

ORIGINAL

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM DORCHESTER COUNTY
Court of Common Pleas

Edgar Warren Dickson, Circuit Court Judge

Case No. 2009-CP-18-1601

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SC Court of Appeals

DAVID AND BRIDGETTE MANNING,
INDIVIDUALLY AND AS LEGAL GUARDIANS OF
TATE M. AND COLBY M
BOTH MINORS LESS THAN 18 YEARS OF AGE..... Respondents.

v.

LENNAR CAROLINAS, INC., DON GALLOWAY
HOMES, LLC AND LENNAR COMMUNITIES
OF THE CAROLINAS, INC..... Appellants.

FINAL REPLY BRIEF OF APPELLANTS

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The disposition of this appeal will signal whether arbitration remains a viable means of dispute resolution in this state. In declining to enforce an arbitration agreement between a purchaser and a builder for the design, construction, and sale of a residence, the lower court refused to apply federal arbitration law, overlooked the nature of the underlying dispute, and expanded the unconscionability doctrine well beyond its prior bounds. Nothing Respondents state in their opposition brief refutes those points.

ARGUMENT

I. THE LOWER COURT ERRED BY DECLINING TO APPLY THE FEDERAL ARBITRATION ACT (“FAA”).

Respondents disagree that the lower court should have applied the FAA. However, this position overlooks that (1) the parties expressly stipulated that the arbitration provisions would fall within the coverage of FAA, (2) the purchase and construction of the subject residence involved interstate commerce, and (3) the FAA and general state law principles are not mutually exclusive in a court’s evaluation of the enforceability of arbitration clauses. Each of these points will be addressed *seriatim*.

A central purpose of the FAA is to enforce arbitration agreements. *Munoz v. Green Tree Financial Corp.*, 343 S.C. 531, 540-41, 542 S.E.2d 360, 364 (2001). As a result, courts rigorously give effect to the contractual rights and expectations of the parties and resolve every doubt in favor of arbitration. *Volt Info. Scis. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 476, 109 S.Ct. 1248 (1989) (The FAA “requires courts to enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms.”); *Zabinski v. Bright Acres Assocs.*, 346 S.C. 580, 553 S.E.2d 110, (2001) (federal and state policy strongly favor arbitration). Where, as here, the parties’ contract expressly stipulates that the FAA will apply, courts are

required to enforce the stipulation. *See, e.g., Munoz*, 343 S.C. at 539, 542 S.E.2d at 364 (overturning trial court’s refusal to apply the FAA to parties’ agreement, which stated that “this contract and the relationships which result from this contract” are to be governed by the FAA).

Even if the arbitration agreement did not expressly stipulate that the FAA applies, which it does, the FAA must apply based on the extensive and undisputed evidence of interstate commerce,¹ including out-of-state parties, materials, and suppliers, and a legal presumption that construction involves interstate commerce. *New Hope Missionary Baptist Church v. Paragon Builders*, 379 S.C. 620, 626-27, 667 S.E.2d 1, 4 (Ct. App. 2008) (affirming trial court’s determination that FAA applies where arbitration agreement “pertains to a transaction involving interstate commerce due to the nature of the construction project” and affidavits demonstrated that the construction project required the infusion of out-of-state businesses and supplies). Based on the undisputed evidence of interstate activity and the legal presumption of such activity in the construction context, the lower court was compelled to apply the FAA.

Although Respondents appear to concede the interstate nexus, they argue that federal arbitration law is nevertheless irrelevant to the dispute. A review of *Herron v. BMW*, 387 S.C. 525, 530, 693 S.E.2d 394, 397 (2010), *vacated by Sonic Auto. Inc. v.*

¹ Respondents’ allegation that the Affidavit of David Murphy fails for lack of personal knowledge was neither raised nor ruled on by the lower court and, consequently, is not properly before this Court. *See State v. NV Sumatra Trading Co.*, 379 S.C. 81, 666 S.E.2d 218 (2008) (refusing to entertain issue of insufficient authentication of affidavit on appeal where argument was not raised in any submission to lower court); *Poch v. Bayshore Concrete/South Carolina, Inc.*, 386 S.C. 13, 686 S.E.2d 689 (Ct. App. 2009) (declining to exclude affidavit from consideration where issue was not preserved for appellate review). The same reasoning precludes consideration of Respondents’ merger by deed argument, which is raised for the first time in their opposition brief and is unsupported by the record evidence.

Watts, 131 S.Ct. 2872 (2011), *original opinion reinstated by* 395 S.C. 461, 719 S.E.2d 640 (2011), and *Munoz*, 343 S.C. at 539, 542 S.E.2d at 364 confirms that the lower court was required to determine, as a threshold matter, whether the FAA applied, so that it knew the extent to which state law might be considered. For these reasons, the lower court erred by declining to apply the FAA.

II. THE LOWER COURT ERRED BY DETERMINING THAT THE NEGLIGENCE, WARRANTY AND OTHER CLAIMS FALL OUTSIDE THE SCOPE OF THE ARBITRATION AGREEMENT.

Because Respondents have asserted no breach of contract claim, they contend that the arbitration provisions within the parties' pre-construction agreement do not cover their claims for negligence, warranty, unfair trade practices, and personal injury.

Pursuant to our Supreme Court's reasoning in *Zabinski*, 346 S.C. at 597-98, 553 S.E.2d at 119, tort claims that relate to the underlying contract are arbitrable. Citing *Zabinsky*, this Court has stated that "[a] broadly-worded arbitration agreement applies to disputes that do not arise under the governing contract when a 'significant relationship exists between the asserted claims and the contract in which the arbitration clause is contained.'" *Partain v. Upstate Automotive Group*, 378 S.C. 152, 156, 662 S.E.2d 426, 428-29 (Ct. App. 2008).

Here, the arbitration provisions provide, in pertinent part, that:

ALL CLAIMS, CONTROVERSIES, OR DISPUTES . . . ARISING OUT OF OR RELATING TO THIS CONTRACT, THE BREACH THEREOF, AND ALL CLAIMS RELATING TO THE CONSTRUCTION OF THE SUBJECT RESIDENCE, OR OF ANY OTHER KIND, SHALL BE SETTLED BY ARBITRATION.

(R. p. 167) (emphasis in original). The plain language of the arbitration provisions neither limits the scope to contract claims nor excludes the arbitration of tort claims. On

the contrary, “all claims relating to the construction of the subject residence” fall within the express scope of the arbitration provisions. (R. p. 167; R. p. 143, lines 7-24).

While Respondents assert no contract claims, Respondents’ claims undoubtedly relate to the parties’ pre-construction contract for a single-family residence. Specifically, the Complaint alleges that Respondents’ injuries result from a failure “to design and/or construct the Subject Residence in accordance...with the approved construction plans and specifications.” (R. pp. 14, 16-17). The alleged construction defects include the alleged failure of structural systems, inadequate flashing, improperly installed siding, roofing, and exterior cladding, and improper site preparation. Simply casting a claim as a tort as an “end-run” around an arbitration provision is insufficient to avoid a contractual agreement to arbitrate. *See Partain*, 386 S.C. at 494-95, 689 S.E.2d at 605; *Aiken v. World Fin. Corp. of S.C.*, 373 S.C. 144, 152, 644 S.E.2d 705, 709 (2007) (“[A] tort claim which essentially alleges a breach of the underlying contract...would be within the contemplation of the parties in agreeing to arbitrate.”).

Even if the tort claims did not relate to the contract, which they do, it is undisputed that they “relat[e] to the construction of the subject residence.” (R. p. 167). To confirm, this Court need look no further than Respondents’ and the lower court’s own characterization of the claims. The Complaint states that “[t]his matter arises out of the design, development, construction and sale of the Subject Residence” (R. p. 13), and the first line of Respondents’ brief states “[t]his is a construction defect case,” (Respondents’ Initial Brief, p. 1). Furthermore, the first page of the Order states “[t]his case arises out of alleged construction defects to a single-family home in Summerville, South Carolina.” (R. p. 3). Thus, the underlying allegations and the remedies sought,

whatever the legal label used, derive from the parties' written agreement for residential construction.

On similar facts, a local federal court held that claims seeking relief for personal injuries allegedly suffered due to improper construction of condominium had a "significant relationship" to the arbitration agreement so as to require the submission of the case to arbitration. *See Osborne v. Marina Inn at Grande Dunes, LLC*, No. 0490, 2009 WL 3152044, at *7-8 (D.S.C. Sept. 23, 2009) (determining condo purchaser's tort claims, including negligence causing personal injury as a result of mold damage, were related to construction defects and subject to arbitration agreement); *see also Palmetto Homes, Inc. v. Bradley*, 357 S.C. 485, 593 S.E.2d 480 (Ct. App. 2004) (finding negligence claims stemming from allegedly defective installation of masonry fell within the scope of arbitration provision). Accordingly, regardless of the legal labels attached to the dispute (*i.e.*, tort or breach of contract), a significant relationship exists between the unfair trade practice, warranty, negligence, and personal injury claims and the operative agreement.

III. THE LOWER COURT ERRED BY DETERMINING THAT THE ARBITRATION PROVISIONS ARE UNCONSCIONABLE.

The lower court determined that the arbitration agreement is unconscionable based on a single South Carolina state court decision that stands in sharp contrast with this matter. Indeed, the factual findings underpinning the lower court's determination fall well short of establishing "the absence of meaningful choice on the part of one party, due to one-sided contract provisions, together with terms that are so oppressive that no reasonable person would make them and no fair and honest person would accept them,"

as South Carolina law requires to invalidate an arbitration agreement as unconscionable.

Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 25, 644 S.E.2d 663, 668 (2007).

A. RESPONDENTS DID NOT LACK MEANINGFUL CHOICE IN ENTERING INTO THE AGREEMENT.

In the decision below, the court concluded that Respondents had no meaningful choice in agreeing to arbitrate claims based on the following findings: (1) Appellants are relatively sophisticated business entities; (2) Respondents are first-time homebuyers; and (3) the terms of the arbitration clauses are contained in a dense agreement. (R. pp. 6-7).²

The parties' contract for construction of a single-family residence is markedly different from the agreement and surrounding circumstances in *Simpson* — the one located decision in which the appellate courts of our state have deemed an arbitration clause to be unconscionable. As the Supreme Court explained in *Herron*, 387 S.C. at 533, 693 S.E.2d at 398, “the *Simpson* arbitration agreement was inconspicuously buried in the sales contract, on the opposite page from the customer’s signature, in paragraph ‘10’ of sixteen other paragraphs. Additionally, the *Simpson* customer alleged the contract was ‘hastily’ presented for her signature.”

By contrast, the instant arbitration agreement, like that in *Herron*, “is clearly labeled to be an arbitration agreement at the top of the document in bold, capital, and underlined font. The important terms and provisions of the agreement appear in the body

² The lower court did not find the subject agreement to be an adhesion contract. Nor did the court make any other factual findings with respect to the meaningful choice prong of the two-part unconscionability test. *FoodMart v. South Carolina Dept. of Health & Envtl. Control*, 322 S.C. 232, 471 S.E.2d 688 (holding matters not argued to or ruled on by the trial court are not preserved for appellate review and are procedurally barred). Respondents discuss such issues, but the Order plainly shows that the lower court did not rule on such issues. *Elam v. South Carolina Dept. of Trans.*, 361 S.C. 9, 24, 602 S.E.2d 772, 780 (2004) (“A party must file [a Rule 59(e) motion] when an issue or argument has been raised but not ruled on, in order to preserve it for appellate review.”).

of the contract [and] above the signature line.” *Id.*; (See R. p. 167).³ Indeed, the lower court commented on the record as follows:

I have a one page contract that at the top say it’s subject to arbitration, and then it says, see Paragraph Seven. And Paragraph Seven takes up twenty percent of the front page and it’s underlined in big letters and says, y’all arbitrating. That’s what it says to me.

(R. p. 157, lines 10-14).⁴ Clearly, the evidence does not reasonably support the finding that the arbitration provisions are contained in a dense agreement.

³ Respondents claim they were surprised by the arbitration provisions. The lower court made no such finding. However, to the extent this Court entertains this allegation, it is important to note that contrary to Respondents’ assertion, there should be no element of surprise with regard to the arbitration provisions because they are clear, conspicuous, and unambiguous. (See R. pp. 167). Moreover, the parties owe a duty to each other and to the public to learn the contents of documents before they sign the contract. *See Regions Bank v. Schumach*, 354 S.C. 648, 663, 582 S.E.2d 432, 440 (Ct. App. 2003). In addition, Respondents concede an attorney dually represented the parties in the residential closing and that the attorney owed both parties a fiduciary obligation. *See* Respondants’ Initial Brief at pp. 3, 13. If Respondents had preferred an alternative attorney, there is no evidence that they were prevented from retaining him or her. The record is also clear that Respondents were represented by an independent real estate agent in connection with the execution of the agreement as demonstrated by the agent’s signature on the agreement. (See R. p. 138; R. p. 167). As a result, the overwhelming evidence shows that Respondents had every opportunity to review and understand the arbitration provisions.

⁴ The arbitration provisions are the only bolded and emphasized terms on the face of the contract. *Id.* Courts routinely enforce arbitration provisions with the same amount of, or even less, emphasis. *See, e.g., Munoz* 343 S.C. at 536, 542 S.E.2d at 362 (holding not unconscionable arbitration agreement that was neither bolded nor underlined); *Lucey v. Meyer*, No. 4960, 2012 WL 1020984 (Ct. App. March 28, 2012) (compelling arbitration in spite of claims of unconscionability where arbitration provision appeared in regular type and was not bolded, capitalized or underlined); *Lackey v. Green Tree Fin. Corp.*, 330 S.C. 388, 498 S.E.2d 898 (Ct. App. 1998) (determining arbitration provision that was capitalized but not underlined or bolded was not unenforceable as unconscionable); *Osborne*, 2009 WL 3152044, at *2 (finding arbitration provision in capital, bold and underscored print on first page of purchase and sale agreement of new home to be enforceable and not unconscionable).

Nor is there any allegation or evidence that the contract was “hastily” presented. On the contrary, Respondents reviewed the contract overnight and decided upon various construction items such as the type of garage, foundation, and exterior cladding they specified for their residence. (See R. pp. 167; R. p. 137). In fact, the second page of the contract is replete with their “Sales Contract Specifications.” (See R. p. 168). The inescapable conclusion based on these facts is that Respondents had a meaningful choice in making the decision to enter into this contract. See *Lucey v. Meyer*, No. 4960, 2012 WL 1020984, (Ct. App. Mar. 28, 2012) (reversing trial court’s determination that arbitration agreement contained in employment contract was unconscionable where party had unequal bargaining power but sufficient time to review and accept the terms).

B. THE TERMS OF THE ARBITRATION PROVISIONS ARE NEITHER ONE-SIDED NOR OPPRESSIVE.

Nor can Respondents point to any oppressive, one-sided terms justifying the lower court’s decision. In *Lucey*, this Court reiterated that “this prong of the test [requires that] no reasonable person would make [the terms] and no fair and honest person would accept them.” 2012 WL 1020984 at *10. The *Simpson* agreement satisfied this prong, but it differs significantly from the arbitration agreement at issue here.⁵

“The arbitration provision in *Simpson* required the customer to waive her right to punitive damages and double and treble compensatory damages.” *Herron*, 387 S.C. at 534, 693 S.E.2d at 399. Nothing in the parties’ agreement prevents the arbitrator from awarding double or treble damages. (See generally R. p. 167). Nor does any provision

⁵ *Simpson* represents the only located appellate case in South Carolina finding the terms of an arbitration agreement to be unduly and overly one-sided and biased.

prohibit the award of punitive damages. There are simply no limitations on damages whatsoever.

Far from being unconscionable, certain provisions favor Respondents. For instance, Respondents are permitted to participate in the selection of the arbitral venue and are not obligated to arbitrate in a location that would be potentially inconvenient to them. (Construction Industry Arbitration Rule R-12). Moreover, based on the terms of the provision, an unbiased arbitrator will decide the parties' dispute in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association ("AAA"), which is universally recognized as a full service provider of alternative dispute resolution. *McMullen v. Meijer, Inc.*, 355 F.3d 485 (6th Cir. 2004) (finding AAA to be a neutral, non-profit public service organization that provides unbiased dispute resolution services); *Andrews v. Education Ass'n of Cheshire*, 829 F.2d 335 (2nd Cir. 1987) (same). Respondents are expected to participate in the selection of the AAA arbitrator, and the parties are to bear the costs of arbitration equally. (Construction Industry Arbitration Rules R-14, 53 and 54).

Nevertheless, Respondents argue that the arbitration provisions grossly favor Appellants by allowing them to pursue certain equitable relief in a judicial forum. (Respondents' Initial Brief, pp. 14-15).⁶ This argument overlooks the fact that South Carolina law imposes no mutuality of remedy requirement. *See Munoz*, 343 S.C. at 542, 542 S.E.2d at 365; *Lackey* 330 S.C. at 402, 498 S.E.2d at 905; *Alala v. Peachtree Plantations, Inc.*, 292 S.C. 160, 355 S.E.2d 286 (Ct. App. 1987) (allowing one party an

⁶ The Agreement states that Appellants "may bring an equitable judicial proceeding against [Respondents] for an injunction or specific performance..." (R. p. 167).

exclusive remedy to compel property purchase does not invalidate the agreement for lack of mutuality).

Unconscionability arises only when a party's reservation of judicial remedies completely undermines the other party's ability to arbitrate. *Simpson*, 373 S.C. at 32, 644 S.E.2d at 672 (arbitration agreement was unconscionable where dealer could repossess a vehicle and collect a civil judgment from owner before the owner could even arbitrate its rights in the same vehicle). Allowing Appellants to file a motion for a preliminary injunction or specific performance in state court does not undermine Respondents' ability to pursue their claims in arbitration.⁷

"A party desiring to avoid an arbitration clause on the grounds that no reasonable person would have agreed to it merely because it precludes judicial remedies must demonstrate how he or she has been prejudiced by compelled arbitration. This requires, at the very least, identification of judicial relief not available in arbitration." *Id.* Respondents have not identified any judicial relief not available in arbitration. Indeed, Respondents have not been "deprived of a remedy – they simply must seek their remedy through arbitration rather than through the judicial system." *Munoz*, 343 S.C. at 342, 542 S.E.2d at 365. Thus, the limited judicial carve-out should not have invalidated the arbitration agreement.

⁷ The lower court's conclusion ignores the realities of business risks. Appellants retained the option to use judicial relief to seek to enforce a pre-construction agreement through equitable means. Such an option is a business necessity where, as here, the residence was being built to Respondents' express specifications. (*See R.* pp. 168-170). Carving out an exception for equitable relief is also necessitated by the fact that such relief could only be obtained through the courts. *See Lackey* 330 S.C. at 402, 498 S.E.2d at 905 (reversing trial court's determination that arbitration agreement was unconscionable where the relief reserved could only be obtained judicially).

Respondents' argument that the contractual language in Paragraph 10 invalidates the arbitration provisions in Paragraph 7 is also without merit. Paragraph 10 states as follows:

The written text of this Purchase Agreement, any addendum, sales contract specifications, and the attached Standard Provisions represent the complete intent and understanding of the parties involved. There are no other promises, representations, or guarantees, either verbal or written, other than what are contained in the Purchase Agreement's Special Stipulation Section #6, any addendum, sales contract specifications or in the Standard Provisions.

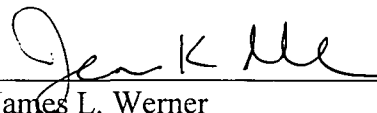
(R. p. 167). The lower court concluded that this merger language excludes implied warranties and therefore renders the arbitration agreement unconscionable.

If the foregoing language disclaims warranties, as the lower court decided, it applies with equal force in judicial and arbitral forums. In other words, both an arbitrator and a trial court would be required to enforce the disclaimers. Thus, Respondents are able to get "the same relief in arbitration which is [or is not] available in a judicial setting," such that Respondents are not prejudiced by compelled arbitration. *Lackey*, 330 S.C. at 400-01, 498 S.E.2d at 905 (reversing trial court's invalidation of arbitration agreement where respondents failed to demonstrate that remedies available in court are foreclosed to them in arbitration).

In light of the foregoing, there is simply no basis to conclude that the arbitration provisions are oppressive, one-sided, and not geared toward achieving an un-biased decision by a neutral decision-maker. In conjunction with the evidence of meaningful choice in agreeing to arbitrate, these provisions are not an unconscionable waiver of any judicial rights and are therefore enforceable.

CONCLUSION

For the reasons in Appellants' initial and reply briefs, the lower court erred by denying Appellants' Motion to Stay and Compel Arbitration.



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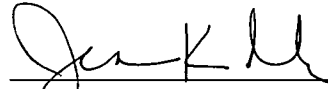
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The undersigned hereby certifies that the Final Reply Brief of Appellants
complies with Rule 211(b), SCACR.



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CERTIFICATE AND PROOF OF SERVICE

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