BUSINESS & COMMERCIAL LAW UPDATE

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State Bar of Texas
25th ANNUAL LITIGATION UPDATE INSTITUTE
February 26-27, 2009
Houston

CHAPTER 18

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BUSINESS & COMMERCIAL LAW UPDATE

1. SCOPE OF ARTICLE

This article summarizes the key commercial and business cases decided by the Texas Supreme Court between October 1, 2007 and October 1, 2008, as well as one US Supreme Court case that affects Texas case law.

2. FORUMS

a. When can you avoid a forum selection clause?

In In re Lyon Financial Services, Inc., 257 S.W.3d 228 (Tex. 2008), the Texas Supreme Court held that forum-selection clauses must be enforced absent evidence that "clearly show[s] . . . (1) enforcement would be unreasonable or unjust; (2) the clause is invalid for reasons of fraud or overreaching; (3) enforcement would contravene a strong public policy of the forum where the suit was brought, or (4) the selected forum would be seriously inconvenient for trial." Id. at 231-32. The Court explained that "[a] forum-selection clause is generally enforceable, and the burden of proof on a party challenging the validity of such a clause is heavy." Id. at 232.

The plaintiff below contended that the defendant "fraudulently induced it to agree to the [agreement's] forum-selection clause." Id. at 232. The Court rejected this argument, stating "[w]e have held that fraudulent inducement to sign an agreement containing a dispute resolution agreement such as an arbitration clause or forum-selection clause will not bar enforcement of the clause unless the specific clause was the product of fraud or coercion." Id. The plaintiff then argued that the forum-selection clause was invalid because it was unfair. Id. The Court rejected this argument as well, noting that unequal bargaining power is of no matter so long as the contract does not result in unfair surprise or oppression.

The plaintiff then argued that the selected forum was so inconvenient that "enforcing the forum-selection clause would produce an unjust result." Id. at 233. The Texas Supreme Court cited the position of the United States Supreme Court:

> The Supreme Court observed that inconvenience in litigating in the chosen forum may be foreseeable at the time of contracting, and when that is the case, "it should be incumbent on the party seeking to escape his contract to show that trial in the contractual forum will be so gravely difficult and inconvenient that he will for all practical purposes be deprived of his day in court."

The Texas Supreme Court then concluded that:

> By entering into an agreement with a forum-selection clause, the parties effectively represent to each other that the agreed forum is not so inconvenient that enforcing the clause will deprive either party of its day in court, whether for cost or other reasons. MNI executed a Master Agreement and the Restructuring Agreement, both containing clauses vesting jurisdiction in Pennsylvania courts. There is no evidence that MNI's financial or "logistical" conditions changed from the time the agreements were executed to the time MNI filed suit in Hidalgo County or Hernandez executed the affidavit. If merely stating that financial and logistical difficulties will preclude litigation in another state suffices to avoid a forum-selection clause, the clauses are practically useless. Financial difficulties on behalf of one party or the other are typically part of the reason litigation begins. Further, Pennsylvania is not a "remote alien forum." Absent proof of special and unusual circumstances, which are not shown here, trial in another state is not "so gravely difficult and inconvenient" as to avoid enforcement of an otherwise valid forum-selection clause.

Id.

Finally, the Court considered the plaintiff's objection that "enforcement of the forum-selection clause would unjustly preclude its day in court" because Pennsylvania law does not allow a corporation to maintain cause of action for usury. Id. at 234. The Court rejected this argument, holding that its prior case law establishes that "absent a Texas statute requiring suit to be brought in Texas, the existence of Texas statutory law in an area did not establish such Texas public policy as would negate a contractual forum-selection provision." Id. at 234.

b. Can you avoid a venue ruling by nonsuiting?

On May 23, 2008, the Texas Supreme Court decided In Re Team Rocket, L.P., 256 S.W.3d 257 (Tex. 2008). The Texas Supreme Court held that Texas Rule of Civil Procedure 87, which prohibits changes in venue after the initial venue ruling, prevents a plaintiff from nonsuiting a case in order to file in a more favorable venue after an adverse venue ruling. Id. at 258.

In In Re Team Rocket, the family of decedent Thomas Creekmore brought suit against Team Rocket for the manufacture and sale of the plane kit Creekmore had purchased. "Creekmore died when the airplane he was flying crashed in Fort Bend County."

Id. However, the family brought suit in Harris County. Id. Team Rocket moved to transfer venue to Williamson County, "which was Team Rocket's principle place of business and the residence of its representative." Id. at 259. "After the transfer, the Creekmores voluntarily nonsuited the case and immediately refiled the same claims against the same defendants in Fort Bend County." Id. Team Rocket moved to transfer venue back to Williamson County, arguing that collateral estoppel precluded reconsideration of the prior venue ruling. Id. The trial court refused, and Team Rocket sought mandamus relief.

The Court of Appeals denied the petition, but the Texas Supreme Court conditionally granted the petition. The Texas Supreme Court held that only one venue determination may be made in a proceeding and that Texas Rule of Civil Procedure 87 specifically prohibits changes in venue after the initial venue ruling. Id. Texas Rule of Civil Procedure 87 provides that "if an action has been transferred to a proper county in response to a motion to transfer, then no further motions to transfer shall be considered." The Court held that "Once a ruling is made on the merits, as in a summary judgment, that decision becomes final as to that issue and cannot be vitiated by nonsuing and refiling the case. . . . Just as a decision on the merits cannot be circumvented by nonsuiting and refiling the case, a final determination fixing venue in a particular county must likewise be protected from relitigation." Id. at 260. The court explained that "[t]o interpret the provisions [of Rules 15.064 and 87] otherwise would allow forum shopping, a practice we have repeatedly prohibited." Id.

3. ARBITRATION

a. When do you waive arbitration?

In Perry Homes et al v. Cull et ux , 258 S.W.3d 580 (Tex. May 2, 2008), the Texas Supreme Court interpreted for the first time what constitutes a waiver of arbitration. In the 5-4 decision, the Texas Supreme Court held that a party can waive a contractual agreement to arbitrate by substantially invoking the litigation process.

The plaintiffs sued Perry Homes and other warranty providers for defects in their home. Id. at 584. The warranty agreement "included a broad arbitration clause. Id. Defendants (other than Perry Homes) immediately moved to compel arbitration. Id. at 585. The plaintiffs vigorously opposed the motion, but the court never ruled on the motions. Id. The plaintiffs engaged in discovery, taking 10 depositions, filing motions to compel, seeking protective orders and the like. Id. at 596. Four days before trial of their suit, plaintiffs moved to compel. Id. at 585.

The trial court "ordered arbitration because the Defendants had not shown any prejudice from litigation conduct, [saying] 'all I have heard from [defense counsel] insofar as what is the prejudice suffered by people you represent is that they have participated in litigation activities that may or may not have been required by the arbitrator. So without anything further, am going to grant the motion to abate the case for arbitration.'" Id.

"After a year in arbitration," the arbitrator entered an award for the plaintiffs, and the defendants moved to vacate the award, arguing that the case "should never have been sent to arbitration after so much activity in court." Id. The trial court denied the motion to vacate, and defendants appealed. Id.

The Supreme Court held that while "there is a strong presumption against waiver of arbitration, . . . it is not irrebuttable." Id. at 584. The Supreme Court noted that it had previously held:

> on many occasions that a party waives an arbitration clause by substantially invoking the judicial process to the other party's detriment or prejudice. Due to the strong presumption against waiver of arbitration, this hurdle is a high one. To date, we have never found such a waiver, holding in a series of cases that parties did not waive arbitration by:
>
> - filing suit;
> - moving to dismiss a claim for lack of standing;
> - moving to set aside a default judgment and requesting a new trial;
> - opposing a trial setting and seeking to move the litigation to federal court;
> - moving to strike an intervention and opposing discovery;
> - sending 18 interrogatories and 19 requests for production;
> - requesting an initial round of discovery;
> - noticing (but not taking) a single deposition, and agreeing to a trial resetting; or
> - seeking initial discovery, taking four depositions, and moving for dismissal based on standing.

Id. at 589-90.

The Court explained that:

> These cases well illustrate the kind of conduct that falls short. But because none amounted to a waiver, they are less instructive about what conduct suffices. We have stated that "allowing a party to conduct

> full discovery, file motions going to the merits, and seek arbitration only on the eve of trial" would be sufficient. But what if (as in this case) only two out of these three are met? And how much is "full discovery"?

Id. at 590.

The Court of Appeals had found that waiver was impossible because the plaintiffs "did not ask the court to make any judicial decisions on the merits of their case." Id. However, the Texas Supreme Court noted that federal courts sometimes found waiver where only factor was present and thus "[w]hile this is surely a factor, it is not the only one. Waiver involves substantial invocation of the judicial process, not just judgment on the merits." Id. at 592.

Instead, looking at federal court decisions for guidance, the Court adopted a totality of the circumstances analysis that would consider the following factors:

- whether the movant was plaintiff (who chose to file in court) or defendant (who merely responded);
- how long the movant delayed before seeking arbitration;
- whether the movant knew of the arbitration clause all along;
- how much pretrial activity related to the merits rather than arbitrability or jurisdiction;
- how much time and expense has been incurred in litigation;
- whether the movant sought or opposed arbitration earlier in the case;
- whether the movant filed affirmative claims or dispositive motions;
- what discovery would be unavailable in arbitration;
- whether activity in court would be duplicated in arbitration; and
- when the case was to be tried.

Id. at 590.

The Court did "agree with the courts below that waiver of arbitration requires a showing of prejudice." Id. at 592. However, the Court found that defendants had been prejudiced. Id. at 598. The Court reasoned that:

> "Prejudice" has many meanings, but in the context of waiver under the FAA it relates to inherent unfairness - that is, a party's attempt to have it both ways by switching between litigation and arbitration to its own advantage. [The Plaintiffs] got the court to order discovery for them and then limited their opponents' rights to appellate review. Such manipulation of litigation for one party's advantage and another's detriment is precisely the kind of inherent unfairness that constitutes prejudice under federal and state law.

Id. at 598.

The Court concluded that the totality of the circumstances reflected a waiver, explaining that:

> the plaintiffs vigorously opposed (indeed spurned) arbitration in their pleadings and in open court; then they requested hundreds of items of merit-based information and concocted months of discovery under the rules of court; . . . having gotten what they wanted from the litigation process, they could not switch to arbitration at the last minute like this.

Id. The Court reached this holding even though the practical result was to force the case to be retried in a court after having already been fully tried in arbitration. Id. The Court reasoned:

> The Plaintiffs argue – and we agree – that sending them back to the trial court not only deprives them of a substantial award but also wastes the time and money spent in arbitration. But they knew of this risk when they requested arbitration at the last minute because all of the Defendants objected. Accordingly, we vacate the arbitration award and remand the case to the trial court for a prompt trial.

Id.

Finally, the majority criticized the dissent for "defin[ing] prejudice in a way that makes it impossible to prove":

> both dissents quibble with the Defendants' proof of prejudice because it was insufficiently detailed. This confuses proof of the fact of prejudice with proof of its extent; the Defendants had to show substantial invocation that prejudiced them, not precisely how much it all was.

Id. at 599

A month later, the Texas Supreme Court found that a party had not waived its right to arbitration. In

the case of In Re Fleetwood Homes of Texas L.P., 257 S.W.3d 692 (Tex. June 20, 2008), Gulf Regional Services, Inc., an owner and developer of mobile home parks in southeast Texas that also sells and leases mobile homes, sued Fleetwood Enterprises, Inc., a manufacturer of mobile homes for improper cancellation of a dealer agreement. "After Gulf filed suit in October 2005, Fleetwood filed an answer demanding arbitration, but did not actually move to compel arbitration until July 2006." Id. at 693.

Before moving to compel arbitration, Fleetwood talked with opposing counsel regarding a trial date; noticed but cancelled before taking a deposition; and sent out written discovery requests the day before it moved to compel arbitration. Id. at 694. Gulf argued that this conduct amounted to a waiver by Fleetwood of its right to arbitration. Id. The Court framed the question as "whether Fleetwood impliedly waived arbitration by failing to pursue its arbitration demand for eight months while discussing a trial setting and allowing limited discovery." Id. The Court answered the question no, finding its prior opinion in EZ Pawn Corp. v. Mancias, 934 S.W.2d 87, 90 (Tex. 1996) to be controlling and noting that it had just reaffirmed in Perry Homes the requirement of a non-movant to show prejudice. Id. at 694-95.

b. When can you appeal an order to arbitrate?

In Chambers et al. v. O'Quinn et al., 242 S.W.3d 30 (Tex. Dec. 14, 2007), the Texas Supreme Court set out new law regarding the appeal of trial court orders compelling arbitration. The case had a complicated history. The plaintiffs were former clients of the O'Quinn law firm. Id. at 31. They alleged legal malpractice in the settlement of their toxic tort claims. Id. The firm moved to compel arbitration. Id. The trial court granted the motion to compel. Id. The plaintiffs sought mandamus relief for this ruling from the Court of Appeals and the Texas Supreme Court, both of which denied the appeals without commenting on the merits. Id.

After the appellate courts refused to grant any relief, the trial court directed the plaintiffs to arbitrate by a certain date or have them dismissed. When the plaintiffs failed to demand arbitration, the trial court dismissed his suit for want of prosecution, and the plaintiffs appealed. Id.

"While this appeal was pending, the parties proceeded to arbitration, with the arbitrator ultimately ruling in O'Quinn's favor. Because the trial court had already dismissed his original action, Chambers filed a new suit to vacate the arbitration award. The trial court, however, confirmed the arbitration award, and Chambers perfected a second appeal from this judgment." Id. at 31 (citing Chambers v. O'Quinn, 2006 Tex. App. LEXIS 9006, at *3-4; 2006 WL 2974318, at *1 (Tex. App.—Houston [1st Dist.] Oct. 19, 2006)).

"Both appeals were assigned to the same panel of the First Court of Appeals, but they were not consolidated." Id. The Court of Appeals confirmed the arbitration award and dismissed the appeal of the order compelling arbitration on jurisdictional grounds, concluding that mandamus was the proper remedy to review an order compelling arbitration, that mandamus had already been sought and refused, and thus that it was bound by that prior ruling and thus lacked jurisdiction. Id.

The Texas Supreme Court reversed. The Court held that while mandamus was the appropriate remedy for an order compelling arbitration, it was not the only method for appealing such a ruling. Id. at 32. The Court held:

> Since our decision in Freis, the United States Supreme Court has said that orders compelling arbitration can be reviewed after final judgment in the case. Green Tree Fin. Corp. v. Randolph, 531 U.S. 79, 89, 121 S. Ct. 513, 148 L. Ed. 2d 373 (2000). . . . The writ of mandamus is a discretionary writ, and its denial, without comment on the merits, cannot deprive another appellate court from considering the matter in a subsequent appeal. See In re AIU Ins. Co., 148 S.W.3d 109, 119 (Tex. 2004) (noting that "failure to grant a petition for writ of mandamus is not an adjudication of, nor even a comment on, the merits of a case in any respect, including whether mandamus relief was available"). Thus, the court of appeals has jurisdiction to review the order compelling arbitration in this appeal.

Id.

c. Can you eliminate statutory remedies in an arbitration agreement and when will provisions found to be unconscionable render the entire agreement to arbitrate unenforceable?

In re Poly-America, LP, 2008 Tex. Lexis 770 (Tex. Aug. 29, 2008), the Texas Supreme Court considered whether certain features in an arbitration agreement were unconscionable and if they were, whether the provisions were severable or so pervasive as to render the agreement void in its entirety. In that case, the plaintiff, Johnny Luna, sued his employer in Texas state court, alleging wrongful discharge and retaliation. Id. at *1. However, Luna had twice signed agreements to arbitrate "any and all disputes." Id. at *2. Each arbitration agreement required that:

- all claims be asserted within a year;
- fees be split between the parties with the employee's share capped at one month's gross pay;
- limited discovery;
- confidentiality; and
- no punitives and no reinstatement.

Id. at *2-3.

The court noted that arbitration agreements are not presumed to be more valid than any other contract, but rather are subject to the same rules that apply to all contracts. Id. at *14. To determine whether a contract is invalid for unconscionability, the courts should consider whether "the clause involved is so one-sided that it is unconscionable under the circumstances existing when the parties made the contract." Id. at *15 (quoting FirstMerit Bank, 52 S.W.3d at 757).

Where the arbitration agreement covers statutory claims, however, the arbitration provisions must not "waive the substantive rights and remedies the statute affords"; an employee must be able to "effectively vindicate his statutory rights." Id. at *17. In this case, the plaintiff's claims were covered by the Workers Compensation Act, which specifically entitled a prevailing plaintiff to actual damages (which Texas courts have construed to include punitive damages) and reinstatement of employment. Id. at *18. Thus, the court concluded that the arbitration agreement's elimination of punitive damages and reinstatement were unconscionable. Id. at *26. The Court reasoned as follows:

> In this case, Luna contends Poly-America acted with actual malice in unlawfully discharging him, a claim for which the Workers' Compensation Act allows punitive damages. See TEX. LAB. CODE § 451.002; Azar Nut Co., 734 S.W.2d at 668. Permitting an employer to contractually absolve itself of this statutory remedy would undermine the deterrent purpose of the Workers' Compensation Act's anti-retaliation provisions. In creating the Texas Workers' Compensation Act, the Legislature carefully balanced competing interests – of employees subject to the risk of injury, employers, and insurance carriers – in an attempt to design a viable compensation system, all within constitutional limitations. See Garcia, 893 S.W.2d at 521. Were we to endorse Poly-America's position and permit enforcement of these remedy limitations, a subscribing employer could avoid the Act's penalties by conditioning employment upon waiver of the very provisions designed to protect employees who have been the subject of wrongful retaliation.

Id. at *27-28.

With regard to the fee splitting provisions, the court considered and adopted the approach taken by the majority of other courts around the country:

> We agree that fee-splitting provisions that operate to prohibit an employee from fully and effectively vindicating statutory rights are not enforceable. However, this Court joins the majority of other courts which – though recognizing the same policy concerns articulated by courts holding fee-splitting arrangements per se unconscionable – require some evidence that a complaining party will likely incur arbitration costs in such an amount as to deter enforcement of statutory rights in the arbitral forum.

Finally, with regard to the discovery limitations, the court considered the plaintiff's claim that the limitations made "it virtually impossible for him to prove his claim of retaliatory discharge and render the arbitration agreement unconscionable." Id. at 42. The Texas Supreme Court felt that this was an "issue of first impression" and so considered the rule adopted by courts around the country: "courts refuse to enforce such limitations when adequate evidence is presented that a plaintiff's ability to present his or her claims in an arbitral forum is thereby hindered." Id. at 42. The court refused to adopt this approach, however, reasoning:

We agree with these courts that, where the underlying substantive right is not waivable, ex ante limitations on discovery that unreasonably impede effective prosecution of such rights are likewise unenforceable. However, because the relevant inquiry depends upon the facts presented in a given case and the particular discovery limitations' effect upon the relevant statutory regime, we are doubtful that courts – assessing claims and discovery limitations before arbitration begins – are in the best position to accurately determine which limits on discovery will have such impermissible effect. Id. at 43-44.

The court ruled instead that:

> The assessment of particular discovery needs in a given case and, in turn, the enforceability of limitations thereon, is a determination we believe best suited to the arbitrator as the case unfolds. As with cost-sharing, discovery

> limitations that prevent vindication of non-waivable rights or "prove insufficient to allow [Luna] a fair opportunity to present [his] claims," Gilmer, 500 U.S. at 31, would be unconscionable and thus not binding on the arbitrator, as the agreement in this case specifically acknowledges.

Id. at *45.

As to whether each of these provisions were severable, the Court stuck with its previous holdings that provisions are severable unless they are "integral to the purpose of the agreement" so that they cannot be severed. Id. at *51. The court reasoned:

> We agree with Poly-America that the intent of the parties, as expressed by the severability clause, is that unconscionable provisions be excised where possible. Furthermore, it is clear by the contract's terms that the main purpose of the agreement is for the parties to submit their disputes to an arbitral forum rather than proceed in court. See id. Excising the unconscionable provisions we have identified will not defeat or undermine this purpose, which we have upheld in the context of agreements to arbitrate employment disputes.

Id. at *51-52.

d. Can parties agree in arbitration agreements to expand judicial review?

In Hall Street Associates, LLC v. Mattell, Inc., 128 S. Ct. 1396 (Mar. 25, 2008), the United States Supreme Court considered whether parties could agree in an arbitration agreement to expand the scope of judicial review. After several years of litigation, the parties in Hall Street agreed to arbitrate a claim that had not yet been tried. Id. at 1400. The district court agreed to this approach and approved the parties' written agreement which provided in part that:

> [t]he United States District Court for the District of Oregon may enter judgment upon any award, either by confirming the award or by vacating, modifying or correcting the award. The Court shall vacate, modify or correct any award: (i) where the arbitrator's findings of facts are not supported by substantial evidence, or (ii) where the arbitrator's conclusions of law are erroneous.

Id. at 1400-01.

After arbitration, the losing party filed in the district court a motion for order vacating, modifying and/or arbitrating the arbitration decision. Id. at 1401. The losing party argued that the arbitrator had committed legal error. Id. The district court agreed, vacated the award and remanded back to the arbitrator. Id.

"The [district] court expressly invoked the standard of review chosen by the parties in the arbitration agreement, which included review for legal error, and cited LaPine Technology Corp. v. Kyocera Corp., 130 F.3d 884, 889 (CA9 1997), for the proposition that the FAA leaves the parties "free . . . to draft a contract that sets rules for arbitration and dictates an alternative standard of review." Id. at 1401.

After further back and forth and up and down between the Ninth Circuit and the district court, the United States Supreme Court "granted certiorari to decide whether the grounds for vacatur and modification provided by §§ 10 and 11 of the FAA are exclusive." Id. The court determined that they were. Id.

The court reasoned:

> Instead of fighting the text, it makes more sense to see the three provisions, §§ 9-11, as substantiating a national policy favoring arbitration with just the limited review needed to maintain arbitration's essential virtue of resolving disputes straightaway. Any other reading opens the door to the full-bore legal and evidentiary appeals that can "rende[r] informal arbitration merely a prelude to a more cumbersome and time-consuming judicial review process," Kyocera, 341 F.3d at 998; cf. Ethyl Corp. v. United Steelworkers of America, 768 F.2d 180, 184 (CA7 1985), and bring arbitration theory to grief in post-arbitration process.

Id. at 1405.

Because the FAA preempts state arbitration law wherever issues of interstate commerce are involved, the application of the United States Supreme Court's ruling in Hall Street is likely to bind Texas courts in most instances.

4. FRAUDULENT INDUCEMENT

a. Can you avoid arbitration by claiming fraudulent inducement?

In Forest Oil Corporation et al. v. McAllen et al, 2008 Tex. LEXIS 768 (Tex. Aug. 29, 2008), the Texas Supreme Court considered whether "an unambiguous waiver-of-reliance provision precludes a fraudulent-

inducement claim as a matter of law." Id. at *1. "In 1999, Forest Oil Corporation had settled a long-running lawsuit over oil and gas royalties and leasehold development with James McAllen and others with interests in the McAllen Ranch." Id. at *2. After a week-long mediation, the parties settled the matter. Id. The settlement agreement included a broad release, an express waiver of reliance, and an agreement to arbitrate specific claims, including claims for environmental damage. Id. at *2-3.

Despite this, McAllen sued Forest Oil in 2004 "to recover for environmental damage caused when Forest Oil allegedly 'used its access under the leases to the surface estate to bury highly toxic mercury-contaminated material on the McAllen Ranch.'" Id. at *7. McAllen also alleged that Forest Oil had moved drilling pipe contaminated with radioactive material from the McAllen Ranch to another ranch, which housed a sanctuary for endangered rhinoceroses. Id. at *8.

"Forest Oil sought to compel arbitration under the settlement agreement, but McAllen argued the arbitration provision was induced by fraud and thus unenforceable." Id. at *9. McAllen alleged that an attorney for one of the defendants assured him there would be "no problem" and that Forest Oil knew when the representation was made about the radioactive-contaminated pipe and the mercury-contaminated material. Id. at *10.

In finding for McAllen at the district and appellate court levels, both courts found that there was some evidence to support McAllen's claim of fraud. Id. However, the Texas Supreme Court saw the issue as a legal one and found that McAllen's disclaimer of reliance negated a fraudulent-inducement claim as a matter of law. Id. at *10 and *1. The Texas Supreme Court found its prior decision in Schlumberger v. Swanson controlling, rejecting McAllen's attempts to distinguish that prior holding. Id. at *15-27. The Court reasoned that:

> Refusing to honor a settlement agreement – an agreement highly favored by the law – under these facts would invite unfortunate consequences for every-day business transactions and the efficient settlement of disputes. After-the-fact protests of misrepresentation are easily lodged, and parties who contractually promise not to rely on extra-contractual statements . . . should be held to their word. Parties should not sign contracts while crossing their fingers behind their backs. McAllen accuses Forest Oil of deceit but Forest Oil could make the same allegation against McAllen – who by his own admission and in writing is claiming the opposite now of what he expressly disclaimed then. If disclaimers of reliance cannot ensure finality and preclude post-deal claims for fraudulent inducement, then freedom of contract, even among the most knowledgeable parties advised by the most knowledgeable legal counsel, is grievously impaired.

Id. at *25-26. The Court concluded:

> the arbitration requirement is integral to the overall release and the settlement agreement's waiver-of-reliance language applies by its terms to the parties' commitment to arbitrate. . . . Today's holding should not be construed to mean that a mere disclaimer standing alone will forgive intentional lies regardless of context. We decline to adopt a per se rule that a disclaimer automatically precludes a fraudulent-inducement claim, but we hold today, as in Schlumberger, that "on this record, the disclaimer of reliance refutes the required element of reliance."

Id.

Interestingly, Justices Jefferson and Medina dissented, finding that "under the court's analysis a party may intentionally misrepresent facts essential to the bargain to induce the other to sign, as long as the agreement says reliance is waived." The dissent noted that even in Schlumberger, the Court had held that "a merger clause can be avoided based on fraud in the inducement and that the parole evidence rule does not bar proof of such fraud."

b. Can you avoid the requirement that Rule 11 agreements be in writing by claiming fraudulent inducement?

In Knapp Medical Center v. De La Garza et al., 2007 Tex. LEXIS 1091 (Tex. Dec. 14, 2007) the Texas Supreme Court held that one cannot make a fraudulent inducement claim to circumvent Rule 11's requirement that agreements between counsel be in writing. During the trial of that matter, the parties' attorneys allegedly orally agreed to a settlement that included the defendant's contribution of $200,000 in addition to its insurance policy's limits. Knapp Medical Center v. de la Garza, et al., 238 S.W.3d 767, 767 (Tex. 2007). When the agreement was read into the record, however, the defendant's counsel said that $200,000 additional amount was not part of the deal. Id. at 768. The plaintiff reserved his right to litigate that issue and entered the settlement for policy limits. Id. After judgment was entered, there was a bench trial on the

$200,000 issue. Id. The trial court found for the plaintiff and awarded him attorneys' fees. Id. The defendant appealed. Id. The Court of Appeals affirmed, but the Texas Supreme Court reversed. Id. The Texas Supreme Court held

> "Because the hospital's alleged agreement . . . was neither in writing nor made in open court and entered of record, it is not enforceable. . . . In short, settlement agreements 'must comply with Rule 11 to be enforceable.'"

Id. at 769.

The defendant moved for rehearing, arguing that the Court overlooked his fraud claim. Knapp Medical Center v. De La Garza et al., 2007 Tex. LEXIS 1091 *1 (Tex. Dec. 14, 2007). The defendant contended that the $200,000 representation fraudulently induced him to make a written Stower's demand on the hospital's insurer to settle for policy limits. Id. The Texas Supreme Court rejected this argument as well, stating:

> Texas Rule of Civil Procedure is essentially a 'statute of frauds' for settlement agreements. . . We have previously rejected attempts to 'use a fraud claim essentially to enforce a contract the Statute makes unenforceable' as an improper circumvention of the statute's purpose . . . Thus, we have held that 'the Statute of Frauds bars a fraud claim to the extent the plaintiff seeks to recover as damages the benefit of a bargain that cannot otherwise be enforced because it fails to comply with the Statute of Frauds.' Similarly, a fraud claim cannot be used to circumvent Rule 11 in this manner and thereby enforce an otherwise unenforceable settlement agreement.

Id.

5. CONSPIRACY TO COMMIT FRAUD

In the remarkable case of Chu v. Hong, 249 S.W.3d 441 (Tex. 2008), the Texas Supreme Court held that a lawyer who conspired with a husband to defraud the husband's wife was not liable for damages. In that case, a husband represented himself as the sole owner of a business in documents selling the business to the lawyer's client. The lawyer, Chu, and the lawyer's client knew that the husband was not the sole owner, but the lawyer drafted up the documents; the sale was made; and the husband fled to Korea with the proceeds from the sale. Id. at 446. The wife sued the husband and the lawyer seeking to void the transfer. Id. at 443. The jury ruled for the wife, but the Texas Supreme Court took it all away. Id. The Court held that under settled Texas law, a spouse cannot sue another spouse in tort for damage to the community. Id. at 444. Because Texas law does not recognize an independent tort for the wrongful disposition of community assets by a spouse, the lawyer could not be liable for conspiracy. Id.

While the outcome may first appear surprising, Justice Brister begins the opinion with a reasonable explanation:

> "A spouse who gives away community property to friends or relatives when divorce is imminent has defrauded the community estate. In such cases, a trial court can order the spouse to return the property or take the fraud into account in making a just-and-right division.
>
> But in this case the trial court did neither. After finding a husband sold community property to third parties without his wife's consent, the trial court ordered the buyers to return the property to the wife but allowed the husband to keep the money they paid for it, and added a judgment against the buyers and their lawyer for more than $1.75 million. Thus, because one spouse defrauded the other, both are better off and the community estate vastly increased. We hold the courts below erred in allowing one spouse to recover damages without first recovering the community property from the spouse who took it."

Id. at 442-43

The Court also noted that the claim against Chu, the opposing attorney was particularly inappropriate, because the attorney had a duty to further the best interests of his clients, the buyers. Id. at 446. Thus, concluding: "We need not approve of Chu's ethics to hold that Schleuter requires Hong to seek restitution from her own husband before seeking it from someone else's lawyer."

6. PARTNER LIABILITY

In Kao Holdings, LP et al. v. Young, 61 S.W.3d 60, 2008 Tex. LEXIS 572 (Tex. June 13, 2008), the Texas Supreme Court held that a partner cannot be liable for a default judgment unless he was named and served as a defendant individually. In that case, the plaintiff "sued Kao Holdings, LP for damages, alleging that it owned the Sebring Apartments where she was living when she fell in the laundry room and injured her hip." Id. at 1. The plaintiff did not name the partnership's general partner, Mr. Kao, as a defendant

"but served the partnership by serving him." Id. However, when the partnership failed to answer, the plaintiff moved for a default judgment against the partnership and Mr. Kao individually. The district court entered an award against both, and the "court of appeals affirmed the liability portion of the judgment, holding that judgment against Kao individually was proper, even though he was not a party, because he was Kao Holdings' general partner and the person to whom citation on the partnership was delivered." Id. at *1-2.

The Texas Supreme Court reversed. Mr. Kao argued "that judgment could not be rendered against him individually when he was neither named nor served as a party." Id. at *2. The Court agreed. The Court explained that the holding was required not just by "fundamental concepts of due process," but also by Rules 124 and 239 of the Texas Rules of Civil Procedure and Section 17.022 of the Texas Civil Practice and Remedies Code. Rule 124 states that "[i]n no case shall judgment be rendered against any defendant unless upon service . . . except where otherwise provided by law or these rules." Id. at *2-3. The plaintiff argued and the Court of Appeals had agreed that Section 17.022 of the Texas Civil Practice and Remedies code provided the exception. Id. at *3. That section provides that "[c]itation served on one member of a partnership authorizes a judgment against the partnership and the partner actually served." The Texas Supreme Court reviewed the history of the Rule and determined that it was applicable in a suit against a partner, in order to hold judgment against the partnership but not vice versa. Id. at *4-6. The Court also noted that Rule 239 of the Texas Rules of Civil Procedure provides for default judgment only against 'a defendant.'" Id *11-12. Because Mr. Kao was not a defendant, the Court held that a default judgment could not be entered against him. Id. *12.

7. EMPLOYMENT DISCRIMINATION

In City of Waco v. Lopez, 259 S.W.3d 147 (Tex. 2008), the Texas Supreme Court held that where two statutory schemes cover the same conduct, but one is more specific, a plaintiff must proceed under the more specific scheme. The plaintiff, Robert Lopez, filed an EEO complaint, alleging that his supervisor had discriminated against him on the basis of age and race. Id. at 149. About six weeks later, the City terminated Mr. Lopez, asserting that he had violated City policy. Id. Mr. Lopez then sued, asserting a retaliation claim under the Whistleblower Statute. Id. at 149-50. The City filed a plea to the jurisdiction, arguing that the CHRA was the exclusive remedy for Lopez's retaliatory discharge claim. Id. at 150. "The trial court denied the City's plea to the jurisdiction, and a divided court of appeals affirmed." Id.

The Texas Supreme Court held that the key question was "whether the Legislature intended to allow a claimant to elect between two remedial schemes addressing essentially the same conduct but providing different procedures and remedies." Id. at 153. "Whether a regulatory scheme is an exclusive remedy depends on whether 'the legislature intended for the regulatory process to be the exclusive means of remedying the problem to which the regulation is addressed.'" Id. The Court noted that the Court of Appeals to have considered the issue were split. Id. The court held: "Because the statutes provide irreconcilable and inconsistent regimes for remedying employer retaliation, and the CHRA is focused precisely on combating the discrimination-rooted retaliation of which Lopez complains, the more specific and comprehensive anti-retaliation remedy in the CHRA forecloses relief under the more general Whistleblower Act." Id. at 154. The Court explained: "If a public employee had the option to pursue a retaliation claim under either the Whistleblower Act or the CHRA pursuit of the former would render the limitations in the CHRA utterly meaningless as applied to public employees. Such breadth must not be permitted to defeat CHRA's comprehensive statutory scheme." Id.

The Court thus concluded that the CHRA provides the exclusive state statutory remedy for public employees alleging retaliation arising from activities protected under the CHRA. Id. at 156.

In Montgomery County, Texas v. Park, the Texas Supreme Court defined what "adverse" means when determining whether a plaintiff who alleges retaliation under the Whistleblower Act suffered "adverse personnel action." In that case, the Commissioner reported alleged sexual harassment to the sheriff. Before the report, the Commissioner had the authority to assign officers (including himself) to provide security for the Montgomery County Lone Star Convention Center for extra pay. After the report, the responsibility for assigning officers moved back and forth between the Sherriff's office and the Constable's office. The Commissioner alleged that this was retaliation. The Texas Supreme Court held: "We hold that a personnel action is adverse within the meaning of the Whistleblower Act if it would be likely to dissuade a reasonable, similarly situated worker from making a report under the Act." The Court then determined that Park did not suffer any adverse action in his case because "there is no evidence that the ability to assign himself convention center jobs actually increased Park's access to extra work and thus indirectly his compensation."

The court concluded that: "applying the objective standard . . ., we conclude that Park's loss of the first choice of convention center jobs would not, as a mater

of law, be likely to deter a similarly disturbed reasonable employee from reporting a violation of the law and thus was not materially adverse."

8. CLASS ACTION

In DaimlerChrysler Corporation v. Inman, et al., 252 S.W.3d 299 (Tex. 2008), the Texas Supreme Court set out the minimum standard a class representative must meet in order to have standing to bring the action on behalf of the class. In DaimlerChrysler, three named plaintiffs brought a class action lawsuit against DaimlerChrysler, alleging that seat belt buckles were too easily unlatched and should be replaced with ones that are harder to unlatch. Id. at 300. "Two of the plaintiffs had never experienced anything like what they claimed might happen, and the third is not sure whether he has or not, but he has never been injured." Id. DaimlerChrysler argued that "the plaintiffs' fear of possible injury from an accidental release of a seatbelt is so remote that they lack standing to assert their claim." Id. at 301. In a 5-4 decision, the Supreme Court agreed.

The majority reasoned that concrete injury is required for standing, because "if injury is only hypothetical, there is no real controversy" and held that to "hold that [the three plaintiffs] have standing would drain virtually all meaning from the requirements that a plaintiff must be 'personally aggrieved' and that his injury must be 'concrete' and 'actual or imminent.'"

The dissent criticized the majority for "inverting traditional standing doctrine, focusing not on the party but on the issues to be adjudicated." Id. at 308. The dissent argued that the "law on warranty claims based on unmanifested defects is unclear" so that "[a]bsent a full record, in which the claim's contours can be thoroughly vetted, [the court should not] say the plaintiffs' claims of economic injury are conclusively unsound." Id. at 309. The dissent suggested the majority was reaching merits-based issues in the guise of a jurisdictional analysis, noting that "[w]e have never before held that any time a plaintiff's claims fail as a matter of law, the trial court is deprived of jurisdiction." Id. at 313.

9. JURY INSTRUCTIONS

On December 21, 2007, the Texas Supreme Court issued its opinion in Ford Motor Co. v. Ledesma, 242 S.W.3d 32 (Tex.) and held that the Texas Pattern Jury Charge's definition on manufacturing defect is erroneous and should no longer be used.

In Ledesma, the trial court followed Texas Pattern Jury Charge 71.3 for the definition of design defect. Id. at 41. The Texas Supreme Court held that the charge was erroneous because it "omitted an indispensable element: that the produce deviated, in its construction or quality, from its specifications or planned output in a manner that rendered it unreasonably dangerous." Id. at 42. The Court reasoned:

> The requirement of a deviation from the manufacturer's specifications or planned output serves the essential purpose of distinguishing a manufacturing defect from a design defect. . . . The distinction is material. The danger of allowing a jury to conclude that the defect was or might have been a design defect is that 'a design defect claim requires proof and a jury finding of a safer alternative design.' The charge did not make such an inquiry.

Id.

The Court also concluded that Texas Pattern Jury Charge 70.1, which defines producing case should no longer be used. Id. at 45. PJC 70.1 states "'Producing cause' means an efficient, exciting, or contributing case that, in a natural sequence produces the incident in question. There may be more than one producing cause." Id. There was no dispute about the second sentence. Id. However, Ford contended that the first sentence should require producing cause to be a "substantial factor in bringing about an event . . .without which the event would not have occurred." Id. The Texas Supreme Court agreed, found the pattern jury charge incomplete, the words "efficient" and "exciting" as "foreign to modern English language" and thus the charge providing "little concrete guidance" to a jury. Id. at 46. The Court thus concluded that the "definition that should be given in the jury charge" must convey "the essential components of producing cause that (1) the cause must be a substantial cause of the event in issue and (2) it must be a but-for cause, namely one without which the event would not have occurred." Id.

10. ATTORNEYS FEES

a. Can you get attorneys fees on a breach of express warranty claim?

In Medical City Dallas, Ltd. v. Carlisle Cor., 251 S.W.3d 55, 57 (Tex. 2007), the Texas Supreme Court considered whether a prevailing plaintiff on an action for breach of express warranty is entitled to attorneys fees. In that case, the plaintiff Medical City had contracted with Carlisle for roofing repairs. Id. Carlisle gave Medical City an express warranty. Id. After a few years of continuous problems with the roof, Medical City sued for breach of that express warranty. The jury came back with a verdict in favor of the plaintiff that included attorneys fees. Id.

The Court of Appeals reversed the attorneys fee award, reasoning that Texas Civil Practice and

Remedies Code section 38.001(8), which allows fees for claims based on oral or written contracts, did not encompass breach of warranty claims. 196 S.W.3d 855, 868-72. Id. at 58. It noted that Medical City did not plead or try a breach of contract cause of action and did not recover on that theory. Id.

The Texas Supreme Court "granted the [plaintiff's] petition to decide whether a party who prevails in a breach of express warranty action is entitled to attorney's fees." Id. at 61. The court recognized that breach of express warranty is a claim distinct from breach of contract, but held that "it is nonetheless a part of the basis of a bargain and is contractual in nature." The Court noted that it "is the result of a negotiated exchange," "is a 'creature of contract,'" that when courts "ascertain the parties' intentions in a warranty, we look to well-established rules for interpretation and construction of contracts," and that "a breach of express warranty claim, like one for breach of contract, involves a party seeking damages based on an opponent's failure to uphold its end of the bargain;" and the damages sought in each claim are the same. Id. at *61-62. The court thus concluded:

> Because Texas Civil Practice and Remedies Code section 38.001(8) permits an award of attorney's fees for a suit based on a written or oral contract, and because we conclude that breach of an express warranty is such a claim, the court of appeals erred in reversing Medical City's attorney's fees award in connection with its successful claim for breach of an express warranty.

Id. at *63.

b. Must attorney fee agreements include a total price for services?

On July 11, 2008, a unanimous Texas Supreme Court "reversed a decision by Houston's 1st Court of Appeals and reinstated Harris County Court-at-Law No. 2's judgment awarding the Sack's Firm in Houston and its president, David J. Sack's, $30,214 on the firm's breach of contract claims against [a former client]. The high court's decision also reinstated the court-at-law's judgment awarding Sacks and his firm about $120,000 in attorneys' fees incurred in pursing the contract claims against the former client." Mary Alice Robbins, Lawyer Wins Fee Fight with former Client at Supreme Court, Texas Lawyer, July 21, 2008 at 5.

In a 2-1 decision, the 1st Court of Appeals held that because the fee agreement was silent as to whether the parties had agreed to an open account or a flat maximum fee, the defendant could present evidence of an oral agreement capping the attorney's fees. Id. at 6. The Supreme Court disagreed. The Supreme Court held that the fee agreement was unambiguous and the failure to include a total price for services did not "indicate failure of the parties to reach a meeting of the minds." The court explained that "the lack of such explicit language is irrelevant if the agreement can be reasonably interpreted only one way. . . . We have never held that an open-ended hourly fee agreement will be enforced only if it expressly states that there is no cap on fees and we decline to do so now." And with that, tens of thousands of attorneys who regularly enter into hourly fee agreements with thousands of clients breathed a collective sigh of relief!