Mandatory Arbitration Hits Home

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Texas and federal courts provide little protection to consumers trapped in arbitration agreements. The recent housing surge in the Lone Star State gave rise to a number of disputes between homeowners and homebuilders. Many homeowners learned, to their chagrin, that during the excitement of signing the contracts for their dream homes, they may have inadvertently signed away the constitutional right to have juries settle complaints against the homebuilders.

Although Texas Civil Practice and Remedies Code §171.022 prohibits judges from enforcing mandatory arbitration clauses when such the agreement is determined to be unconscionable at the time the contract was formed, there is no standard for the court to apply. Texas courts - for example Houston's 1st Court of Appeals in Emerald Texas Inc. v. Peel (1996) - have upheld binding arbitration clauses in homebuilder contracts where all evidence indicates that buyer had no knowledge of real estate or even a basic understanding of what arbitration meant. Furthermore, the Texas Supreme Court has made it clear - in 1999's In re Oakwood Mobile Homes Inc. - that it makes no difference if the arbitration clause is an option or a take-it-or-leave-it adhesion contract. In the words of the court in Emerald, "public policy favors of arbitration." In April 2001, Texas Lawyer reported an ongoing case of Dawn Richardson, an Austin homeowner, who filed a suit against David Weekley Homes after she learned that her family's new home allegedly was contaminated with dangerous levels of toxic mold and volatile organic compounds such as benzene, benzaldehyde, decane, heptane, formaldehyde, methylbenzene, octane, styrene and xylene. [See "In Austin: Arbitration-Bound Texans Seek Lawmakers' Help," Texas Lawyer, April 15, 2001, page 1.] As alleged, all the family's personal belongings were ruined by the contamination, and they were forced to evacuate after discovering the contaminants caused the family serious health problems, including neurological damage to their baby and the death of their family cat, which had cancer.

Recently, in Richardson v. Weekley Homes, the 53rd District Court of Travis County ordered the Richardsons to arbitrate their dispute with Weekley before the American Arbitration Association on the arbitration clause, which the Richardsons alleged they did not understand when they signed the contract with the homebuilder.

In Richardson, the homebuilder agreed to advance filing fees and arbitration fees, but this underscores another problem with mandatory arbitration clauses in consumer contracts. Large companies often contract with arbitration firms to handle all consumer disputes. Companies naturally tend to use the same arbitrator repeatedly - as long as they are happy with the results they obtain. Moreover, the secrecy of arbitration proceedings and loss of trial and evidentiary precedent makes it difficult for consumers to go up against arbitration regulars, such as large homebuilders. Because of the recent surge in new home construction in Texas and the usage of mandatory arbitration clauses by savvy homebuilders, it is likely this alternative justice will mean no justice to many homeowners.

Despite the longstanding public policy favoring arbitration and other forms of alternative dispute resolution, there is reason to believe that the tides may be changing. For instance, earlier this year, the U.S. Supreme Court ruled in EEOC v. Waffle House Inc. that the Equal Employment Opportunity Commission could bring suit on behalf of employees in court even when the employer requires their employees to enter into binding arbitration agreements as a condition for employment. Justice John Paul Stevens, speaking for the court, noted that "[d]espite the FAA [Federal Arbitration Act] policy favoring arbitration agreements, nothing in the FAA authorizes a court to compel arbitration of any issues, or by any parties, that are not already covered in the agreement." In the dissenting opinion, Justice Clarence Thomas argued that "[b]y allowing the EEOC to pursue victim-specific relief on behalf of [the employee] . . . the court eviscerates [the employee's] arbitration agreement. . . ."

Several weeks after the EEOC decision, the 5th U.S. Circuit Court of Appeals, interpreting Texas law, also refused to compel arbitration in a case involving the sale of a mobile home, in which the sales contract included a mandatory arbitration clause. In that case, Fleetwood Enters. v. Gaskamp, the buyer's children allegedly suffered personal injuries from exposure to formaldehyde in the new mobile home. The court held that since the children were not parties to the contract, the parents were entitled to bring suit on behalf of their children.

While the EEOC case and the 5th Circuit case relate to the party bringing suit, one court suggested that another controlling factor is whether the particular disputed issue is covered by the contract. In a 1999 Florida case, Seifert v. U.S. Home Corp., brought against a homebuilder by a homeowner whose husband allegedly was killed due to a defective air conditioning system installed in their new home, the Florida Supreme Court refused to compel arbitration because the court ruled that the agreement to arbitrate is not necessarily binding on independent tort actions based upon common-law duties.

While these recent court decisions offer some hope for consumers who unknowingly sign away their constitutional right to have juries settle complaints, the recent decision by the 53rd District Court to compel arbitration in Richardson highlights the need for re-examination of the policy of allowing adhesion contracts by large corporations to deny consumers a day in court.

On May 15, 2002, the Texas Legislature held a hearing on binding arbitration to review the topic, "trends in the use of binding arbitration requirements in consumer agreements, with special attention to transactions in which the consumer has little or no bargaining power." Consumer groups as well as representatives of the homebuilding industry participated full-force in the debate. However, both sides agree that as far as the Texas homebuilding industry is concerned, mandatory arbitration is not an option for aggrieved homebuyers - it is the rule.

One homebuilder tells homebuyers who refuse to sign his company's arbitration clause to go elsewhere. He says they will continue this practice, even if and when the roaring economy slows down, according to the information in the committee packet of the Subcommittee on Binding Arbitration. According to information received by the Subcommittee on Binding Arbitration, several homebuilders require purchasers to enter into mandatory arbitration agreements.

Because the FAA pre-empts state law, it is difficult for state legislatures to do away with mandatory arbitration. However, some states have taken positive steps to protect their consumers. For instance, California recently enacted a law - California Code of Civil Procedure §1298.7 - that eviscerates agreements in any claims related to bodily injury or wrongful death. More significantly, last year, New Mexico became the first state to adopt the Fair Bargain Act developed by Paul Carrington, a professor at Duke Law School, according to a report submitted to the subcommittee, "Public Citizen, Revised Uniform Arbitration Act: An Opportunity for State-Level Reform."

The Fair Bargain Act, which applies to all standard form contracts or leases, provides statutory guidance for judicial relief to have clauses that "disable civil disputes" declared unenforceable in certain circumstances. The act is a legislative attempt to make arbitration fairer to consumers, and since the act applies across-the-board to form contracts - whether they include a mandatory arbitration clause - the act is not anti-arbitration, but pro-fair-arbitration, which is consistent with the philosophy of the Federal Arbitration Act, and thus should survive pre-emption challenges.

Maybe it is time for Texas to follow New Mexico's lead and protect its consumers.

Texas Lawyer June 3, 2002

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