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Summary of Gonski v. Dist. Ct., 126 Nev. Adv. Op. No. 51

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CONTRACTS

I. SUMMARY

The Second Judicial District Court entered an order compelling arbitration in a construction defect dispute. Petitioners asked for a writ of mandamus vacating the order compelling arbitration.

II. DISPOSITION/OUTCOME

The Nevada Supreme Court granted the writ of mandamus because the arbitration provisions of the contract were unconscionable.

III. FACTUAL AND PROCEDURAL HISTORY

Donald and Linda Gonski signed a purchase agreement for a single residence from Pulte Homes in April of 2004. At the time of the signing, Pulte presented the Gonskis with a stack of forms amounting to 469 pages and told the Gonskis that others were willing to step in and buy the home if they did not sign all the documents at that time. The Gonskis signed.

Months after, the Gonskis served Pulte Homes with a NRS Chapter 40 notice of construction defects, and the parties mediated the matter. Mediation did not prove fruitful, so the Gonskis brought suit in district court. Pulte Homes moved to compel arbitration based on the arbitration clause of the purchase agreement. The Gonskis opposed, stating there was an additional arbitration clause under the separate limited warranty that applied to construction defects, and claiming that the arbitration clauses under both the purchase agreement and the limited warranty were unconscionable and unenforceable.

The purchase agreement arbitration clause stated the following:

ARBITRATION: Any controversy, claim or dispute arising out of or relating to this Agreement or Your purchase of the Home (other than claims under the Limited Warranty) shall be settled by arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association (AAA) and the Federal Arbitration Act (Title 9 of the United States Code) and judgment rendered by the arbitrator(s) may be confirmed, entered and enforced in any court having jurisdiction. As a condition precedent to arbitration, the dispute shall first be mediated in accordance with the Construction Industry Mediation Rules of the AAA, or such other mediation service selected by Us. Claims under the Limited Warranty will be arbitrated in

¹ By Ryan Johnson

accordance with the arbitration provision set forth in the Limited Warranty.

In the event the claim relates to a construction defect, the construction dispute provisions (including good-faith mediation) of Chapter 40 of Nevada Revised Statutes shall also apply if and to the extent that the alleged defect is covered by the Limited Warranty.

The additional arbitration clause contained within the limited warranty stated the following:

DISPUTE SETTLEMENT

This Dispute Settlement provision sets forth the exclusive remedy of all disputes or controversies under this LIMITED WARRANTY.

....

If the Plan Administrator is unable to successfully mediate the dispute, the Plan Administrator will inform THE HOMEOWNER and THE BUILDER that the dispute is unresolved and that Binding Arbitration is provided as a remedy for resolving the dispute.

....

Any binding arbitration proceeding will be conducted pursuant to the United States Arbitration Act (9 U.S.C. § 1 et seq.) (“the Act”) by an independent, nationally recognized, arbitration organization designated by the Plan Administrator. The rules and procedures followed will be those under the Act, which may be supplemented by the arbitration organization’s rules. A copy of the applicable rules and procedures will be delivered to you upon your request to the Plan Administrator.

The arbitration will determine THE HOMEOWNER’S, THE BUILDER’S and (if applicable) the Insurer’s rights and obligations under this LIMITED WARRANTY. These rights and obligations include, but are not limited to, those provided to THE HOMEOWNER or THE BUILDER by local, state or federal statutes in connection with this LIMITED WARRANTY. The award of the arbitrator(s) will be final, binding and enforceable as to THE HOMEOWNER, THE BUILDER and (if applicable) the Insurer, except as modified or vacated in

accordance with the Act or the arbitration organization's rules. A judgment rendered by the arbitrator(s) may be confirmed, entered and enforced in any court having jurisdiction.

The Gonskis argued that both provisions were unconscionable and, therefore, unenforceable. In addition, they asserted that they did not have enough time to review the documents in full and that the documents were not adequately explained to them. The district court ruled that the arbitration clauses were not unconscionable and ordered the parties to participate in arbitration. The Gonskis then filed a petition for a writ of mandamus to the Nevada Supreme Court. The Supreme Court case was heard by a panel of three justices; Justice Douglas wrote the opinion with Justice Hardesty concurring. Justice Pickering concurred in part and dissented in part.

IV. DISCUSSION

The Gonskis argued that the arbitration clauses in both agreements were unconscionable and made the clauses unenforceable. The Court will not uphold an arbitration agreement if it finds the agreement both procedurally and substantively unconscionable.² Both types of unconscionability are required to make an agreement unenforceable, but Justice Douglas referred to a California case that reasons “the stronger the showing of substantive unconscionability, the less necessary is a strong showing of procedural unconscionability,” and vice versa.³

Procedural Unconscionability

Procedural unconscionability arises when a party has no “meaningful opportunity to agree to the clause terms either because of unequal bargaining power, as in an adhesion contract, or because the clause and its effects are not readily ascertainable upon a review of the contract.”⁴

The Nevada Supreme Court previously stated that “to be enforceable, an arbitration clause must at least be conspicuous and clearly put a purchaser on notice that he or she is waiving important rights under Nevada law.”⁵ Regarding the Pulte arbitration agreement, the Court said that it “in no way draws the reader’s attention.” The agreement was towards the end of an eighteen-page document and had no kind of formatting differences from the paragraphs around it, even though some other paragraphs in the document were given more attention through using all capital letters and bolding.

² D.R. Horton, Inc. v. Green, 120 Nev. 549, 553, 96 P.3d 1159, 1162 (2004).

³ See, e.g., Armendariz v. Foundation Health Pyschcare, 6 P.3d 669, 690 (Cal. 2000).

⁴ D.R. Horton Inc., 120 Nev. at 554, 96 P.3d at 1162.

⁵ *Id.* at 557, 96 P.3d at 1164.

In addition, the arbitration agreement under the limited warranty was given to the Gonskis with a large stack of other documents and was slightly different from the agreement under the purchase contract. Consequently, the Court said the second agreement caused the Gonskis to forfeit specific rights without knowing it. The Court stated that although the violations were not great, procedural unconscionability was present.

Substantive Unconscionability

Substantive unconscionability is based on the one-sidedness of the arbitration terms and consists of terms that are oppressive.⁶ In the present case the Court found two occurrences of substantive unconscionability: one with the disclaiming of arbitration expenses and the other with the disregard of NRS Chapter 40 rights.

Arbitration Expenses

The Court held that the conflict between the arbitration clauses in the purchase agreement and the limited warranty agreement, taken together with the one-sidedness of the clause in the limited warranty agreement constituted substantive unconscionability. In the purchase agreement, the clause stated that Pulte Homes would advance the fees necessary for the arbitration. The Court said that this seemed to apply to any arbitration case between the parties. However, in the limited warranty agreement, the clause stated that the purchaser must pay the fees up front. This burden, along with the conflicting language in the clauses, constituted substantive unconscionability.

NRS Chapter 40 Rights

NRS Chapter 40 was enacted to protect the rights of homebuyers, and, in contrast to common law, allowed homeowners to bring negligence claims against contractors for construction defects. The Court here held that **contractor's may not "limit a homeowner's recovery to defects covered by contract or warranty."** Doing so would defeat the public policy of the state that created by Chapter 40.

In the current instance, Pulte Homes tried to limit its liability by using the limited warranty agreement. Thus, the provision tried to limit Chapter 40 rights and was, therefore, substantively unconscionable. The court said that the denial of these rights constituted "significant substantive unconscionability."

V. OPINION CONCURRING IN PART AND DISSENTING IN PART

In her opinion, Justice Pickering concurred that the writ of mandamus should be issued overturning the district court's order; however, Justice Pickering expressed her feelings that

⁶ *Id.* at 554, 96 P.3d at 1162-1163.

under the recent U.S. Supreme Court case *Rent-A-Center, West, Inc. v. Jackson*⁷ case, the Gonskis' case should have been remanded to the district court for further arguments regarding whether the agreements contained an enforceable delegation clause. If so, Justice Pickering reasoned that an arbitrator should be the one who determines if the arbitrator or the district court should hear the case.

VI. CONCLUSION

Despite the slight procedural unconscionability, the contracts' strong substantive unconscionability due to the disregard of NRS Chapter 40 rights created sufficient reason to invalidate the arbitration clauses altogether.

⁷ *Rent-A-Center, West, Inc. v. Jackson*, 561 U.S. ____, 130 S.Ct. 2772 (2010) (holding that unless the party "challenged the delegation provision specifically, we must treat it as valid").