial performance was not available to Chopsticks. Finally, the court held that any non-performance was a breach of the agreement and therefore material.

“An uncertified check is merely a conditional payment for an obligation and payment is made absolute when the check is presented and honored.”