THE INTERSECTION BETWEEN ARBITRATION AND LITIGATION IN TEXAS

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CHAPTER 7

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SELECTED PUBLICATIONS AND SPEECHES

- "The New World of Unpublished Appellate Decisions as Precedent," 2007 ABA Annual Meeting
- "Marketing the Appellate Practice," 2005 ABA Annual Meeting
- "What Clients Want: The In-House Counsel's View of Appellate Specialists," CAL/AJEI Summit, 2004
- "Federal Appellate Review of Decisions of Trial Court Before Final Judgment on All Claims," 17 Fifth Circuit Reporter 577
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Contributing Editor, *Yale Law Journal*, 1996-98
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AWARDS AND HONORS

Selected as a "Rising Star" by *Law and Politics* and *Texas Monthly* magazine in 2004-2007.
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SELECTED PROFESSIONAL ACHIEVEMENTS

- Persuaded the Texas Supreme Court to strike down the Texas public school finance system on constitutional grounds. *Neeley v. West Orange-Cove C.I.S.D.*, 176 S.W.3d 746 (Tex. 2005). This decision was the culmination of a four and one-half year effort, including a previous successful appeal to the Supreme Court and a successful five-week bench trial upon remand. *West-Orange Cove C.I.S.D., v. Alanis*, 107 S.W.3d 558 (Tex. 2003).

- Obtained reversal of class certification in a suit where appellees were authorized to represent a class of hundreds of thousands of Texas-based music club members who sought recovery of the late fees they had paid on their compact disc purchases. *BMG Direct Marketing, Inc. v. Peake*, 178 S.W.3d 763 (Tex. 2005).

- Successfully persuaded trial court to reconsider and withdraw summary judgment dismissing client's multi-million dollars claims. Obtained summary judgment against adversary's multi-million dollar counterclaims. Ultimately obtained very favorable settlement for client. *Jerral W. Jones. v. Sanford Brass*, No. 99-01743, in the 113th District Court of Harris County.

RECENT PUBLICATIONS:

- "*Webcasts Open a Window to Texas Supreme Court,"* Op-ed, Houston Chronicle, Mar. 30, 2007.
- "*Risky Business: Altering the Scope of Judicial Review of Arbitration Awards by Contract*," Texas Bar Journal, Vol. 69, No. 9 (October 2006).
- "*Arbitration-Related Litigation and Appeals,"* Advanced Civil Appellate Practice Course, State Bar of Texas (September 2006).
- "*Texas Supreme Court Update*," State Bar College Summer School (July 2005) (co-author)
- "*The Class Action Fairness Act of 2005: The Federalization of Class Actions*," The Appellate Advocate (Spring 2005).

SELECTED PRESENTATIONS:

- "*Arbitration-Related Litigation and Appeals,"* Advanced Civil Appellate Practice Course, State Bar of Texas (September 2006).
- *"A Toolbox for Complex Litigation"* – Panelist, HBA's Law & the Media 20th Annual Seminar (Feb. 25, 2006).
- *"Business Development and Marketing for the Appellate Lawyer,"* Panelist, HBA Appellate Section Lunch (September 28, 2005)
- "*Texas Supreme Court Update*," State Bar College Summer School (July 21, 2005). .

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89 S.W.3d 761 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding) 5

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95 S.W.3d 286 (Tex. App.—Dallas 2001, pet. dism'd by agr.) 3, 13, 14

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166 S.W.3d 795 (Tex. App.—Houston [14th Dist.] 2005, orig. proceeding) 7, 12

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28 S.W.3d 732 (Tex. App.—Corpus Christi 2002, orig. proceeding) 14

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THE INTERSECTION BETWEEN ARBITRATION AND LITIGATION IN TEXAS

I. INTRODUCTION[1]

Arbitration is generally considered an alternative to litigation. Businesses frequently include arbitration clauses in their contracts in an attempt to avoid the time and costs associated with the traditional court system. But judging from the steady stream of arbitration-related decisions emanating from the Fifth Circuit and Texas appellate courts in recent years, even the most "air-tight" arbitration clause cannot guarantee that disputes will be resolved without judicial intervention.

Courts typically deal with arbitration-related disputes in two circumstances. First, when a party to a contract with an arbitration clause resists arbitrating a dispute, the contracting parties often litigate the enforceability and scope of the arbitration clause before any arbitration proceeding begins. Second, after an arbitration panel renders its decision and issues an award, parties frequently turn to the courts in an effort to confirm, modify, or vacate the arbitral award.

This paper provides a comprehensive overview of arbitration-related litigation in Texas and offers guidance for handling an arbitration-related dispute in the court system.

II. THE EFFECT OF THE GOVERNING LAW ON ARBITRATION-RELATED LITIGATION

The law that governs an arbitration agreement has a significant impact, both substantively and procedurally, on arbitration-related litigation.

A. Possible Sources of Governing Law.

1. The Texas Arbitration Act and Federal Arbitration Act.

The two most common statutory sources of the governing law for arbitration agreements in Texas are the Texas Arbitration Act, TEX. CIV. PRAC. & REM. CODE, Ch. 171 ("TAA") and the Federal Arbitration Act, 9 U.S.C. § 1 *et. seq*. ("FAA").

Both the FAA and TAA are intended to apply broadly, with only limited "carve outs" in the statutory text. For example, the FAA does not apply to employment contracts of "seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."[2] The TAA does not apply to collective bargaining agreements, workers' compensation benefit claims, or any agreements made before January 1, 1966.[3] In addition, the TAA does not apply to (1) a claim based on a transaction with an individual where the consideration is less then $50,000 or (2) a claim for personal injury, unless the arbitration agreements are in writing and signed by each party *and* his or her attorney.[4]

The FAA applies to all suits pending in state and federal court when the dispute concerns a "contract evidencing a transaction involving commerce."[5] Both state and federal courts have applied this test very liberally in favor of application of the FAA. As defined in the FAA, "interstate commerce" is not limited to the interstate shipment of goods but rather includes all contracts "relating to" interstate commerce.[6] The Texas Supreme Court has concluded that, under this language, the FAA "extends to any contract affecting commerce, as far as the Commerce Clause of the United States Constitution will reach."[7]

2. Other Statutory Sources.

Other statutory sources for arbitration include the Texas Family Code (*see, e.g.*, TEX. FAM. CODE § 6.601, § 153.0071); collective bargaining agreement disputes, covered under Chapter 102 of the Texas Labor Code; Worker's Compensation Benefit disputes, covered under Chapter 410 of the Texas Labor Code; and disputes involving residential construction, covered by Chapter 436 of the Texas Property Code.

3. Common Law.

Even if a dispute is not subject to arbitration under statute, an agreement may be enforceable under

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[1] The authors thank Elizabeth (Heidi) Bloch for allowing us to build upon a series of excellent CLE papers that she authored on this subject.

[2] 9 U.S.C. § 1.

[3] TEX. CIV. PRAC. & REM. CODE § 171.002(a).

[4] *Id.* § 171.002(b), (c).

[5] *Perry v. Thomas*, 482 U.S. 483, 489 (1987); *see also* 9 U.S.C. § 1 ("'commerce' . . . means commerce among the several States").

[6] *In re FirstMerit Bank*, 52 S.W.3d 749, 754 (Tex. 2001).

[7] *In re L & L Kempwood Assoc.*, 9 S.W.3d 125, 127 (Tex. 1999). One Texas court found that the contract for the construction of a home evidenced a "transaction involving commerce," because discovery answers in the record listed Wal-Mart as one of the subcontractors who participated in the design or construction of the home. *In re Nasr*, 50 S.W.3d 23, 25-26 (Tex. App.—Beaumont 2001, orig. proceeding); *see also In re Profanchik*, 31 S.W.3d 381 (Tex. App.—Corpus Christi 2000, orig. proceeding).

common law.[8] For example, in *Hoeppner v. Statewide Remodeling, Inc.*, the Waco Court of Appeals concluded that it need not address whether the FAA applied to a particular arbitration clause because the clause was enforceable under common law, which required the arbitration provision to be enforced according to its plain terms.[9]

The statutory and the common law schemes regarding the enforceability of arbitration agreements and vacatur of arbitration awards appear to exist side-by-side in Texas.[10]

B. FAA Preemption.

The Texas Supreme Court recently reemphasized that the FAA and TAA are not mutually exclusive.[11] Rather, "the FAA only preempts contrary state law, not consonant state law."[12] The purpose of the FAA is to create substantive rules, applicable in state and federal courts, to prevent states from limiting the enforceability of arbitration agreements.[13]

The Texas Supreme Court has promulgated a four-part test for determining whether the TAA would thwart the goals and policies of the FAA in a particular case. The FAA preempts the TAA only if: "(1) the agreement is in writing, (2) it involves interstate commerce, (3) it can withstand scrutiny under traditional contract defenses [under state law], and (4) state law affects the enforceability of the agreement."[14] The fourth factor is satisfied only where state law would "refuse to enforce an arbitration agreement that the FAA would enforce," either because (1) the TAA has expressly exempted the agreement from coverage (*see* TEX. CIV. PRAC. & REM. CODE § 171.002(a)), or (2) the TAA has imposed an enforceability requirement not found in the FAA.[15]

FAA preemption has two practical effects. First, as indicated above, the FAA will nullify a state statute purporting to limit the ability of parties to arbitrate their claims in a manner inconsistent with the FAA.[16] For example, if a state arbitration statute requires the signature of a witness, then the FAA, if it applies, will preempt such requirement and render a non-conforming arbitration agreement enforceable.[17]

Second, whether the FAA applies to an arbitration agreement and preempts the TAA significantly impacts the availability and manner of appellate review of a trial court's order compelling or denying arbitration in state court. As discussed in greater detail below, mandamus relief is generally available when the trial court refuses to compel arbitration under the FAA and when the trial court compels arbitration under the TAA. In contrast, an interlocutory appeal is the appropriate way to challenge a trial court's refusal to compel arbitration under the TAA.[18] However, an interlocutory appeal is not available for review of an order compelling arbitration under the FAA, and mandamus relief may be available only in rare cases.[19]

C. Choice of Law Agreements.

Arbitration clauses often contain specific provisions stating that either the TAA or the FAA will apply, or the arbitration clauses may be contained in a contract with a general choice of law provision. Such clauses may or may not be determinative of which statute applies.

The Texas Supreme Court has concluded that a general choice of law provision stating that the contract will be governed by "the law of the place where the project is located" – Houston – did not preclude

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[8] *L.H. Lacy Co. v. City of Lubbock*, 559 S.W.2d 348, 350 (Tex. 1977); *Mullinax, Wells, Baab & Cloutman, P.C. v. Sage*, 692 S.W.2d 533, 535 (Tex. App.—Dallas 1985, writ ref'd n.r.e.).

[9] 2003 WL 21357277 (Tex. App.—Waco 2003, pet. denied).

[10] *Id.*; *Monday v. Cox*, 881 S.W.2d 381, 385 n.1 (Tex. App.—San Antonio 1994, writ denied); *Massey v. Galvan*, 822 S.W.2d 309, 315-16 (Tex. App.—Houston [14th Dist.] 1992, writ denied).

[11] *See In re D. Wilson Constr. Co.*, 196 S.W.3d 774, 779 (Tex. 2006).

[12] *Id.*

[13] *Southland Corp. v. Keating*, 465 U.S. 1, 14-16 (1984).

[14] *In re D. Wilson Constr. Co.*, 196 S.W.3d at 780 (citing *In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69 (Tex. 2005)).

[15] *Id.*

[16] *In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69 (Tex. 2005); *In re Jim Walter Homes, Inc.*, 207 S.W.3d 888, 896 (Tex. App.—Houston [14th Dist.] 2006, orig. proceeding).

[17] *In re Nexion Health*, 173 S.W.3d at 69 (Tex. 2005) ("The TAA interferes with the enforceability of the arbitration agreement by adding an additional requirement—the signature of a party's counsel—to arbitration agreements in personal injury cases.").

[18] *See infra* Part III.E.

[19] *See infra* Part III.E; *In re Palacios*, -- S.W.3d --, 2006 WL 1791683, at *1-2 (Tex. June 30, 2006) (per curiam); *In re Wolff*, No. 05-07-00656-CV, 2007 WL 2120654, at *1 (Tex. App.—Dallas July 27, 2007, orig. proceeding) (holding mandamus relief was available to review an order compelling arbitration where the party seeking relief meets a particularly heavy burden).

application of the FAA because Houston is subject to federal law as well as to Texas law.[20] This holding is consistent with the concept that choice of law provisions generally address the applicability of one state's law over another state's law, not state versus federal law. Citing this holding, the Corpus Christi Court of Appeals went even further, holding that a choice of law provision in the contract, requiring that it be construed and interpreted in accordance with the laws of the State of Texas, did not preclude application of the FAA.[21]

Several courts of appeals have held that an agreement between the parties to arbitrate under the FAA establishes the applicability of the FAA, even without a showing that the transaction affects or involves interstate commerce.[22]

The Texas Supreme Court has not directly addressed the issue, but in *In re FirstMerit Bank*, the court at least indicated that mere agreement that the FAA will govern may not be sufficient. *FirstMerit* involved a specific clause in an arbitration agreement stating that the underlying transaction "involves interstate commerce . . . and shall be governed by the Federal Arbitration Act" and yet the court nonetheless examined whether the transaction did, in fact, involve interstate commerce.[23]

To be on the safe side, contracting parties who wish to be governed by the FAA should include a recitation in their agreement of the underlying facts necessary to establish applicability of the FAA, in addition to a statement that the FAA applies. In contrast, a statement that the TAA applies likely will not be effective if the contract involves interstate commerce.

III. PRE-ARBITRATION LITIGATION

Most arbitration-related litigation occurs when a dispute arises between parties to a contract with an arbitration clause and one of the parties resists arbitrating the dispute. Whether the arbitration clause is governed by the TAA or the FAA, this litigation typically focuses on two questions: (1) is the arbitration clause enforceable (*i.e.*, was there a valid agreement to arbitrate) and (2) does the parties' dispute fall within the scope of the clause?[24]

This section will examine these substantive questions and then will analyze the procedural issues involved in litigating these questions in trial and appellate courts.

A. Enforceability of Arbitration Clauses.

1. Interplay between the FAA and the TAA.

Where the FAA applies, it will preempt any contrary state laws governing the enforceability of arbitration clauses. However, the FAA will not validate an agreement that is otherwise unenforceable under general contract principles. Even if the FAA applies, an agreement to arbitrate must still be valid under general principles of state contract law.[25]

Texas procedure under the TAA controls the determination of whether an arbitration clause is enforceable in litigation in Texas state courts.[26] In other words, the procedures set forth in the TAA, such as filing an application in court to compel arbitration, apply to an arbitration clause whose enforceability is governed by the FAA. The only exception to this rule appears to be the interlocutory appeal procedures set forth in the TAA, which courts have concluded are not available to review a decision regarding the enforceability of an agreement covered by the FAA.[27]

2. Existence of an Agreement to Arbitrate.

The first step of the analysis is determining whether there was a contractual agreement to arbitrate. Absent such an agreement, "a party cannot be forced to forfeit the constitutional protections of the judicial system and submit its dispute to arbitration."[28] The intention to have disputes resolved through arbitration must be expressed with certainty. Such certainty was absent in *Tenet Healthcare Ltd. v. Cooper*, where the Houston Court of Appeals held that a company handbook, which stated that its contents were

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[20] *In re L & L Kempwood Assoc.*, 9 S.W.3d 125, 127 (Tex. 1999).

[21] *In re Valle Redondo*, 47 S.W.3d 655, 660-62 (Tex. App.—Corpus Christi 2001, orig. proceeding).

[22] *In re Ledet*, 2004 WL 2945699, at *2 (Tex. App.—San Antonio Dec. 22, 2004, orig. proceeding); *In re Kellogg Brown & Root*, 80 S.W.3d 611 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding); *In re Choice Homes, Inc.*, 174 S.W.3d 408, 412 (Tex. App.—Houston [14th Dist.] 2005, orig. proceeding).

[23] *In re FirstMerit Bank, N.A.*, 52 S.W.3d 749, 754 (Tex. 2001).

[24] *FirstMerit*, 52 S.W.3d at 753-54.

[25] *In re AdvancePCS Health L.P.*, 172 S.W.3d 603, 606 (Tex. 2005) (per curiam); *In re Halliburton Co.*, 80 S.W.3d 566, 568 (Tex. 2002).

[26] *Jack B. Anglin Co., Inc. v. Tipps*, 842 S.W.2d 266, 268-69 (Tex. 1992); *In re MHI P'ship, Ltd.*, 7 S.W.3d 918, 921 (Tex. App.—Houston [1st Dist.] 1999, orig. proceeding).

[27] *See infra* Part III.E.1.

[28] *Glazer's Wholesale Distribs., Inc. v. Heineken USA, Inc.*, 95 S.W.3d 286, 296 (Tex. App.—Dallas 2001, pet. dism'd by agr.); *accord Freis v. Canales*, 877 S.W.2d 283, 284 (Tex. 1994) (per curiam).

"guidelines," did not create an enforceable contract requiring arbitration despite a policy provision in the handbook stating a preference for arbitration to resolve disputes.[29]

a. State Contract Law Principles.

The existence of an agreement to arbitrate, even one governed by the FAA, is determined under state law general contract principles.[30] Courts have resorted to general contract principles in the following decisions:

- While the TAA and FAA both require a written agreement, an oral agreement to arbitrate can be enforceable under common law.[31]

- An arbitration agreement contained in a separate agreement can be incorporated into the parties' contract by reference.[32] For example, one court held that an unsigned arbitration clause contained in a general-conditions document, which was incorporated by reference into the signed contract, was an enforceable agreement to arbitrate.[33]

- In *Massey v. Galvan*, the court concluded that a series of letters between attorneys on behalf of their respective clients constituted a series of writings sufficient to demonstrate an agreement to arbitrate.[34]

- In *In re Bunzl USA, Inc*., there was a written employment agreement containing an arbitration clause, but it was not signed by the employee.[35] The court denied arbitration because the record was insufficient to establish that the parties intended to be bound by the agreement regardless of whether it was signed.

b. Agreement to be bound.

The general rule is that parties need not expressly state that an award is binding. At least one court has recognized that arbitration is, by definition, binding under the TAA even without the term "binding" appearing in the agreement.[36] There is certainly no requirement in either the TAA or the FAA that an agreement state that it is binding in order for the parties to be bound by an arbitration award.[37]

However, there are some exceptions for non-TAA arbitration clauses arising under certain statutes. The Family Code makes a distinction between binding and non-binding arbitration and provides the parties will not be bound by an arbitration award unless they have expressly so agreed. Similarly, under the new Texas Residential Construction Commission Act, an "action" is defined to include an "arbitration," and an "arbitration" means the procedure described in TEX. CIV. PRAC. & REM. CODE § 154.027. That section states that an arbitration will be non-binding unless the parties "stipulate in advance" that the award will be binding.[38]

c. Enforcement by or against Non-signatories.

Both federal and state courts have recognized that "under certain circumstances, principles of contract law and agency may bind a non-signatory to an arbitration agreement."[39] Federal courts have recognized six theories that may bind non-signatories to arbitration agreements: (1) incorporation by reference; (2) assumption; (3) agency; (4) alter ego; (5) equitable estoppel; and (6) third-party beneficiary.[40] The Fifth

[29] 960 S.W.2d 386 (Tex. App.—Houston [14th Dist.] 1998, pet. dism'd w.o.j.).

[30] *In re Palm Harbor Homes, Inc.*, 195 S.W.3d 672, 676 (Tex. 2006).

[31] *Id.; L. H. Lacy Co. v. City of Lubbock*, 559 S.W.2d 348 (Tex. 1977).

[32] *In re D. Wilson Constr. Co.*, 196 S.W.3d 774, 781 (Tex. 2006).

[33] *Teal Constr. Co./Hillside Villas Ltd. v. Darren Casey Interests, Inc.*, 46 S.W.3d 417, 420 (Tex. App.—Austin 2001, pet. denied).

[34] 822 S.W.2d 309, 315-16 (Tex. App.—Houston [14th Dist.] 1992, writ denied).

[35] 155 S.W.3d 202, 209 (Tex. App.—El Paso 2004, orig. proceeding).

[36] *Porter & Clements, LLP v. Stone*, 935 S.W.2d 217, 220-22 (Tex. App.—Houston [1st Dist.] 1997, no writ).

[37] *Nabors Drilling USA v. Carpenter*, 198 S.W.3d 240, 247 (Tex. App.—San Antonio 2006, no pet.).

[38] There is one other noteworthy case relating to the use of the term "binding." In *High Valley Homes, Inc. v. Fudge*, the court concluded that a contract provision requiring "mandatory, binding mediation" required arbitration despite the use of the word "mediation." 2003 WL 1882261 (Tex. App.—Austin 2003, no pet.).

[39] *In re Kellogg Brown & Root, Inc.*, 166 S.W.3d 732, 738 (Tex. 2005) (citing cases); *see also McMillan v. Computer Translation Sys. & Support*, 66 S.W.3d 477, 481 (Tex. App.—Dallas 2001, no pet.).

[40] *See In re Kellogg*, 166 S.W.3d at 739 (relying on state law but noting a desire to maintain consistency between state and federal law).

Circuit analyzes application of these theories under federal law.[41] The Texas Supreme Court has chosen to rely on state law, but explained that its reliance is "informed by persuasive and well-reasoned federal precedent."[42]

(1) Equitable Estoppel/Direct Benefits Estoppel.

Of these six bases listed above, estoppel has been the focus of the most judicial attention of late.

The Fifth Circuit's decision in *Grigson v. Creative Artist Agency, L.L.C.* paved the way for application of the equitable estoppel doctrine in Texas.[43] In *Grigson*, the court held that the doctrine of equitable estoppel applies to preclude a signatory to a contract containing an arbitration clause from avoiding arbitration against a non-signatory, when the signatory "raises allegations of substantially interdependent and concerted misconduct by both the non-signatory and one or more of the signatories to the contract."[44] The party to the arbitration clause in *Grigson* could not escape enforcement of the clause by including a non-signatory in its suit when the claims against the non-signatory were intertwined with those against the other party to the arbitration agreement.

Numerous Texas courts, including the Texas Supreme Court, have adopted the *Grigson* holding.[45] In *Meyer v. WMCO-GP, LLC*, the supreme court held that two non-signatory defendants could compel a signatory to arbitrate even though the arbitration provision stated that it applied to "[a]ny controversy between the parties to this Agreement."[46] The court stated that the phrase "between the parties" meant that it applies to disputes between them, but was not intended to preclude application of equitable estoppel.[47]

Equitable estoppel cannot be used by a signatory to compel a non-signatory to arbitrate, regardless of how closely the non-signatory is affiliated with the signing party.[48] However, a non-signatory may be compelled to arbitrate under the related theory of "direct benefits estoppel." Under direct benefits estoppel, "a non-signatory plaintiff seeking the benefits of a contract is estopped from simultaneously attempting to avoid the contract's burdens, such as the obligation to arbitrate disputes."[49] The underlying principle behind this doctrine is that a "nonparty [to a contract] cannot both have his contract and defeat it too."[50]

The Texas Supreme Court has recently examined direct benefits estoppel in several cases and has determined that parties may be bound to arbitrate under this theory: (1) when the non-signatory pursues a claim "on the contract" or (2) when the non-signatory seeks and obtains substantial benefits from the contract.[51] A non-signatory will not be bound simply because a claim is *related* to a contract with an arbitration provision.[52] Rather, the Court has explained that "a non-signatory should be compelled to arbitrate a claim only if it seeks, through the claim, to derive a direct benefit from the contract containing the arbitration provision."[53]

Thus, a non-signatory subcontractor in *In re Kellogg* was not forced to arbitrate its quantum meruit claim when its right to payment stemmed from a second-tier subcontract containing no arbitration clause, even though the first-tier subcontract contained an arbitration agreement.[54] In contrast, a non-signatory in *In re Weekley Homes*, whose father purchased a home for her benefit, could be compelled to arbitrate when she had exercised contract rights in the past and was equitably entitled to other contractual benefits.[55]

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[41] *Wash. Mut. Fin. Group, LLC v. Bailey*, 364 F.3d 260, 267 (5th Cir. 2004).

[42] *In re Kellogg*, 166 S.W.3d at 739.

[43] 210 F.3d 524 (5th Cir. 2000).

[44] *Id.* at 527.

[45] *See, e.g.*, *Meyer v. WMCO-GP, LLC*, 211 S.W.3d 302, 305 (Tex. 2006); *Brown v. Anderson*, 102 S.W.3d 245, 249 (Tex. App.—Beaumont 2003, pet. denied); *In re EGL Eagle Global Logistics, L.P.*, 89 S.W.3d 761, 764-56 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding); *Cash Am. Int'l, Inc. v. Exch. Servs., Inc.*, 83 S.W.3d 183 (Tex. App.—Amarillo 2002, no pet.).

[46] 211 S.W.3d 302, 305 (Tex. 2006).

[47] *Id*. at 307-08.

[48] *Bridas S.A.P.I.C. v. Gov't of Turkmenistan*, 345 F.3d 347, 361 (5th Cir. 2003); *In re Merrill Lynch, Pierce, Genner & Smith, Inc.*, 195 S.W.3d 807, 815 (Tex. App.—Dallas 2006, no pet.).

[49] *In re Kellogg*, 166 S.W.3d at 739.

[50] *In re Weekley Homes, L.P.*, 180 S.W.3d 127, 135 (Tex. 2005).

[51] *In re Weekley Homes*, 180 S.W.3d at 131-33. The Texas Supreme Court has taken note of another species of direct benefits estoppel applied by federal courts, which binds non-signatories "who, during the life of the contract, have embraced the contract despite their non-signatory status but then, during litigation, attempt to repudiate the arbitration clause in the agreement." However, the court did not reach the question of whether this form of direct benefits estoppel would be available under Texas law. *In re Kellogg*, 166 S.W.3d at 741 n.9 (citing cases).

[52] *In re Kellogg*, 166 S.W.3d at 741.

[53] *Id*.

[54] 166 S.W.3d at 741.

[55] 180 S.W.3d at 133-35. *But see Fleetwood Enters., Inc. v. Gaskamp*, 280 F.3d 1069, 1076-77 (5th Cir. 2002) (finding

In *In re Vesta Ins. Group, Inc.*, the supreme court also addressed the question of whether a claim of tortious interference against nonsignatories was arbitrable under the direct benefits estoppel doctrine.[56] It explained that, under this doctrine, nonsignatories generally must arbitrate claims arising from the contract, but not if the claim arises from general legal obligations.[57] While the court found that a tortious interference claim arises from both the contract and general law, it fell "on the arbitration side of the scale."[58] Thus, non-signatories may be bound to arbitrate a tortious interference claim.

Texas courts and the Fifth Circuit have utilized the direct benefits estoppel doctrine only to compel arbitration by nonsignatories who have sued signatories.[59] However, the Southern District of Texas recently held that the doctrine may be employed outside this context.[60] It remains to be seen whether other courts in Texas will follow the Southern District's lead.

(2) Incorporation by reference.

A court can also use incorporation by reference to bind a non-signatory. For example, in *In re Bank One*, the Texas Supreme Court found a valid arbitration agreement was incorporated by reference when the plaintiff's representative signed an account signature card.[61]

In *Cappadonna Electrical Management v. Cameron County*, the court declined to apply incorporation by reference to compel arbitration when subcontractors did not attempt to incorporate the terms of the Prime Contract into their subcontract, and the Prime Contract was the only contract that had an arbitration clause.[62] The court found that incorporation by reference applies when a party binds itself by incorporating a document by reference into its own contract, but non-signatory non-parties could not use the doctrine to enforce a provision of a document it did not sign or incorporate.[63]

(3) Affiliated Companies.

Federal courts have consistently held that affiliated companies, including parent, subsidiary, and successor corporations, can be forced to arbitrate when the claims against them arise from the same operative facts and are inherently inseparable from claims against an affiliate or predecessor corporation that is a party to an arbitration agreement.[64]

(4) Third party beneficiary.

A party resisting arbitration on the grounds that he or she has not signed an agreement to arbitrate may nonetheless be required to arbitrate as a third party beneficiary of the agreement.[65]

Finally, it is important to keep in mind that a non-signatory must establish, in a proceeding to compel arbitration, the grounds that give it a basis for compelling arbitration. In *Mohamed v. Auto Nation USA Corp.*, a non-signatory attempted to enforce arbitration, and would likely have succeeded in doing so, but failed to prove its status as an assignee of the contract containing the arbitration agreement.[66]

3. Defenses to Enforcement.

As noted above, because an arbitration agreement is governed under general state contract principles, any defense available to avoid other contractual obligations is similarly available to challenge the enforceability of an arbitration agreement. It is important at the outset, however, to note the distinction between those defenses that would invalidate only the agreement to arbitrate, which can be determined initially by a court addressing a motion to compel arbitration, and those that involve procedural questions or would void the contract as a whole (as opposed to just the arbitration clause), which are generally for the arbitrator to decide. This distinction will be pointed out, where relevant, below.

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that, without more, children of signatory parents could not be bound to arbitrate merely on the basis of the parent-child relationship).

[56] 192 S.W.3d 759, 761-62 (Tex. 2006) (per curiam).

[57] *Id*. at 761.

[58] *Id*. at 762.

[59] *See, e.g., In re Weekley Homes*, 180 S.W.3d at 134-35; *Hellenic Inv. Fund, Inc. v. Det Norske Veritas*, 464 F.3d 514, 517-20 (5th Cir. 2006).

[60] *Wood v. PennTex Res., L.P.*, 458 F. Supp. 2d 355, 370-73 (S.D. Tex. 2006);.

[61] No. 06-0093, 2007 WL 549744 (Tex. Feb. 23, 2007) (per curiam).

[62] 180 S.W.3d 364, 373 (Tex. App.—Corpus Christi 2005, no pet.).

[63] *Id*.

[64] *In re Koch Indus., Inc.*, 49 S.W.3d 439, 447 (Tex. App.—San Antonio 2001, orig. proceeding), and cases cited therein.

[65] *See Nationwide of Bryan, Inc., v. Dyer*, 969 S.W.2d 518, 520 (Tex. App.—Austin 1998, no pet.); *In re Rangel*, 45 S.W.3d 783, 787 (Tex. App.—Waco 2001, orig. proceeding).

[66] 89 S.W.3d 830 (Tex. App.—Houston [1st Dist.] 2002, no pet.).

a. Conditions Precedent.

It is not uncommon for an arbitration clause to include certain prerequisites or conditions precedent to arbitration. These may include an agreement to first attempt mediation, to send a particular type of notice of default or demand for arbitration, or perhaps to provide for an opportunity to cure.[67]

For many years, there had been a split among Texas courts of appeals regarding whether a court or arbitrator should resolve the issue of whether a condition precedent to arbitration has been satisfied.[68] The United States Supreme Court reached the issue in *Howsam v. Dean Witter Reynolds, Inc.* and determined that this issue was for the arbitrator to decide.[69] At least two Texas courts of appeal have recognized that the prior circuit split has been resolved by *Howsam*.[70] Despite *Howsam*, however, some courts have recognized a rare exception which would allow a court to refuse to compel arbitration if "no rational mind" could question that the parties intended for a procedural provision to preclude arbitration and that the breach of the procedural requirement was clear.[71]

b. Fraud.

Under both state and federal law, claims of fraud that would invalidate the entire contract are subject to arbitration, and thus determinable by the arbitrator.[72] In contrast, a claim that the arbitration clause itself has been induced by fraud may be adjudicated by the court.[73]

In *Teal Constr. Co./Hillside Villas, Ltd. v. Darren Casey Interests, Inc.*, the Austin Court of Appeals noted that there is some authority for the proposition that, under state law, fraudulent inducement voids a contract *ab initio*, and therefore an arbitration clause in such a contract is invalid.[74] However, that court rejected the contention that fraudulent inducement of the construction contract had rendered the arbitration clause invalid because the issues of payment and performance, which were the bases of the fraudulent inducement claim, were subject to arbitration.[75]

c. Unconscionability and Duress.

As with fraud, defenses to arbitration such as unconscionability, duress, and revocation must specifically relate to the arbitration clause itself, not to the contract as a whole.[76] If a defense of unconscionability or duress is asserted against the entire contract, those issues are to be arbitrated.[77] Where a party claims that the duress relates to both the arbitration provision and the contract as a whole, the issue must be arbitrated unless the arbitration provision alone was singled out from the other provisions.[78]

In evaluating the validity of an arbitration clause, courts may consider both procedural and substantive unconscionability.[79] Procedural unconscionability refers to circumstances surrounding the adoption or execution of the arbitration provision.[80] Substantive unconscionability refers to the fairness of the arbitration provision itself.[81] The test for substantive unconscionability is whether, "given the parties' general commercial background and the commercial needs of the particular trade or case, the clause involved is so

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[67] *See, e.g., In re R & R Pers. Specialists of Tyler, Inc.*, 146 S.W.3d 699, 704-05 (Tex. App.—Tyler 2004, orig. proceeding) (arbitration agreement required written notice of intent to arbitrate, compliance with deadlines regarding notice of claim, and participation in mediation prior to arbitration).

[68] *See Valero Energy Corp. v. Teco Pipeline Co.*, 2 S.W.3d 576, 583 (Tex. App.—Houston [14th Dist.] 1999, no pet.) (citing cases).

[69] 537 U.S. 79, 84 (2002).

[70] *See In re Global Constr. Co.*, 166 S.W.3d 795, 798-99 (Tex. App.—Houston [14th Dist.] 2005, orig. proceeding); *In re R & R Pers. Specialists of Tyler, Inc.*, 146 S.W.3d 699, 705 (Tex. App.—Tyler 2004, orig. proceeding).

[71] *See General Warehousemen & Helpers Union Local 767 v. Albertson's Distrib., Inc.*, 331 F.3d 485, 488 (5th Cir. 2003) (refusing to apply the exception where a rational mind could have concluded that the district court should have compelled arbitration); *In re Pisces Foods, L.L.C.*, 03-06-00274-CV, 2007 WL 1518076, at *4 (Tex. App.—Austin May 24, 2007, orig. proceeding) (holding that where it was undisputed that the parties had not complied with a mediation pre-requisite, the trial court did not abuse its discretion in refusing to compel arbitration).

[72] *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 (1967); *Teal Constr. Co./Hillside Villas, Ltd. v. Darren Casey Interests, Inc.*, 46 S.W.3d 417, 420-21 (Tex. App.—Austin 2001, pet. denied).

[73] *Prima Paint Corp.*, 388 U.S. at 403-04.

[74] 46 S.W.3d at 421.

[75] *Id.*

[76] *In re FirstMerit Bank, N.A.*, 52 S.W.3d 749, 756 (Tex. 2001).

[77] *Id.*

[78] *In re RLS Legal Solutions, LLC*, 221 S.W.3d 629, 632 (Tex. 2007).

[79] *In re Halliburton Co.*, 80 S.W.3d 566, 571 (Tex. 2002); *see also* TEX. CIV. PRAC. & REM. CODE § 171.022 (stating that "a court may not enforce an agreement to arbitrate if the court finds the agreement was unconscionable at the time the agreement was made").

[80] *In re Halliburton*, 80 S.W.3d at 571.

[81] *Id.*

one-sided that it is unconscionable under the circumstances existing when the parties made the contract."[82]

It is difficult to strike down an arbitration clause on the grounds of unconscionability because there is nothing inherently unconscionable about an arbitration agreement or a contract of adhesion.[83] A party that has had an opportunity to read an arbitration agreement is presumed to know its contents.[84] Thus, ignorance of the inclusion of the clause will not defeat it.[85]

Furthermore, unconscionability will not negate a bargain simply because one party is in a less advantageous bargaining position.[86] To defeat an agreement to arbitrate due to unequal bargaining power, a party must demonstrate that the clause was the result of the type of fraud or overwhelming economic power that would be grounds for revocation of any contract.[87]

While unconscionability is difficult to prove, a court may find an arbitration agreement unconscionable due to excessive costs.[88] A party opposing arbitration on this basis must prove with specific information the likelihood of incurring excessive costs.[89] In *Olshan Foundation Repair Co. v. Ayala*, the court found arbitration unconscionable when it would have cost plaintiffs $33,000 to arbitrate their $22,650 claim.[90] The plaintiffs supported their motion in the trial court with specific information regarding the fees and asserted that the costs would effectively deprive them of the opportunity to bring their claims.[91]

d. Waiver.

Whether a party waives its right to seek arbitration is an issue for the court.[92] The two-prong test for waiver is the same under both the TAA and the FAA: (i) did the party seeking arbitration substantially invoke the judicial process; and (ii) did the opposing party prove that it suffered prejudice as a result?[93]

There is a strong presumption against waiver.[94] While a party waives arbitration by substantially invoking the judicial process to the opponent's detriment, mere participation in litigation is not enough to establish waiver.[95] For example, in *In re Vesta*, the Texas Supreme Court found no waiver even though the parties had litigated in the trial court for two years and the plaintiff had incurred more than $200,000 in expenses and fees.[96] The court determined that much of the plaintiff's pre-trial costs were "self-inflicted" and that he failed to demonstrate prejudice when he conceded that the discovery would be useful in arbitration.[97]

Similarly, in *In re D. Wilson Construction Co.*, the supreme court found that petitioners had not waived their right to arbitration by asserting cross-actions against the respondent in a separate related suit or by seeking injunctive relief to preserve evidence in the present suit, because the respondent had not shown that the litigation worked to its detriment.[98] The supreme court also found no waiver in *In re Bank One*, where the defendant had moved to set aside a default judgment, filed an answer, and then waited eight months before moving to compel arbitration.[99]

The court has set a high bar to prove the requisite prejudice necessary to establish waiver. The fact that a party participated in litigation prior to arbitration is not sufficient to show prejudice.[100] Rather, a party asserting

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[82] *In re Palm Harbor Homes, Inc.*, 195 S.W.3d 672, 678 (Tex. 2006) (quoting *In re FirstMerit Bank*, 52 S.W.3d 749, 757 (Tex. 2001)).

[83] *See In re Palm Harbor Homes*, 195 S.W.3d at 678.

[84] *EZ Pawn Corp. v. Mancias*, 934 S.W.2d 87, 90 (Tex. 1996).

[85] *Id.*

[86] *In re Palm Harbor Homes*, 195 S.W.3d at 679 (finding no unconscionability when parties claimed they would not have signed the arbitration agreement had the concept of arbitration been explained to them).

[87] *In re AdvancePCS Health L.P.*, 172 S.W.3d 603, 606 (Tex. 2005).

[88] *See FirstMerit Bank, N.A.*, 52 S.W.3d 749, 756 (Tex. 2001).

[89] *Id.*

[90] 180 S.W.3d 212, 214-16 (Tex. App.—San Antonio 2005, pet. denied).

[91] *Id.* at 215-16. *But see TMI, Inc. v. Brooks*, -- S.W.3d --, 2007 WL 1362635, at **7-8 (Tex. App.—Houston [14th Dist.] May 10 2007, no pet. h.) (distinguishing *Olshan* and holding parties failed to prove unconscionability, even where they showed projected arbitration costs as high as $120,000, because less expensive means of arbitration were available).

[92] *In re Bruce Terminix Co.*, 988 S.W.2d 702 (Tex. 1998).

[93] *In re Bank One*, No. 06-0093, 2007 WL 549744 (Tex. Feb. 23, 2007) (per curiam) (applying the FAA); *Menna v. Romero*, 48 S.W.3d 247, 251 (Tex. App.—San Antonio 2001, pet. dism'd w.o.j.) (applying the TAA).

[94] *In re Vesta Ins. Group, Inc.*, 192 S.W.3d 759, 763 (Tex. 2006) (per curiam).

[95] *Id.*

[96] *Id.* at 763.

[97] *Id.*

[98] 196 S.W.3d 774, 783 (Tex. 2006).

[99] No. 06-0093, 2007 WL 549744 (Tex. Feb. 23, 2007) (per curiam).

[100] *Tex. Residential Mortgage v. Portman*, 152 S.W.3d 861, 864 (Tex. App.—Dallas 2005, no pet.); *Perry Homes v. Cull*,

waiver must present evidence showing additional work or costs that it otherwise would not have incurred in its anticipation of arbitration.[101]

e. Lack of Consideration/Lack of Mutuality.

Arbitration agreements must be supported by consideration.[102] Consideration may be in the form of bilateral promises to arbitrate or may be a part of a larger, underlying contract to which the arbitration clause belongs.[103]

Consideration and mutuality are common issues in arbitrations arising from employment agreements.[104] To enforce an arbitration agreement against an at-will employee, the employer must show that the employee received notice of the arbitration policy and accepted it.[105] An employee accepts the terms of the arbitration policy as a matter of law if he continues working after receiving notice of the policy.[106] In *In re Dallas Peterbilt, Ltd*., for instance, an employee claimed that he did not receive notice of the policy. However, the employee had signed an acknowledgment form stating that he had received a summary of the policy.[107] The court found this summary to be sufficient notice.[108]

Even if an arbitration agreement is formed during an at-will employment relationship, it is not illusory if the promises to arbitrate are not dependent upon continued employment.[109] In *In re Halliburton Company*, an employer adopted a dispute resolution program and sent its employees a notice that continuing employment would constitute acceptance of the plan.[110] A disgruntled employee filed suit and alleged that the arbitration agreement was illusory and without consideration because the employment was at will and the employer retained the option of either discontinuing employment or changing the policy.[111] The Texas Supreme Court concluded that the agreement was binding and enforceable on both parties. It noted that the employer could not avoid its promise to arbitrate, because the agreement required ten days notice of modification and any such amendment would apply only prospectively.[112]

f. Ambiguity.

A determination of ambiguity is for the court, and the court may conclude a contract is ambiguous even if the parties do not contend that it is.[113]

In *J.M. Davidson, Inc. v. Webster*, the Texas Supreme Court was unable to determine whether a clause included in a dispute resolution policy, allowing the company to "unilaterally abolish or modify any personnel policy without prior notice," permitted the company to terminate the arbitration agreement without notice.[114] The clause was included in a separate paragraph which addressed employment issues, but did not relate to alternative dispute resolution.[115] Finding proper interpretation of the language was critical to conclude whether the agreement was illusory, the court remanded to the trial court for a determination of what the parties meant by the clause.[116] The court explained, "While we generally favor arbitration agreements, we should not reflexively endorse an agreement so lacking in precision that a court must first edit the document for comprehension, and then rewrite it to ensure its enforceability."[117]

g. Statutory Preemption.

Parties pursuing a statutory cause of action have often complained that an agreement to arbitrate undercuts their ability to seek statutory relief. As noted above, the supremacy clause of the United States Constitution dictates that the FAA "takes precedence over state attempts, legislative or judicial, to undercut

173 S.W.3d 565, 570 (Tex. App.—Fort Worth 2005, pet. granted).

[101] *Portman*, 152 S.W.3d at 864.

[102] *In re Palm Harbor Homes*, 195 S.W.3d at 676.

[103] *Id*.

[104] *See, e.g., J.M. Davidson, Inc. v. Webster*, 128 S.W.3d 223 (Tex. 2003); *In re Kellogg, Brown & Root*, 80 S.W.3d 611 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding); *In re Jebbia*, 26 S.W.3d 753, 758 (Tex. App.—Houston [14th Dist.] 2000, orig. proceeding) (rejecting the argument that an arbitration provision lacked consideration because the employment relationship was at-will).

[105] *In re Dallas Peterbilt, Ltd*., 196 S.W.3d 161, 162 (Tex. 2006) (per curiam).

[106] *Id*. at 163.

[107] *Id*.

[108] *Id*.

[109] *In re Dillard Dep't Stores, Inc*., 198 S.W.3d 778, 782 (Tex. 2006) (per curiam).

[110] 80 S.W.3d 566, 568 (Tex. 2002).

[111] *Id*. at 569.

[112] *Id.* at 569-70. *But see J.M. Davidson, Inc. v. Webster*, 128 S.W.3d 223, 230 (Tex. 2003) (implying that an arbitration clause reserving the right to unilaterally modify without prior notice would be improper).

[113] *J.M. Davidson, Inc.*, 128 S.W.3d at 229, 231.

[114] *Id.* at 230.

[115] *Id.* at 229.

[116] *Id*. at 230.

[117] *Id*. at 231.

the enforceability of arbitration agreements."[118] Therefore, a contention that federally mandated arbitration runs afoul of a state statutory scheme is generally irrelevant.[119]

With respect to a federal statutory cause of action, only a contrary congressional command can override the FAA's mandate to enforce arbitration agreements.[120] The test articulated by the United States Supreme Court in *Shearson/American Express, Inc. v. McMahon* requires the party opposing arbitration to show a clear congressional intent to override the FAA's mandate to enforce arbitration agreements, which intent must be evidenced in the statute's text or history or through an inherent conflict between arbitration and the statute's purposes.[121] Claims such as those arising under the Securities Exchange Act and the Age Discrimination in Employment Act have been held to be subject to arbitration.[122]

B. Scope of Arbitration Clauses.

1. Presumptions.

A determination of whether a given dispute falls within the scope of an arbitration clause is a matter of contract interpretation that must be performed by a court.[123]

The strong presumption favoring arbitration generally requires that courts resolve doubts as to the scope of the agreements in favor of coverage, whether they arise under the FAA or TAA.[124] Presumptions are often necessary so that a court will not be forced to intrude on the merits of a case in determining the scope of an arbitration agreement.[125] However, under the FAA, "the presumption arises only after the party seeking to compel arbitration proves that a valid arbitration agreement exists, because the purpose of the FAA was to make arbitration agreements as enforceable as other contracts, not more so."[126]

To determine whether a claim falls within the scope of an arbitration agreement, courts look at the terms of the agreement and the factual allegations in the petition, rather than the legal causes of action asserted.[127] A broad arbitration clause, purporting to cover all claims, disputes, and other matters relating to the contract or its breach, creates a presumption of arbitrability.[128] A court should not deny a motion to compel arbitration "unless it can be said with positive assurance that an arbitration clause is not susceptible to an interpretation which would cover the dispute at issue."[129] The burden is on the party opposing arbitration to show that the claims fall outside the scope

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[118] *In re Turner Brothers Trucking Co.*, 8 S.W.3d 370, 374 (Tex. App.—Texarkana 1999, orig. proceeding); *Perry v. Thomas*, 482 U.S. 483, 492 n. 9 (1987).

[119] *In re David's Supermarkets*, 43 S.W.3d 94, 98 (Tex. App.—Waco 2001, orig. proceeding); *Jack B. Anglin Company, Inc. v. Tipps*, 842 S.W.2d 266, 268 (Tex. 1992) (arbitration agreement enforceable under FAA for DTPA claims).

[120] *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 226 (1987); *In re Am. Homestar of Lancaster, Inc.*, 50 S.W.3d 480, 484 (Tex. 2001). There is some authority for the proposition that a state-based claim with a parallel federal underpinning is not arbitrable if the parallel federal statutory scheme reflects a congressional intent that such claims not be arbitrated. *See In re David's Supermarkets, Inc.*, 43 S.W.3d 94, 99 (Tex. App.—Waco 2001, orig. proceeding), and cases cited therein.

[121] 482 U.S. at 227; *see also American Homestar*, 50 S.W.3d at 485.

[122] In *American Homestar*, the Texas Supreme Court addressed whether the Magnuson-Moss Warranty Act, which provides for informal dispute settlement mechanisms as a prerequisite to litigation, rendered a binding arbitration clause unenforceable. 50 S.W.3d 480 (Tex. 2001). The FTC has concluded that the informal dispute settlement mechanisms could not be binding, and the court of appeals had reasoned that this meant the Magnuson-Moss Act prohibited the use of binding arbitration clauses in written warranties. *In re Van Blarcum*, 19 S.W.3d 484, 491 (Tex. App.—Corpus Christi 2000), *vacated*, *In re Am. Homestar*, 50 S.W.3d 480 (Tex. 2001). The Texas Supreme Court held otherwise, noting that expressly providing for one type of out-of-court settlement mechanism does not necessarily preclude enforcing an agreement to participate in another. 50 S.W.3d at 487. Ultimately, the court found nothing in either the text of the Act or in its legislative history that would preclude arbitration, nor was there any inherent conflict between the FAA and the purposes of the Magnuson-Moss Act.

[123] *See, e.g.*, *In re Choice Homes, Inc.*, 174 S.W.3d 408, 413 (Tex. App—Houston [14th Dist.] 2005, orig. proceeding); *Tittle v. Enron Corp.*, 363 F.3d 410 (5th Cir. 2006).

[124] *In re D. Wilson Constr. Co.*, 196 S.W.3d 774, 782 (Tex. 2006); *In re Kellogg, Brown & Root, Inc.*, 166 S.W.3d 732, 737 (Tex. 2005); *In re FirstMerit Bank*, 52 S.W.3d 749, 753 (Tex. 2001).

[125] *See In re BP America Prod. Co.*, 97 S.W.3d 366 (Tex. App.—Houston [14th Dist.] 2003, orig. proceeding).

[126] *In re Kellogg*, 166 S.W.3d at 737-38 (internal citations omitted).

[127] *Prudential Sec., Inc. v. Marshall*, 909 S.W.2d 896, 900 (Tex. 1995).

[128] *American Realty Trust, Inc., v. JDN Real Estate-McKinney, L.P.*, 74 S.W.3d 527 (Tex. App.—Dallas 2002, pet. denied); *Lost Creek Mun. Util. Dist. v. Travis Indus. Painters, Inc.*, 827 S.W.2d 103, 105 (Tex. App.—Austin 1992, writ denied).

[129] *Marshall*, 909 S.W.2d at 899; *see also In re D. Wilson Constr.*, 196 S.W.3d at 783.

of the arbitration agreement as interpreted by the court.[130]

2. Related Claims.

The test for determining whether related claims are subject to an arbitration clause is looser than the "inextricably intertwined" test found in other areas of the law. Generally, if the facts alleged in a petition "touch matters," have a "significant relationship" to, are "inextricably enmeshed" with, or are "factually intertwined" with the issue that is subject to the arbitration agreement, the claim will be arbitrable.[131]

When a contract contains a broad arbitration clause, related tort claims arising out of the contract will be arbitrable as well. If a particular tort claim is so interwoven with the contract that it could not stand alone, it will be subject to arbitration.[132] In contrast, if the facts alleged in support of a claim stand alone, or are completely independent of the contract, and could be maintained without reference to the contract, the claim is not subject to arbitration.[133] Under this test, a broad range of tort or statutory claims could be covered under an agreement covering contract claims.[134]

[130] *Marshall*, 909 S.W.2d at 900.

[131] *In re Medallion, Ltd.*, 70 S.W.3d 284 (Tex. App.—San Antonio 2002, orig. proceeding); *Pennzoil Co. v. Arnold Oil Co., Inc.*, 30 S.W.3d 494, 498 (Tex. App.—San Antonio 2000, orig. proceeding).

[132] *Valero Energy Corp. v. Teco Pipeline Co.*, 2 S.W.3d 576, 590 (Tex. App.—Houston [14th Dist.] 1999, no pet.); *In re Medallion*, 70 S.W.3d at 828.

[133] *In re Medallion*, 70 S.W.3d at 828.

[134] *See Prima Paint Corp., v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 398 (1967) (fraudulent inducement claims); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Co., Inc.*, 473 U.S. 614 (1985) (antitrust claims arising from the contract); *Am. Employers Ins. Co., v. Aiken*, 942 S.W.2d 156 (Tex. App.—Fort Worth 1997, no writ) (tortious interference and infliction of emotional distress claims); *Prudential Sec., Inc. v. Marshall*, 909 S.W.2d 896 (Tex. 1995) (defamation and DTPA claims factually intertwined with the contract); *In re Sun Communications, Inc.*, 86 S.W.3d 313 (Tex. App.—Austin 2002, orig. proceeding) (claims of breach of fiduciary duty and conversion were inextricably intertwined with the contract); *In re First Texas Homes, Inc.*, 120 S.W.3d 868 (Tex. 2003) (alleged violations of the state and federal Fair Housing Acts and claims for intentional infliction of emotional distress were within the broad arbitration clause).

C. Who Gets to Decide Preliminary Issues--the Court or the Arbitrator?

As indicated above, in considering a motion to compel arbitration, a trial court often is faced with numerous factual and legal disputes that bear upon the enforceability and scope of an arbitration clause. For example, the existence of an agreement to arbitrate may turn on the incorporation of one contract into another by reference, the scope of an agent's authority to bind a principal to an agreement, issues involving non-signatories, and the like. Questions relating to the scope of the agreement are generally more clear-cut because they are resolved by comparing the language of the agreement with the factual allegations, as discussed in more detail below. Trial courts are also often faced with various defenses to enforcement. There has been much litigation over who gets to decide these issues, the court or the arbitrator.

The United States Supreme Court narrowed the role of courts in addressing preliminary issues in *Howsam v. Dean Witter Reynolds, Inc.*[135] The Court held that, generally, the question of whether the parties have submitted a particular dispute to arbitration, *i.e.* the "*question of arbitrability*," is "an issue for judicial determination."[136] Although recognizing that any potentially dispositive gateway question could be a "question of arbitrability," the Court emphasized that the phrase actually has a very limited scope.[137] Questions of arbitrability that are for a court to decide include whether the parties are bound by a given arbitration clause and whether the clause applies to the dispute at issue.[138] A question of whether an arbitration agreement is binding on a nonparty is also a gateway matter for the court.[139]

However, if a challenge is to the validity of a contract as a whole, rather than to the arbitration clause specifically, then the question is for the arbitrator, regardless of whether the challenge is brought in state or federal court.[140] "Procedural" questions that grow out of the dispute and bear on its final disposition are for the arbitrator to decide.[141] For example, arbitrator issues include conditions precedent to arbitrability, and

[135] 537 U.S. 79 (2002).

[136] *Id.* at 83 (emphasis added).

[137] *Id.*

[138] *Id.* at 84.

[139] *In re Weekley Homes, L.P.*, 180 S.W.3d 127, 743 (Tex. 2005).

[140] *Buckeye Check Cashing, Inc. v. Cardegna*, 126 S. Ct. 1204, 1210 (2006).

[141] *Howsam*, 537 U.S. at 84; *In re Pisces Foods, L.L.C.*, 03-06-00274-CV, 2007 WL 1518076, at *2 (Tex. App.—Austin May 24, 2007, orig. proceeding)

"waiver, delay, or a like defense to arbitrability."[142] In addition, deciding whether an arbitration claim is time-barred, for example, is a question for the arbitrator.[143]

The analysis as to whether a court or arbitrator should consider defenses to enforcement of an arbitration clause is set out in large part in Part III.A.3 above. A few other related holdings are worth mentioning:

Class Actions. Both the United States and the Texas Supreme Courts have concluded that class certification issues are for an arbitrator to decide.[144]

Illegality. The United States Supreme Court has held that, even if a party challenges that the contract is illegal and void *ab initio*, the question still should be considered by the arbitrator.[145]

Standing. In *Hisaw & Associates General Contractors, Inc. v. Cornerstone Concrete Systems, Inc*., the court was faced, in a post-arbitration suit to confirm an award, with the issue of whether the arbitrator had exceeded its authority in determining the standing of the claimant to bring the claim in the face of an assignment of that claim to a third party.[146] The court concluded that the broad arbitration clause at issue gave the arbitrator the authority to make the determination as to whether the claimant was the properly named party.[147]

D. Pre-Arbitration Litigation in the Trial Court.

1. Actions to Compel Arbitration.

If a party to an arbitration agreement that falls within the scope of the TAA refuses to arbitrate a dispute, the other party can file an application to compel litigation in a trial court. This application can be brought as an independent suit if no litigation is pending or in the form of a motion to compel if civil litigation already has commenced.

The TAA requires a court to order arbitration upon a showing of:

(1) an agreement to arbitrate; and
(2) the opposing party's refusal to arbitrate.

TEX. CIV. PRAC. & REM. CODE § 171.021. If the party opposing the application denies the existence of an agreement to arbitrate, "the court shall summarily determine that issue."[148]

The Texas Supreme Court first addressed how a trial court is to summarily determine the applicability of an arbitration clause in *Jack B. Anglin Co. v. Tipps*. There, the Court concluded that a trial court may summarily decide whether to compel arbitration on the basis of affidavits, pleadings, discovery, and stipulations.[149] If the material facts necessary to determine the issue are controverted, by opposing affidavit or otherwise, the trial court must conduct an evidentiary hearing to determine the disputed material facts.[150] Such an evidentiary hearing must itself be held "summarily."[151] The term "summarily" describes not only the procedure, but the speed with which a court should rule.[152]

Most intermediate appellate courts have held that a trial court cannot avoid appellate scrutiny by refusing to rule on a motion to compel arbitration until after discovery has been completed.[153] The Corpus Christi Court of Appeals, however, has held that a trial court may enjoin parties from proceeding with arbitration pending the completion of discovery.[154] It is questionable whether this holding remains viable in

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[142] *Howsam*, 537 U.S. at 84.

[143] *In re Global Constr. Co.*, 166 S.W.3d 795, 799 (Tex. App.—Houston [14th Dist.] 2005, orig. proceeding).

[144] *Green Tree Fin. v. Bazzle*, 539 U.S. 444 (2003); *In re Wood*, 140 S.W.3d 367, 368 (Tex. 2004).

[145] *Cardegna*, 126 S. Ct. at 1210.

[146] 115 S.W.3d 16, 19 (Tex. App.—Fort Worth 2003, pet. denied) (per curiam).

[147] *Id*. at 20.

[148] *Id.* § 171.021(b).

[149] *Jack B. Anglin Co. v. Tipps*, 842 S.W.2d 266, 269 (Tex. 1992).

[150] *Id.*

[151] *Trico Marine Servs., Inc. v. Stewart and Stevenson Technical Servs., Inc.*, 73 S.W.3d 545, 548 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding).

[152] *In re MHI P'ship Ltd.*, 7 S.W.3d 918, 922 (Tex. App.—Houston [1st Dist.] 1999, orig. proceeding); *see also In re Shredder Co., L.L.C.*, --S.W.3d--, 2006 WL 3234186 (Tex. App.—El Paso 2006, orig. proceeding) (holding trial court abused its discretion by failing to rule upon motion to compel arbitration for six months, despite repeated requests for a ruling).

[153] *In re MHI*, 7 S.W.3d at 922; *In re Champion Techs., Inc.*, 173 S.W.3d 595, 599 (Tex. App.—Eastland 2005, orig. proceeding); *see also In re Heritage Building Sys., Inc.*, 185 S.W.3d 539, 542-43 (Tex. App.—Beaumont 2006, orig. proceeding) (holding trial court could not delay ruling on motion to compel arbitration until after mediation).

[154] *C P & Assocs. v. Pickett*, 697 S.W.2d 828, 831 (Tex. App.—Corpus Christi 1985, no writ).

light of *Anglin's* direction to summarily decide motions to compel arbitration.[155]

If a dispute is to be resolved through arbitration, the court should avoid any scrutiny of the merits of the dispute.[156] For example, in *In re H20 Plumbing*, Inc., the court ruled that a trial court had abused its discretion in entering findings of fact relating to the merits of the dispute while, at the same time, compelling the parties to proceed to arbitration.[157] The court recognized the potential harm if one party presented those findings to the arbitrator.[158]

If an issue referable to arbitration is already pending in litigation before a court of competent jurisdiction, any application relating to arbitration between those parties must be filed in that court. Otherwise, a movant should abide by the TAA's independent venue provision.[159]

A trial court must stay an action involving an issue subject to arbitration if a motion to compel arbitration has been filed or an order compelling arbitration has issued.[160] However, if the arbitrable issues are severable, the stay applies only to those issues.[161] A court can only stay the lawsuit when it compels arbitration; it cannot dismiss the suit in its entirety.[162]

2. Actions to Stay Arbitration.

A party attempting to resist an actual or threatened arbitration may apply to a court for an order staying the arbitration proceeding.[163] If there is a "substantial bona fide dispute as to whether an agreement to arbitrate exists, the court shall try the issue promptly and summarily."[164] If the court rejects the application, it should order the parties to arbitrate.[165]

3. Federal Forum.

If the FAA governs the arbitration clause and diversity of citizenship or a federal question exists, the parties can litigate the arbitrability of their dispute in a federal forum.[166] The procedures for such litigation are described in William Dorsaneo's *Texas Litigation Guide*, Vol. 3, Ch. 44, § 44.07(3).

E. Appellate Review.

1. Proceedings in State Court.

a. Cases arising under the TAA.

An appeal is generally available to review a trial court's final judgment confirming, modifying, or vacating an arbitration award without directing a rehearing, because these are final orders or judgments.[167]

The TAA also allows for an interlocutory appeal of two types of orders:[168]

1. an order denying an application to compel arbitration; and
2. an order granting an application to stay arbitration.

Although an interlocutory appeal is available under the TAA to challenge a trial court's refusal to enforce an arbitration agreement, it is not available to challenge an order compelling arbitration.[169]

The Texas Supreme Court's decision in *Anglin v. Tipps* has caused some confusion on this issue by erroneously stating that the TAA allows a party to appeal from an interlocutory order granting arbitration.[170] While some courts have dismissed *Anglin's* statement as dictum, it is actually just an incorrect statement about the TAA.[171] The TAA permits an interlocutory appeal only from an order

[155] *In re MHI*, 7 S.W.3d at 923.

[156] TEX. CIV. PRAC. & REM. CODE § 171.026.

[157] 115 S.W.3d 79, 81 (Tex. App.—San Antonio 2003, orig. proceeding).

[158] *Id*.

[159] TEX. CIV. PRAC. & REM. CODE §§ 171.024, 171.096.

[160] TEX. CIV. PRAC. & REM. CODE § 171.025(a).

[161] *Id.* § 171.025(b).

[162] *Brooks v. Pep Boys Auto. Supercenters*, 104 S.W.3d 656, 659-60 (Tex. App.—Houston [1st Dist.] 2003, no pet.).

[163] TEX. CIV. PRAC. & REM. CODE § 171.023.

[164] *Id.*

[165] *Id.*

[166] *Bank One, N.A. v. Shumake*, 281 F.3d 507, 513 (5th Cir. 2002); *Specialty Healthcare Mgmt., Inc. v. St. Mary Parish Hosp.*, 220 F.3d 650, 653 n.5 (5th Cir. 2000).

[167] TEX. CIV. PRAC. & REM. CODE § 171.098(a).

[168] *Id.*

[169] *Id*.

[170] 842 S.W.2d 266, 271-72 (Tex. 1992) (stating "both the Texas and federal acts permit a party to appeal from an interlocutory order granting or denying a request to compel arbitration").

[171] *See Trico Marine Services, Inc. v. Stewart and Stevenson Technical Services, Inc.*, 73 S.W.3d 545 (Tex. App.—Houston [1st Dist.] 2002, no pet.); *Glazer's Wholesale Distrib., Inc. v. Heineken USA, Inc.*, 95 S.W.3d 286 (Tex. App.—Dallas 2001, pet. dism'd by agmt); *Mohamed v. Auto Nation USA Corp.*, 89 S.W.3d 830 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding).

denying a request to compel arbitration, not from an order granting one.

The Texas Supreme Court has not addressed whether mandamus relief is available where the trial court erroneously compels arbitration under the TAA, but most courts of appeals have concluded that it is.[172] In *Glazer's Wholesale Distrib., Inc. v. Heineken USA*, Inc., the Dallas Court of Appeals analyzed the case under traditional mandamus principles, and reasoned that "if a trial court erroneously requires a party to participate in binding arbitration, a party will not have an adequate appellate remedy to protect its substantial right to litigate the issues in open court."[173] Borrowing from cases under the FAA, the court concluded that a party who is compelled to arbitrate without having agreed to do so will have lost its right to have the dispute resolved by litigation.[174] Similarly, the Corpus Court of Appeals in *In re Godt* held that mandamus relief is available to challenge an order compelling arbitration, because a party who is compelled to arbitrate without having agreed to do so will have lost its right to litigate the dispute, and will have no adequate remedy by appeal.[175]

b. Cases arising under the FAA.

In contrast to the TAA, a state trial court's order regarding an arbitration agreement governed by the FAA is not reviewable by interlocutory appeal in Texas courts.[176]

The Texas Supreme Court repeatedly has held that an order denying arbitration under the FAA is reviewable by mandamus.[177] However, the court recently held that mandamus relief is generally *not* available for review of an order compelling arbitration under the FAA.[178] The court's decision in *In re Palacios* aligns Texas law with United States Supreme Court precedent holding that the FAA only allows review of an order granting arbitration if the underlying case is dismissed.[179] In overruling its prior decision in *Freis v. Canales*,[180] which allowed mandamus review on an order granting arbitration, the Texas Supreme Court noted that while "Texas courts applying the FAA follow Texas rather than federal procedure . . . it is important for federal and state law to be as consistent as possible in the area, because federal and state courts have concurrent jurisdiction."[181]

The *Palacios* decision did not conclusively resolve this jurisdictional question because the Texas Supreme Court declined to hold that mandamus review was precluded in all circumstances.[182] Instead, it suggested that review might be available "if a party can meet a 'particularly heavy' mandamus burden to show 'clearly and indisputably that the district court did not have the discretion to stay the proceedings pending arbitration.'"[183]

The Eastland, San Antonio, and Dallas courts of appeals recently have interpreted *Palacios* to mean that orders compelling arbitration may be reviewable by mandamus if the relator satisfies a heightened burden of proof, and have proceeded to the merits of the mandamus petitions.[184] Other courts of appeals, while recognizing that a limited exception exists under *Palacios*, have declined to exercise jurisdiction.[185]

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[172] *See Mohamed v. Auto Nation USA Corp.*, 89 S.W.3d 830 (Tex. App.—Houston [1st Dist.] 2002, orig. proceeding) (holding mandamus relief was available to challenge an order compelling arbitration under either the TAA or the FAA); *see also In re Kepka*, 178 S.W.3d 279 (Tex. App.—Houston [1st Dist.] 2005, orig. proceeding).

[173] 95 S.W.3d 286, 294 (Tex. App.—Dallas 2001, pet. dism'd by agmt).

[174] *Id.*

[175] 28 S.W.3d 732, 738 (Tex. App.—Corpus Christi 2002, orig. proceeding).

[176] *Anglin*, 842 S.W.2d at 272.

[177] *See, e.g., In re Bank One*, No. 06-0093, 2007 WL 549744 (Tex. Feb. 23, 2007) (per curiam); *In re Weekley Homes, L.P.*, 180 S.W.3d 127, 130 (Tex. 2005); *In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69-70 (Tex. 2005).

[178] *In re Palacios*, -- S.W.3d --, 2006 WL 1791683, at *1-2 (Tex. June 30, 2006) (per curiam).

[179] *Green Tree Fin. Corp. v. Randolph*, 531 U.S. 79 (2000).

[180] 877 S.W.2d 283, 284 (Tex. 1994).

[181] *Palacios*, 2006 WL 1791683, at * 1.

[182] *Id.* at *2.

[183] *Id.* (quoting *Apache Bohai Corp., LDC v. Texaco China, B.V.*, 330 F.3d 307, 310-11 (5th Cir. 2003)).

[184] *In re Great Western Drilling, Ltd.*, 211 S.W.3d 828, 835 (Tex. App.—Eastland 2006, orig. proceeding) (holding trial court's order compelling arbitration was reviewable on mandamus where the trial court abused its discretion by staying litigation and compelling parties to arbitrate); *In re Premont Indep. Sch. Dist.*, --S.W.3d--, 2007 WL 390784, at *2 (Tex. App.—San Antonio Feb. 7, 2007, pet. filed) (holding the trial court's order compelling arbitration was reviewable on mandamus where there was no arbitration agreement); *In re Wolff*, No. 05-07-00656-CV, 2007 WL 2120654, at *1 (Tex. App.—Dallas July 27, 2007, orig. proceeding) (holding trial court's order compelling arbitration was reviewable on mandamus where party was entitled to a de novo review of an associate judge's decision).

[185] *See, e.g., In re Jim Walter Homes, Inc.*, 207 S.W.3d 888, 894-95 (Tex. App.—Houston [14th Dist.] 2006, orig. proceeding) (holding that it did not have jurisdiction to review a trial court's order compelling arbitration under the FAA).

c. Dual Proceedings in State Court.

Because of the different appellate remedies available under the TAA and the FAA and the frequent uncertainty about which statute applies, a party seeking review of an order denying a motion to compel or an order staying arbitration must pursue both an interlocutory appeal (in the event the TAA governs) and a petition for writ for mandamus (in the event the FAA governs).[186]

The Texas Supreme Court recently issued a reminder that the FAA typically does not preempt the TAA (unless a provision in the TAA would subvert enforcement of the agreements at issue), so in an agreement involving interstate commerce, the court of appeals will have jurisdiction via either procedural route.[187]

In a concurring opinion in the same case, Justice Brister urged that court discontinue requiring litigants to pursue parallel mandamus and interlocutory appeal proceedings.[188] He stated, "This unnecessary duplication makes arbitration more cumbersome and costly than other cases, rather than the 'simplicity, informality and expedition' intended for them."[189] Brister explained that he would allow parties to file either an interlocutory appeal or an original proceeding, and "have the appellate courts treat it as they think proper."[190] While the majority sympathized with Justice Brister's sentiments, it concluded that the problem was one for the Legislature to address, and it again called upon the Legislature to do so.[191] This year, the Texas Senate passed S.B.1167, which would have authorized an interlocutory appeal of an order denying a motion to compel arbitration under the FAA, but the Texas House did not act on the bill.[192] Nevertheless, one commentator persuasively has argued that the Legislature *already* has amended the TAA in a way that solves this problem.[193]

[186] *Anglin*, 842 S.W.2d at 272.

[187] *In re D. Wilson Constr. Co.*, 196 S.W.3d 774, 780 (Tex. 2006).

[188] *Id.* at 784 (Brister, J., concurring).

[189] *Id*. (quotation omitted).

[190] *Id*.

[191] *Id.* at 780 n.4. (repeating earlier request made in *Anglin*, 842 S.W.2d at 272).

[192] *See* http://www.capitol.state.tx.us/BillLookup/History.aspx?LegSess=80R&Bill=SB1167.

[193] *See* Elizabeth (Heidi) Bloch, *Stop the Madness: There's No Need for Dual Proceedings*, 16 Appellate Advocate 9 (Spring 2003).

2. Proceedings in Federal Court.

In federal court, where federal procedural law controls, the FAA permits an appeal from:

- any final order with respect to an arbitration, regardless of whether it is favorable or hostile to arbitration, 9 U.S.C. § 16(a)(3);
- an order refusing to stay litigation pending arbitration, 9 U.S.C. § 16(a)(1)(A); or
- an order denying a motion to compel arbitration, 9 U.S.C. § 16(a)(1)(B).

Unless a party obtains permission to take an interlocutory appeal under 28 U.S.C. § 1292(b), a party may not appeal from an interlocutory order compelling arbitration or granting a stay of litigation in favor of arbitration.[194] In reconciling Section 16(a)(3) and Section 16(b), the United States Supreme Court has held that when a district court compels arbitration and dismisses the remainder of the action, the order is a final judgment and immediately appealable.[195] However, where the district court stays the litigation pending completion of arbitration, rather than dismiss the case, the order is interlocutory and appellate review is unavailable.[196] This is true even where the district court administratively closes the case.[197]

3. Standard of Review.

Federal courts review a grant or denial of a petition to compel arbitration de novo.[198] The Texas standard is less clear. In *J.M. Davidson, Inc. v. Webster*, the Texas Supreme Court stated that "determination of an arbitration agreement's validity is a legal question subject to *de novo* review."[199] Even after *Webster*, however, several courts of appeals have maintained that a no-evidence standard is proper to review factual questions concerning denial of a motion to compel arbitration.[200]

[194] 9 U.S.C. § 16(b).

[195] *Green Tree Fin. Corp. Alabama v. Randolph*, 531 U.S. 79, 89 (2000).

[196] *Mire v. Full Spectrum Lending, Inc.*, 389 F.3d 163, 167 (5th Cir. 2004).

[197] *Id.*

[198] *Banc One Acceptance Corp. v. Hill*, 367 F.3d 426, 428 (5th Cir. 2004).

[199] 128 S.W.3d 223, 233 (Tex. 2003).

[200] *See Colosi v. Guidry*, 2004 WL 1065442, at *1 (Tex. App.—Houston [1st Dist.] 2004, no pet.); *Forest Oil Corp. v. McAllen*, 2005 WL 3435061, at *2 (Tex. App.—Corpus Christi 2005, pet. filed); *Woodhaven Homes, Inc. v. Alford*, 143 S.W.3d 202, 204 (Tex. App.—Dallas 2004, no pet.). *But*

In his dissenting opinion in *Webster*, Justice Schneider explained that Texas courts review denial of a motion to compel arbitration under a "legal sufficiency" or "no-evidence" standard when factual findings are in dispute.[201] However, if no findings of fact were made, and the only issue is the legal interpretation of an arbitration clause, then the court applies a *de novo* standard.[202]

To the extent that the court may consider a decision to grant a motion to compel arbitration via mandamus, the court likely would review such an order for abuse of discretion.[203]

IV. POST-ARBITRATION LITIGATION

Post-arbitration litigation often is necessary when the losing party fails to fully comply with the arbitrator's decision. The prevailing party may seek judicial confirmation of an award to take advantage of the additional enforcement mechanisms available for a court judgment.

Alternately, the losing party often will ask a court to modify or vacate the award, either in response to the winning party's application for confirmation or on its own motion. These challenges are frequently made in spite of the extremely narrow scope of judicial review of arbitration awards. Before initiating post-arbitration litigation, a party should consider a number of factors set forth below.

A. Procedural considerations prior to initiation of litigation.

1. The finality of the arbitration award.

An arbitral award must be final and definite before it can be reviewed by a court. "To be considered *final*, an arbitration award must be intended by the arbitrator to be a complete determination of every issue submitted. It must resolve all the issues submitted to arbitration definitively enough so that the rights and obligations of the parties, with respect to the issues submitted to the arbitrator, need no further adjudication."[204] For example, an arbitration award was not final when the parties had contracted for a two-phased arbitration process that included a de novo appeal from the first arbitration award, and the appeal from the award had not yet occurred.[205]

2. The forum in which to bring the litigation.

A party seeking to confirm, modify, or vacate an award should also consider whether a federal forum is available and desirable. A choice of forum may implicate a variety of economic and legal factors, including the governing law, the applicable procedure, and the chances of success.[206]

State courts are available for the adjudication of post-arbitration litigation, regardless of whether the arbitration agreement is governed by the TAA or FAA. Indeed, the FAA requires federal courts to recognize the enforceability of any arbitral award entered under the Act, including those confirmed in state court.[207]

The FAA provides that "United States court in and for the district wherein the award was made" has the authority to (1) vacate an arbitration award, or (2) confirm an arbitration award if no court is specified in the agreement of the parties.[208] The provision is not a mandatory venue provision. *See Cortez Byrd Chips, Inc. v. Bill Harbert Construction Co.*, 529 U.S. 193 (2000).[209] However, this provision does not confer federal subject-matter jurisdiction; there must be an independent basis for federal jurisdiction before a district court may entertain an application to confirm or petition to vacate an arbitration award.[210]

Therefore, a party seeking a federal tribunal must be able to invoke diversity jurisdiction or federal question jurisdiction to get in the courthouse door, though domestic arbitration cases will rarely present a federal question. Parties cannot contract for a federal forum because they cannot bestow subject matter jurisdiction by contract.

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see ANCO Ins. Servs. of Houston v. Romero, 27 S.W.3d 1, 5 (Tex. App.—San Antonio 2000, pet. denied) (opting to apply an abuse of discretion standard to factual questions, rather than a no-evidence standard).

[201] 128 S.W.3d 223, 233 (Tex. 2003) (Schneider, J., dissenting).

[202] *Id*; *see also Certain Underwriters at Lloyd's of London v. Celebrity, Inc.*, 950 S.W.2d 375, 377 (Tex. App.—Tyler 1996, no writ).

[203] *Bates v. MTH Homes-Texas, L.P.*, 177 S.W.3d 419, 422 (Tex. App.—Houston [1st Dist.] 2005, no pet.).

[204] Thomas H. Oehmke, *Appealing Adverse Arbitration Awards*, 94 AM. JUR. TRIALS 211, at § 40 (2006).

[205] *Lincoln v. C & N Group, Inc.*, 1997 WL 672626 (Tex. App.—Dallas Oct. 30, 1997, no pet.) (not designated for publication).

[206] *See infra* Part IV.E.2.

[207] *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984).

[208] 9 U.S.C. §§ 9, 10(a).

[209] Thus, a party may face circumstances in which a motion to confirm is filed in one district and a motion to vacate is filed in another district.

[210] *See, e.g., Smith v. Rush Retail Centers, Inc.*, 360 F.3d 504 (5th Cir. 2004).

3. The deadlines for action.
   a. State Court.

The TAA imposes deadlines for parties seeking to modify or vacate arbitration awards, which apply to all cases in Texas courts, regardless of whether the FAA applies to the substantive dispute.[211] Under the TAA, an application to vacate must be made within 90 days after the date of delivery of a copy of the award, or within 90 days after the date the party knew or should have known of corruption, fraud, or other undue means as a grounds for vacating the award (subject to the possible acceleration of this deadline described below).[212] Similarly, an application to modify or correct an award must be made no later than the 90th day after the date of delivery of a copy of the award to the applicant (again, subject to the possible acceleration of this deadline described below).[213] In contrast, there is no statutory limitations period for the filing of an application to confirm an award.[214]

A party seeking to confirm an award should consider two strategic options. First, it can delay filing an application for confirmation for at least 90 days, hoping that its adversary will fail to move for vacatur within the statutory period, at which point, its application for confirmation could proceed unimpeded.[215] Second, it can move quickly to file an application for confirmation and set it for a prompt hearing, which has the effect of accelerating its adversary's 90-day deadline to file a motion to vacate or modify the award. This option arises from the holding in *Hamm v. Millennium Income Fund, L.L.C.*, where the court concluded that a motion to vacate or modify an award had to be pending or already ruled upon at the time a court considered an application for confirmation.[216] The court reasoned that judgments confirming arbitration awards were entitled to the same finality as judgments in general, and the policy of expediting arbitration matters would not be promoted by allowing a party to try to vacate an award that had already been confirmed.[217]

It is worth noting that at least one court has concluded that the 90-day deadline for filing a motion for vacatur applies only to the statutory grounds set forth in TEX. CIV. PRAC. & REM. CODE § 171.088, not the common law grounds discussed *infra* at Part IV.E.1.a.[218]

Finally, a request for modification or correction presented to an arbitrator pursuant to TEX. CIV. PRAC. & REM. CODE § 171.054, prior to the initiation of litigation, does not toll the 90-day statutory periods referenced above.[219] However, if the award is ultimately modified by the arbitrator, at least one court has counted the 90-day period from the date of the amended decision.[220]

b. Federal Court.

For FAA cases brought in federal court, a party seeking confirmation must file its application "at any time within one year after the award is made."[221] On the other hand, a party challenging an award must serve its notice of a motion to vacate, modify or correct the award "upon the adverse party or his attorney within three months after the award is filed or delivered."[222] This limitations period applies whether a vacatur, modification or correction is sought in an original petition or in a counterclaim filed in response to an application for confirmation. As in state court, a party seeking confirmation should consider waiting for the expiration of the three-month statutory period for filing a vacatur before filing its application to confirm.

4. Attorneys' Fees Not Recoverable.

The TAA allows a court, in a proceeding to confirm, modify, or correct an award, to award "costs of the application and of the proceedings subsequent to the

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[211] *Hamm v. Millennium Income Fund, L.L.C.*, 178 S.W.3d 256, 260 n.3 (Tex. App.—Houston [1st Dist.] 2005, pet. denied).

[212] TEX. CIV. PRAC & REM. CODE § 171.088(b).

[213] *Id.* § 171.091(b).

[214] *Id.* § 171.087.

[215] *See Smith v. J-Hite, Inc.*, 127 S.W.3d 837 (Tex. App.—Eastland 2003, no pet.) (when successful party at arbitration filed an application to confirm the award after 90 days had run, the losing party could not assert a counterclaim to set aside the award, notwithstanding the counterclaim savings statute.)

[216] 178 S.W.3d 256, 262-68 (Tex. App.—Houston [1st Dist.] 2005, pet. denied).

[217] *Id.*; *see also City of Baytown v. C.L. Winter, Inc.*, 886 S.W.2d 515, 520-21 (Tex. App.—Houston [1st Dist.] 1994, writ denied) (rejecting argument that district court was barred from confirming the award during the 90-day statutory period allotted to file application to vacate, modify or correct the award).

[218] *See East Texas Salt Water Disposal Co. v. Hughes*, 2006 WL 300410 (Tex. App.—Tyler Feb. 8, 2006, pet. denied).

[219] *See Teleometrics Int'l Inc. v. Hall*, 922 S.W.2d 189, 192 (Tex. App.—Houston [1st Dist.] 1995, writ denied).

[220] *Louisiana Natural Gas Pipeline, Inc. v. Bludworth Bond Shipyard, Inc.*, 875 S.W.2d 458, 462 (Tex. App.—Houston [1st Dist.] 1994, writ denied).

[221] 9 U.S.C. § 9.

[222] *Id.* § 12.

application."[223] Several courts have concluded that this language allows the recovery of court costs alone, and not attorneys' fees.[224] This is true even if the underlying dispute (such as a breach of contract claim) would have allowed recovery of attorneys' fees.[225]

It is not at all unusual for parties to spend significant attorneys' fees in seeking to confirm an award through the trial court and appeal. Once an arbitrator has made an award, there is no statutory basis for recovery of attorneys' fees incurred in seeking to either confirm or vacate that award. One possible solution to this problem is to ask the arbitrator to award conditional attorneys' fees in the event of a challenge to the award. This request would be no different than a trial court awarding conditional fees in the event of an appeal. Such fees, of course, would be permissible only if fees are recoverable in the first instance, either because the arbitration agreement allows for their recovery, or because the claim is one for which fees are recoverable.

Given the strong public policy favoring arbitration as a less expensive alternative to litigation, it makes sense to provide financial disincentives to a party seeking to overturn an award. An award of fees to the prevailing party could help fix this problem.

5. Considerations Specific to a Motion for Vacatur.

a. Was error preserved?

Before initiating a challenge to an arbitration award, counsel should confirm that the error was properly preserved in the arbitration proceeding. "A party may not sit idly by during an arbitration procedure and then collaterally attack that procedure on grounds not raised before the arbitrator when the result turns out to be adverse."[226] For example, a party can waive an otherwise valid objection to the partiality of the arbitrator by proceeding with arbitration despite knowledge of facts giving rise to such an objection, even when the arbitrator failed to disclose the grounds for bias.[227]

One commentator wisely advises that to preserve error, a party should make an objection "to the arbitrator and opposing parties orally, followed by a writing that is also sent to the arbitrator, opponents, and any tribunal administrator" so that there is a "paper trail detailed enough for a reviewing court to treat as a *de facto* record."[228] "When the evidentiary hearing commences (whether or not there is a record), the written objection should be proffered as part of the record, and later, preserved in any hearing briefs."[229]

b. Absence of rationale for arbitral decision.

In general, under either the TAA or FAA, an arbitrator need not explain the rationale behind the award.[230] Even if the parties request findings of facts and conclusions of law, the arbitrator is not obligated to make such findings.[231] The absence of a reasoned decision can preclude effective judicial review under some of the available grounds for vacatur (e.g., manifest disregard of the law).[232] But while the requirement of a reasoned decision "would help to uncover egregious failures to apply the law to an arbitrated dispute . . . ., such a rule also would undermine the twin goals of settling disputes efficiently and avoiding long and expensive litigation."[233]

The parties may, by agreement, require that the arbitrator provide a reasoned decision (including findings of fact and conclusions of law). This agreement can be made at the time of the original contract, before the appointment with the arbitrator, or by subsequent agreement with the arbitrator.[234]

c. State of the "record."

A party contemplating filing a motion for vacatur should consider whether there is an adequate record to support the anticipated challenge, because it will bear

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[223] TEX. CIV. PRAC & REM. CODE § 171.092(b).

[224] *See, e.g., Monday v. Cox*, 881 S.W.2d 381 (Tex. App.—San Antonio 1994, writ denied).

[225] *Kline v. O'Quinn*, 874 S.W.2d 776 (Tex. App.—Houston [14th Dist.] 1994, writ denied).

[226] *Bossley v. Mariner Fin. Group, Inc.*, 11 S.W.3d 349, 351-52 (Tex. App.—Houston [1st Dist.] 2000), *aff'd*, 79 S.W.3d 30 (Tex. 2002).

[227] *See Kendall Builders, Inc. v. Chesson*, 149 S.W.3d 796 (Tex. App.—Austin 2004, pet. denied).

[228] Thomas H. Oehmke, *Appealing Adverse Arbitration Awards*, 94 AM. JUR. TRIALS 211, at § 77 (2006).

[229] *Id.*

[230] *Gray v. Noteboom*, 159 S.W.3d 750, 754 (Tex. App.—Fort Worth 2005, pet. denied); *Thomas v. Prudential Sec., Inc.*, 921 S.W.2d 847 (Tex. App.—Austin 1996, no writ); *Valentine Sugars, Inc. v. Donau Corp.*, 981 F.2d 210, 214 (5th Cir. 1993); *Anderman/Smith Operating Co. v. Tenn. Gas Pipeline Co.*, 918 F.2d 1215, 1219 n.3 (5th Cir. 1990).

[231] *Noteboom*, 159 S.W.3d at 753-54; *see* TEX. CIV. PRAC. & REM. CODE § 171.053(a) (The TAA requires only that the arbitration award "be in writing and signed by each arbitrator joining in the award").

[232] *See, e.g., Pfeifle v. Chemoil Corp.*, 73 Fed. Appx. 720 (5th Cir. 2003) ("Stated simply, we cannot determine from the arbitrators' decision what, if any, rationale produced their [damages] award.").

[233] Oehmke, *supra* note 228 at § 43.

[234] *Id.*

the "burden to bring forth a complete record that establishes [its] basis for relief."[235] When there is no transcript of the arbitration proceedings available, a reviewing court will presume that evidence supported the arbitration panel's award.[236] For example, a court held it could not review a claim that an arbitrator exceeded the scope of her authority where the appellant failed to furnish a record of the arbitration proceedings.[237] Also, when a losing party asserted that its adversary was not entitled to an award of punitive damages, the court rejected the challenge because, in the absence of a transcription of the arbitration proceedings, it was "unable to determine what claims were submitted or what evidence was offered before the arbitrators."[238]

d. Availability of discovery to supplement the record.

In most cases, the "record" for a vacatur action will consist of (1) the arbitration award, (2) the underlying contract between the parties, (3) the transcript of the arbitration proceedings, and (4) any written briefing or documentary evidence submitted to the arbitrators. While no Texas cases have shed light on the availability of discovery to bolster this record, commentators suggest that parties should have at least a limited opportunity to obtain written and oral discovery in certain situations.[239] And discovery is generally available in federal court.[240] An arbitrator may be deposed regarding claims of bias or prejudice, as long as there is clear evidence of impropriety and the questioner avoids questioning the arbitrator on the thought processes underlying his decision.[241] Generally, other testimonial evidence will be limited to the rare cases in which it would be helpful in establishing the intent of the parties, the meaning of disputed terms in the underlying agreement, or the procedural history of the dispute.

e. Possibility of sanctions for frivolous appeal.

Finally, to avoid sanctions, a party should proceed with a vacatur motion only if they have a good faith basis for challenging the arbitral award. Texas courts thus far have been reluctant to award sanctions in unsuccessful vacatur actions. In *Baker Hughes Oilfield Operations, Inc. v. Hennig Prod. Co.*, the prevailing party sought sanctions, alleging that the party seeking vacatur "presented an incomplete record on appeal, raised critical issues for the first time on appeal, and filed an inadequate brief misstating the record and making unsupported accusations."[242] The court refused to award sanctions because the record did not reveal "truly egregious" conduct.[243]

However, courts elsewhere have become more aggressive in awarding sanctions. In *B.L. Harbert, Int'l, LLC v. Hercules Steel Co.*, the Eleventh Circuit warned that "[i]f we permit parties who lose in arbitration to freely relitigate their cases in court, arbitration will do nothing to reduce congestion in the judicial system; dispute resolution will be slower instead of faster; and reaching a final decision will cost more instead of less."[244] It thus concluded that "[a] realistic threat of sanctions may discourage baseless litigation over arbitration awards and help fulfill the purposes of the pro-arbitration policy contained in the FAA. . . . The warning this opinion provides is that in order to further the purposes of the FAA and to protect arbitration as a remedy we are ready, willing and able to consider imposing sanctions in appropriate cases."[245] The Seventh Circuit recently issued a similar warning.[246]

B. Standard of Review.

1. Default Standard.

Judicial review of an "arbitration decision is 'extremely narrow' because Texas law favors arbitration."[247] A reviewing court may not substitute its judgment for that of the arbitrators merely because it

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[235] *Anzilotti v. Gene D. Liggin, Inc.*, 899 S.W.2d 264, 267 (Tex. App.—Houston [14th Dist.] 1995, no writ).

[236] *Thomas v. Prudential Sec., Inc.*, 921 S.W.2d 847 (Tex. App.—Austin 1996, no writ).

[237] *Grand Homes 96, L.P. v. Loudermilk*, 208 S.W.3d 696, 706 (Tex. App.—Fort Worth 2006, pet. filed).

[238] *Kline v. O'Quinn*, 874 S.W.2d 776, 783 (Tex. App.—Houston [14th Dist.] 1994, writ denied).

[239] *See* George Chamberlain, *Cause of Action to Vacate Arbitration Award on Ground of Excess of Powers by Arbitrator*, 27 CAUSES OF ACTION 113, §§ 18-19, 26-27.

[240] *See Matter of Andros Compania Maritima, S.A.*, 579 F.2d 691, 702 (2d Cir. 1978).

[241] *Legion Ins. Co. v. Ins. Gen. Agency, Inc.*, 822 F.2d 541, 543 (5th Cir. 1987); Oehmke, *supra* note 228, at § 105.

[242] 164 S.W.3d 438, 448 (Tex. App.—Houston [14th Dist.] 2005, no pet.).

[243] *Id.*

[244] 441 F.3d. 905, 906 (11th Cir. 2006).

[245] *Id.* at 913-14.

[246] *See CUNA Mut. Ins. v. Office and Prof'l Employees Int'l Union, Local No. 39*, 443 F.3d 556 (7th Cir. 2006) ("The filing of meritless suits and appeals in arbitration cases warrants Rule 11 sanctions.")

[247] *Universal Computer Sys., Inc. v. Dealer Solutions*, 183 S.W.3d 741, 752 (Tex. App.—Houston [1st Dist.] 2005, pet. denied) (citations omitted).

would have reached a different result.[248] Every reasonable presumption must be indulged to uphold the arbitrators' decision, and none is indulged against it.[249] The court may not review the arbitrators' decision on the merits even if it is alleged that the decision is based on factual error or it misinterprets the parties' agreement.[250]

Appellate courts apply a *de novo* standard of review of a district court's order confirming an arbitration award.[251] In reviewing an order granting a vacatur, the Fifth Circuit accepts findings of fact that are not clearly erroneous and applies a de novo standard to questions of law and the application of law to facts.[252] Both the Fifth Circuit and Texas courts emphasize that appellate review is "intended to reinforce the strong deference due an arbitrative tribunal."[253]

2. Modification by Contract.

Both the Fifth Circuit and at least one Texas appellate court have held that parties to an arbitration agreement can contractually agree for a different or expanded scope of appellate review, although such an intent must be clearly and unmistakably expressed.[254]

In *Gateway*, the Fifth Circuit enforced an arbitration provision that provided that the "arbitration decision shall be final and binding on both parties, except that errors of law shall be subject to appeal."[255] In a subsequent case, the Fifth Circuit construed a similar provision – permitting appeals of "errors of law" – to apply only to pure legal questions.[256] It refused to apply this provision to mixed questions of law and fact, like the evidentiary sufficiency challenges urged by the appellants.[257] The court reasoned that, absent a definition of the phrase "errors of law" in the arbitration agreement, the phrase should be read narrowly, because a broader reading would have encompassed all of the arbitrator's findings.[258]

The Fifth Circuit expanded upon its *Gateway* holding in *Hughes Training, Inc. v. Cook*, when it enforced an arbitration clause that permitted review of an arbitrator's findings of fact under the same standard that an appellate court would apply to a trial court's findings.[259]

The *Gateway* holding has been adopted by the Third and Fourth Circuits, but rejected by the Eighth, Ninth and Tenth Circuits, creating a circuit split that will require resolution by the United States Supreme Court.[260] A Supreme Court decision rejecting the *Gateway* holding could deny parties to an existing arbitration agreement the judicial safety net for which they contracted.

Courts are much less inclined to permit parties to contractually limit or eliminate appellate review. The San Antonio Court of Appeals recently considered a provision in an arbitration agreement that stated that "[a]n award or determination of the arbitration tribunal shall be final and conclusive upon the parties . . . and no appeal thereof shall be made by the parties."[261] It held that, notwithstanding this provision, it would consider a challenge that the award was tainted by fraud, misconduct, or gross mistake – a ground for vacatur available under the common law.[262] It also held that the statutory grounds for vacating or modifying an award, set forth in Sections 171.088 and 171.091 of the Texas Civil Practice and Remedies Code, could not be waived.[263]

Federal circuit courts have also weighed in on this question. In *MACTEC, Inc. v. Gorelick*, the Tenth Circuit held that a clear and unequivocal agreement foreclosing judicial review of an arbitration award *beyond the district court level is enforceable*.[264] The

[248] *Id.*

[249] *Id.* (citing *CVN Group, Inc. v. Delgado*, 95 S.W.3d 234, 238 (Tex. 2002)).

[250] *Major League Baseball Players Ass'n v. Garvey*, 532 U.S. 504, 509 (2001).

[251] *Executone Info Sys., Inc. v. Davis*, 26 F.3d 1314, 1320 (5th Cir. 1994); *Peacock v. Wave Tec Pools, Inc.*, 107 S.W.3d 631 (Tex. App.—Waco 2003, no pet.).

[252] *Hughes Training, Inc. v. Cook*, 254 F.3d 588, 592 (5th Cir. 2001).

[253] *McIlroy v. PaineWebber, Inc.*, 989 F.2d 817 (5th Cir. 2003); *accord Int'l Bank of Commerce—Brownsville v. Int'l Energy Dev. Corp.*, 981 S.W.2d 38 (Tex. App.—Corpus Christi 1998, pet. denied).

[254] *Gateway Technologies, Inc. v. MCI Telecomm. Corp.*, 64 F.3d 993 (5th Cir. 1995); *Tanox, Inc. v. Akin Gump, Strauss, Hauer & Feld, L.L.P.*, 105 S.W.3d 244, 252 (Tex. App.—Houston [14th Dist.] 2003, pet. denied); *see also Mariner Fin. Group, Inc. v. Bossley*, 79 S.W.3d 30, 42-48 (Tex. 2002)(Owen, J., concurring).

[255] 64 F.3d at 996.

[256] *Harris v. Parker Coll. of Chiropractic*, 286 F.3d 790, 794 (5th Cir. 2002).

[257] *Id.*

[258] *Id.*

[259] 254 F.3d 588, 590 (5th Cir. 2001).

[260] *See* Christopher D. Kratovil, *Judicial Review of Arbitration Awards*, UT State and Federal Appeals Conference (June 2006); Margaret Moses, *Can Parties Tell Courts What To Do? Expanded Judicial Review Of Arbitral Awards*, 52 U. KAN. L. REV. 429, 465 (2004).

[261] *Barsness v. Scott*, 126 S.W.3d 232, 238 (Tex. App.—San Antonio 2003, pet. denied).

[262] *Id.*

[263] *Id.*

[264] 427 F.3d 821 (10th Cir. 2005).

court held that private contractual restrictions on appellate review fulfill the FAA's fundamental purpose of reducing "litigation costs by providing a more efficient forum."[265] The court cautioned, however, that a clause precluding judicial review of any kind probably would be unenforceable. In *Hoeft v. MVL Group, Inc.*, the Second Circuit held that the vacatur grounds set forth in 9 U.S.C. § 10 and in the common law "represent a floor for judicial review of arbitration awards below which parties cannot require courts to go, no matter how clear the parties' intentions."[266]

Parties seeking to incorporate some measure of "appellate" review of an arbitral decision might consider contracting for a private appellate arbitration panel as a substitute for judicial review, especially given the expense of post-award litigation and the fact that the *Gateway* decision might one day be reversed. *See infra* Part IV.F.

C. Confirming an Award.

The procedures for confirming an award set forth in the TAA are equally available with respect to an arbitration clause whose enforceability is governed by the FAA. The TAA requires a court, on application of a party, to confirm an arbitration award unless grounds are offered for vacating, modifying, or correcting the award.[267] The FAA contains a nearly identical provision.[268]

If no proceeding is before the court, a party may initiate one by filing a compliant or petition. Arbitration awards may be confirmed through summary judgment, if the moving party can establish that no issues of material fact prohibit confirmation of the award.[269]

Although an arbitration award has the same effect as a judgment of a court of last resort, confirming an award through the court allows the successful party to take advantage of all enforcement proceedings that are available for other judgments.[270]

D. Modifying an Award.

1. State Law.

The grounds for modifying an award in court are extremely limited. Under the TAA, an award may be modified only if the award contains "an evident miscalculation of numbers," or "an evident mistake in the description of a person, thing, or property referred to in the award."[271] In addition, an award may be modified or corrected in a manner that does not affect the merits if the arbitrators have made an award with respect to a matter not submitted to them, or if the form of the award is imperfect.[272]

Before resorting to litigation, a party can give the arbitrator an opportunity to modify, correct, or clarify its decision on the grounds set forth above, by filing an application for modification or correction with the arbitrator within 20 days after the award is delivered to the applicant.[273] However, any modification cannot affect the merits of, and must be consistent with, the original arbitral decision.[274]

2. Federal Law.

The grounds for modifying an award under the FAA are virtually identical to those under the TAA. 9 U.S.C. § 11. In addition, courts are authorized to substitute their own judgment for that of an arbitrator if the arbitration award, left unchanged, would violate public policy.[275]

E. Vacating an Award.

1. Grounds.

a. State Law.

(1) TAA.

Grounds for vacating an award under the TAA are limited. Because of the great deference courts must give to arbitration awards, judicial scrutiny focuses on the integrity of the process, not the propriety of the result.[276] Even the fact that the relief granted by the arbitrators could not or would not be granted by a court

[265] *MACTEC, Inc. v. Gorelick*, 427 F.3d 821, 826 (10th Cir. 2005).

[266] 343 F.3d 57, 64 (2d Cir. 2003).

[267] TEX. CIV. PRAC. & REM. CODE § 171.087.

[268] 9 U.S.C. § 9.

[269] *See Baker Hughes Oilfield Operations, Inc. v. Hennig Prod. Co.*, 164 S.W.3d 438, 442-443 (Tex. App.—Houston [14th Dist.] 2005, no pet.).

[270] *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984); *City of Baytown v. C.L. Winter, Inc.*, 886 S.W.2d 515, 518 (Tex. App.—Houston [1st Dist.] 1994, writ denied); TEX. CIV. PRAC. & REM. CODE § 171.092; 9 U.S.C. § 13.

[271] TEX. CIV. PRAC. & REM. CODE § 171.091(a)(1).

[272] *Id.* § 171.071(2) and (3).

[273] *Id.* § 171.054.

[274] *Barsness v. Scott*, 126 S.W.3d 232 (Tex. App.—San Antonio 2003, pet. denied).

[275] *W.R. Grace & Co. v. Local Union 759*, 461 U.S. 757, 766 (1983).

[276] *TUCO, Inc. v. Burlington N. R.R. Co.*, 912 S.W.2d 311, 315 (Tex. App.—Amarillo 1995), *modified on other grounds*, 960 S.W.2d 629 (Tex. 1997).

of law or equity is not a ground for vacating or refusing to confirm an arbitration award.[277]

In addition, courts must indulge every reasonable presumption to uphold an arbitrator's decision.[278] A trial court may not substitute its judgment for the arbitrator's merely because it would have reached a different conclusion.[279] Absent a statutory or common law ground to vacate or modify an arbitration award, a reviewing court lacks jurisdiction to review complaints, including the sufficiency of the evidence or errors of substantive law.[280]

The grounds for vacating an award set forth in the TAA are follows: [281]

- If the award was obtained by corruption, fraud, or other undue means;
- If the rights of a party were prejudiced by evident partiality by a neutral arbitrator, corruption in an arbitrator, or misconduct or willful behavior of an arbitrator;
- If the arbitrators exceed their powers, refused to postpone the hearing after a showing of sufficient cause, refused to hear evidence material to the controversy, or conducted a hearing contrary to the TAA or in a manner that substantially prejudiced the rights of a party; or
- If there was no agreement to arbitrate, the parties were not compelled by the court to arbitrate, and the party opposing the arbitration did not participate in the hearing without raising the objection.

Examples of recent successful vacaturs:

Under Section 171.088(a)(2). In *Houston Village Builders v. Falbaum*, the court upheld a trial court's decision to vacate an arbitration award based on "evident partiality" by the sole arbitrator.[282] The dispute involved a construction claim against a homebuilder that was a member of the Greater Houston Builders Association. The arbitrator revealed that he too was a member of that association, but failed to reveal that he had, in the past, represented the association as an attorney. The court concluded that evident partiality was established from the nondisclosure itself, regardless of whether the non-disclosed information necessarily established partiality or bias.

In doing so, the court relied on the Supreme Court's holding in *Burlington Northern Railroad Co. v. Tuco, Inc.*, that a prospective neutral arbitrator exhibits evident partiality if he or she does not disclose facts which might, to an objective observer, create a reasonable impression of the arbitrator's partiality.[283] In *Tuco*, the court found evident partiality where an arbitrator failed to disclose the acceptance of substantial referral from the law firm of a non-neutral co-arbitrator during the course of the arbitration.

In *J.D. Edwards World Solutions v. Estes, Inc.*, the court found that an arbitrator's failure to disclose a business relationship between one of the parties and the neutral arbitrator established evident partiality.[284]

In *Mariner Financial Group, Inc. v. Bossley*, the Texas Supreme Court found that a fact issue existed as to whether the chair of the arbitration panel was "evidently partial" based on the arbitrator's failure to disclose a prior adverse relationship with one of the parties' expert witnesses.[285]

Under Section 171.088(a)(3). An award can be vacated if the arbitrator has exceeded his or her powers by issuing an award that goes beyond the scope of the agreement of the parties.[286] An award may not, however, be vacated based on an "evident mistake" in failing to award damages.[287]

In *Peacock*, a swimming pool contractor and homeowner executed an agreement to arbitrate, in an effort to resolve a dispute over a construction contract.[288] Because the arbitration agreement, and not the construction contract, defined the scope of the arbitrator's authority, the arbitrator exceeded his authority in ordering homeowner to pay an amount in addition to contract price for rock removal, even though construction contract provided for an additional payment for "unforeseen circumstances," where

[277] TEX. CIV. PRAC. & REM. CODE § 171.090.

[278] *IPCO-G & C Joint Venture v. A.B. Chance Co.*, 65 S.W.3d 252 (Tex. App.—Houston [1st Dist.] 2001, pet. denied).

[279] *City of Baytown v. C.L. Winter, Inc.*, 886 S.W.2d 515, 518 (Tex. App.—Houston [1st Dist.] 1994, writ denied).

[280] *J.J. Gregory Gourmet Services, Inc., v. Antone's Import*, 927 S.W.2d 31, 33 (Tex. App.—Houston [1st Dist.] 1995, no writ).

[281] TEX. CIV. PRAC. & REM. CODE § 171.088(a)(1)-(4).

[282] 105 S.W.3d 28 (Tex. App.—Houston [14th Dist.] 2003, pet. denied).

[283] 960 S.W.2d 629 (Tex. 1997).

[284] 91 S.W.3d 836, 844 (Tex. App.—Fort Worth 2002, pet. denied).

[285] 79 S.W.3d 30, 32-35 (Tex. 2002).

[286] *Peacock v. Wave Tec Pools, Inc.*, 107 S.W.3d 631 (Tex. App.—Waco 2003, no pet.).

[287] *Callahan & Assoc. v. Orangefield ISD*, 92 S.W.3d 841 (Tex. 2002).

[288] 107 S.W.3d at 631.

contractor did not seek such payment in the arbitration agreement.

In *Robinson v. West*, the court concluded that the arbitrator exceeded his authority by entering an award that did not dissolve the firm, when the parties' agreement to submit the dispute to an arbitrator stated that the firm would be dissolved.[289]

In *Barsness v. Scott*, the court vacated an arbitration panel's modified award, because the panel exceeded its authority in modifying the award to the extent that the modification rendered the award inconsistent with the merits of the original arbitral decision.[290]

(2) Common Law Grounds.

Because statutory arbitration is cumulative of the common law, an arbitration award governed by the TAA may also be set aside on common law grounds.[291] Such grounds, however, are similarly limited, in that common law allows a trial court to set aside an arbitration award "only if the decision is tainted with fraud, misconduct, or gross mistake as would imply bad faith and failure to exercise honest judgment."[292]

In addition, under the common law, a trial court can vacate an arbitrator's award if the award violates public policy or exceeds the scope of the arbitrator's authority.[293] In *CVN Group, Inc. v. Delgado*, the court noted that an illegal contract (for gambling, for example) that is unenforceable through litigation cannot gain legitimacy through arbitration.[294] At issue in *CVN Group* was the arbitrator's declaration of a valid mechanic's lien, despite the homeowners' arguments that the constitutional and statutory requirements had not been satisfied and that the award was thus against public policy. Noting that the evidence regarding the validity of the lien was disputed, the court refused to second-guess the arbitrator's conclusion that the lien was, in fact, valid.

Interestingly, the Texas Supreme Court in both *CVN Group* and in *Callahan*,[295] suggested that it may be an open question in Texas as to whether the statutes governing arbitration have preempted common law grounds for attacking an arbitrator's award. In neither case was the issue raised by the parties, and the court assumed, without deciding, that common law grounds are still viable. The court could have been signaling that it would be willing to address the issue if it is properly raised.

b. Federal Law.

The grounds for vacating an award under the FAA are similar to those found in the TAA:[296]

- Where the award was procured by corruption, fraud, or undue means;
- Where there was evident partiality or corruption in the arbitrators;
- Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy, or of any other misbehavior by which the rights of any party have been prejudiced; or
- Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

Under the common law, a trial court can vacate an arbitrator's award if the award violates public policy.[297] The party making the challenge must direct the court to "laws and legal precedents" that are "explicit, well defined, and dominant."[298]

In addition, the Fifth Circuit has joined other courts of appeals that allow an arbitration award to be vacated when the arbitrators have acted in "manifest disregard of the law."[299] However, the court emphasized the extremely limited nature of this ground for relief. A reviewing court can vacate an award under this ground only if it finds that (1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether, (2) the law ignored by the arbitrators was well-defined, explicit, and clearly

[289] 2004 WL 178586 (Tex. App.—Eastland 2004), *rev'd on other grounds*, 180 S.W.3d 575 (Tex. 2005).

[290] 126 S.W.3d 232 (Tex. App.—San Antonio 2003, pet. denied).

[291] *Massey v. Galvan*, 822 S.W.2d 309, 315-16 (Tex. App.—Houston [14th Dist.] 1992, writ denied).

[292] *Teleometrics Int'l, Inc. v. Hall*, 922 S.W.2d 189, 193 (Tex. App.—Houston [1st Dist.] 1995, writ denied); *IPCO-G&C Joint Venture v. A.B. Chance Co.*, 65 S.W.3d 252, 256 (Tex. App.—Houston [1st Dist.] 2001, pet. denied).

[293] *Lee v. El Paso County*, 965 S.W.2d 668, 672 (Tex. App.—El Paso 1998, pet. denied).

[294] 95 S.W.3d 234 (Tex. 2002).

[295] *Callahan*, 92 S.W.3d at 844.

[296] 9 U.S.C. § 10(a).

[297] *United Paperworkers Int'l Union v. Misco, Inc.*, 484 U.S. 29, 42 (1987).

[298] *Prestige Ford v. Ford Dealer Computer Servs., Inc.*, 324 F.3d 391, 396 (5th Cir. 2003).

[299] *Brabham v. A.G. Edwards & Sons, Inc.*, 376 F.3d 377, 382-86 (5th Cir. 2004).

applicable to the case; and (3) the award results in significant injustice to the losing party.[300] The Fifth Circuit has never approved the vacatur of an award for manifest disregard.

The Fifth Circuit recently explored the scope of the "evident partiality" grounds for vacatur in *Positive Software Solutions, Inc. v. New Century Mortgage Corp*.[301] The district court had vacated an arbitration award because the arbitrator did not disclose that, more than seven years before the arbitration, he had served as co-counsel with one of the lawyers for a party to the arbitration in unrelated litigation. After a panel affirmed the district court's decision, the Fifth Circuit reviewed the case en banc and reversed the district court's vacatur.[302] The court held that an arbitration award may not be vacated based on a trivial or insubstantial prior relationship between the arbitrator and the parties to the proceeding.[303] The court explained that on its face, the FAA, sets out a stern standard, requiring bias to be clearly evident.[304] The court held that the "draconian remedy" of vacatur is warranted only when a nondisclosure involves "a significant compromising relationship."[305]

2. Likelihood of Success.

Given the limited grounds for vacating an arbitration award and the onerous standard of review, the conventional wisdom is that vacaturs rarely are successful. A recent study has shed light on the degree of difficulty of vacating an award, as well as which grounds for vacatur are most successful.[306]

Lawrence Mills reviewed every case, state and federal, published and unpublished, reported between January 1, 2004, and October 31, 2004, in which a court decided a motion to vacate on any of the FAA grounds, excluding employment termination and discrimination suits, as well as statutorily mandated arbitrations in insurance and public contracting disputes.

Of the 182 cases in which vacatur was sought, the motion to vacate succeeded 37 times, or in 20% of the cases.[307] This percentage fell substantially if the comparison is to the total number vacatur grounds asserted in these cases. The parties successfully asserted only 40, or about 14%, of the 277 grounds advanced for vacatur.[308] State courts were much more likely to vacate than federal courts (25.8% to 9.7%).

The most frequently asserted and most successful of the grounds for vacatur was the allegation that the arbitrators had "exceeded their powers, or so imperfectly executed them that a . . . final and definitive award upon the subject matter submitted was not made." This ground was asserted 101 times in the cases, and succeeded in 21, or about 20.8%, of them. The next most-cited ground, that arbitrators "manifestly disregarded the law," was much less successful, succeeding in only 2 out of 52 cases.

The authors of this article, seeking more Texas-specific data, reviewed all Texas state and federal cases from January 1, 2003 through March 31, 2007 in which a court reached the merits of a motion to vacate. After excluding collective bargaining cases and other cases not arising under the TAA or FAA, we found 38 such cases, in which there was a total of 59 grounds for vacatur asserted. During this period, the courts granted vacatur in whole or in part on five occasions, which constituted 13.1% of the total cases or 8.5% of the total grounds for vacatur asserted. And all five occasions were in state court, rather than federal court, suggesting that the choice of forum can make a difference. Note that this analysis of case law would not have captured vacatur decisions by Texas trial courts that were not reviewed on appeal, either because no appeal was taken or because the appellate court lacked jurisdiction to consider the decision (as would be the case if the trial court ordered a rehearing before the arbitrators).[309]

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[300] *Id*. at 392.

[301] 476 F.3d 278 (5th Cir.) (en banc), *cert. denied*, -- S. Ct. --, 2007 WL 1090443 (June 11, 2007).

[302] *Id*. at 279-80.

[303] *Id*. at 283.

[304] *Id*. at 281.

[305] *Id*. at 286. The Texas Supreme Court has adopted a more lenient standard. *See Burlington Northern R.R. Co. v. TUCO, Inc.*, 960 S.W.2d 629 (Tex. 1997) (holding a neutral arbitrator's failure to disclose his acceptance of a substantial referral from the law firm of a non-neutral co-arbitrator during the course of the arbitration proceedings established evident partiality as a matter of law); *see also* Stephen K. Huber, *Addressing Undisclosed Arbitrator Bias: The Law of "Evident Partiality,"* 39 THE ADVOCATE (STATE BAR LITIGATION SECTION REPORT) at 49 (Summer 2007) ("The rule adopted by the Texas Supreme Court can be stated concisely: an arbitration award will be vacated if a neutral arbitrator fails to 'disclose facts which might, to an objective observer, create a reasonable impression of the arbitrator's partiality.'").

[306] *See* Lawrence R. Mills et al., *Vacating Arbitration Awards*, Vol. 11, No. 4, DISPUTE RESOLUTION JOURNAL 23 (Summer 2005).

[307] *Id.* at 24.

[308] *Id.*

[309] *See, e.g., Bison Building Materials, Ltd. v. Aldridge*, 2006 WL 2641280, at **4-5 (Tex. App.—Houston [1st Dist.] 2006, pet. filed) (holding that it lacked jurisdiction to consider trial court's vacatur decision).

While the small sample size undoubtedly affects the utility of this data, the numbers provide at least some indication that vacating an arbitration award in Texas may be even more difficult than it is nationally.

3. Remedy if Vacated.
   a. State Court.

If an arbitration award is vacated on grounds other than TEX. CIV. PRAC. & REM. CODE § 171.098(a)(4), then the court may order a rehearing before new arbitrators chosen (1) as provided in the arbitration agreement; or (2) by the court, if the agreement does not provide the manner of choosing the arbitrators.[310] If an arbitration award is vacated under Section 171.088(a)(3), then the court may order a rehearing before the arbitrators who made the original award.[311]

The El Paso Court of Appeals, in *Tri-Star Petroleum Co. v. Tipperary Corp*., concluded that that the use of the phrase "may" rather than "shall" (as used in some sections of the TAA) suggested that the ordering of a rehearing was permissive, rather than mandatory.[312] *Tri-Star* involved an effort to set aside the determination of an accounting firm, which the parties had agreed would be binding. After the accounting procedure was concluded, however, Tipperary alleged that Tri-Star had breached the arbitration agreement itself in several respects, thus undermining the arbitration process. The court agreed, concluding that this material breach was a valid ground for revoking the arbitration agreement, as well as for setting aside the award. The court declined to follow the holding in *Koch v. Koch*, prohibiting a trial court from setting a case for trial after vacating an award.[313]

b. Federal Court.

The FAA provides that "if an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators."[314] "Absent corruption, fraud, or other misconduct on the part of the arbitrator, or implicating the tribunal administrator or the rules under which it operated, the court vacating an arbitration award should order rehearing before the same panel, though that decision remains within the court's discretion."[315] However, a district court does not have the authority to dictate procedures for a second arbitration.[316]

When a court vacates an award, but the time by which the arbitration agreement required the award to be made has expired, "then the award simply becomes null and void as if the merits were never arbitrated and the dispute can be litigated."[317]

4. Appellate Court Review of Vacatur Orders.

The TAA authorizes an appeal of a trial court order vacating an arbitration award, so long as the trial court does not grant a rehearing before the arbitral panel or order a new arbitration.[318] Based on this statute, Texas courts of appeals have concluded that they lack jurisdiction to review an order that vacates an arbitration award while granting a new arbitration hearing, which has been analogized to a grant of a motion for new trial.[319] This limitation on appellate jurisdiction generally has been applied not only to cases arising under the TAA, but also to FAA cases brought in state court, because such cases are subject to state procedural rules.[320]

The Texarkana Court of Appeals, in *Werline v. East Texas Salt Water Disposal Co*., may have opened up a small crack in this barrier to appellate court jurisdiction.[321] Even though the trial court in *Werline* granted vacatur and directed a rehearing before the arbitration panel, the Texarkana court seized on the fact that the trial court also had denied the successful arbitrating party's motion to confirm the arbitration award. The court reasoned that it had jurisdiction because "a trial court's order granting a motion to vacate and directing a rehearing does not extinguish a party's right to appeal the denial of its motion to confirm."[322]

The Texarkana court's approach directly conflicts with a holding of the Fourteenth Court of Appeals,

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[310] TEX. CIV. PRAC. & REM. CODE § 171.089(a).

[311] *Id.* § 171.089(b).

[312] 107 S.W.3d 607 (Tex. App.—El Paso 2003, pet. denied).

[313] 27 S.W.3d 93, 97 (Tex. App.—San Antonio 2000, no pet.).

[314] 9 U.S.C. § 10(b).

[315] Thomas H. Oehmke, *Appealing Adverse Arbitration Awards*, 94 AM. JUR. TRIALS 211, at § 246 (2006).

[316] *Positive Software Solutions, Inc. v. New Century Mortgage Corp*., 436 F.3d 495, 505 (5th Cir. 2006), *reversed on other grounds*, 476 F.3d 278 (5th Cir. 2007) (en banc), *cert. denied*, --S. Ct.--, 2007 WL 1090443 (June 11, 2007).

[317] Oehmke, *supra* note 315, at § 245.

[318] TEX. CIV. PRAC. & REM. CODE § 171.098(a)(5).

[319] *Stolhandske v. Stern*, 14 S.W.3d 810 (Tex. App.—Houston [1st Dist.] 2000), pet. denied).

[320] *See J.D. Edwards World Solutions Co. v. Estes, Inc.*, 91 S.W.3d 836, 839 (Tex. App.—Fort Worth 2002, pet. denied).

[321] 209 S.W.3d 888, 896 (Tex. App.—Texarkana 2006, pet. filed).

[322] *Id*.

which held that an order vacating an award and directing rehearing is not appealable, even if the order also denied confirmation.[323] Similarly, the First Court of Appeals, in *Bison Building Materials, Ltd. v. Aldridge* held that an order confirming in part and vacating in part was not an appealable interlocutory order, because the trial court's order contemplated a rehearing before the arbitrator.[324] The losing parties in both *Werline* and *Aldridge* have filed petitions for review in the Texas Supreme Court.

Note that FAA cases brought in federal court are not subject to this jurisdictional limitation, as the FAA permits an appeal from an order "modifying, correcting, or vacating an award."[325]

F. The Wave of the Future? Non-Judicial Appellate Tribunals.

Given the expense and time-consuming nature of post-award litigation, both courts and commentators have suggested that parties contract for a private appellate arbitration panel to review the arbitrator's award as a substitute for judicial review.[326] One commentator convincingly sets out the advantages of such an approach in terms of efficiency, flexibility and confidentiality. For example, parties that adopt this approach can exercise more control over the manner and standards by which such an "appeal" would be handled, in essence tailoring the traditional appellate rules to their liking. They could also set a schedule for more expedited review than would be available in the courts.[327]

The Judicial Arbitration and Mediation Services (JAMS) has adopted an optional appeal procedure that is available if both parties agree to the procedure. It is essentially an administrative appeal process whereby an appeal panel will review the arbitration record, may conduct an oral argument, and may reopen the record if appropriate. The panel will apply the same standard of review as a first-level appellate court, and may affirm, reverse or modify an award, which will then be binding upon the parties.

V. CONCLUSION

In today's climate, the inclusion of an arbitration clause in a contract is hardly a guarantee that litigation can be avoided. On the contrary, as this article explains, there has been extensive litigation in recent years over the enforceability and scope of arbitration clauses and the validity of an arbitral award, once rendered. It is the authors' hope that this article will help provide a useful overview of such arbitration-related litigation and practical guidance for navigating through it.

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[323] *Prudential Sec., Inc. v. Vondergoltz*, 14 S.W.3d 329, 330-31 (Tex. App.—Houston [14th Dist.] 2000, no pet.).

[324] 2006 WL 2641280, at *4-5 (Tex. App.—Houston [1st Dist.] 2006, pet. filed).

[325] 9 U.S.C. § 16; *see also Atlantic Aviation, Inc. v. EBM Group, Inc.*, 11 F.3d 1276, 1280 (5th Cir. 1994).

[326] *See, e.g., Chicago Typographical Union No. 16 v. Chicago Sun-Times, Inc.*, 935 F.2d 1501 (7th Cir. 1991); Mark Trachtenberg & Christina Crozier, "*Risky Business: Altering the Scope of Judicial Review of Arbitration Awards by Contract*," TEX. BAR J., Vol. 69, No. 9 (October 2006); Christopher D. Kratovil, *Judicial Review of Arbitration Awards*, at 13-14, University of Texas, 16th Annual Conference on State and Federal Appeals (June 1-2, 2006); Christian A. Garza and Christopher D. Kratovil, *Contracting for Private Appellate Review of Arbitration Awards*, THE APPELLATE ADVOCATE, 20 (Winter 2007).

[327] Kratovil, *supra* note 326, at 14.