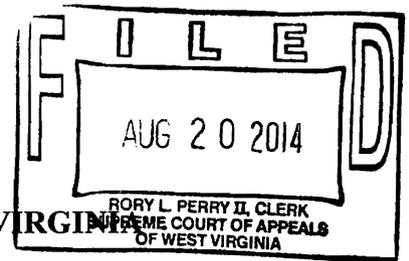


NO. 14-0441



IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

SCHUMACHER HOMES OF
CIRCLEVILLE, INC., a foreign corporation,

Defendant Below,
Petitioner,

v.

JOHN SPENCER and
CAROLYN SPENCER,

Plaintiffs Below,
Respondents.

**FROM THE CIRCUIT COURT OF
MASON COUNTY, WEST VIRGINIA**

**RESPONSE TO PETITION
FOR APPEAL**

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I. KIND OF PROCEEDING AND RULING IN THE LOWER COURT

Petitioner, Schumacher Homes of Circleville, Inc. (“Schumacher”), sought, by motion, to have the Circuit Court of Mason County dismiss the Complaint filed by John and Carolyn Spencer and compel arbitration or in the alternative stay the proceeding pending arbitration. The Circuit Court of Mason County refused to enforce the procedurally and substantively unconscionable arbitration provisions and on March 6, 2014 entered an Order with findings of fact and conclusions of law, denying Schumacher’s motion. Schumacher now appeals.

II. STATEMENT OF FACTS

June 6, 2011 was an exciting time for local Mason County residents John and Carolyn Spencer as they were beginning the process of what they thought would lead to a wonderful new home in which they would spend their retirement years with their grandchildren. Pursuant to the construction contract (“Contract”) (A.R. 40-48; 303-311) drafted by Schumacher, John and Carolyn agreed to pay a purchase price of \$193,855.00 for a new home. The purchase price was to be paid in installments as various stages of construction were completed as set forth in the Contract. *See Contract*. Mr. and Mrs. Spencer paid the installment amounts pursuant to Schumacher’s provision in the contract which states “[h]omeowners do not have the right to defer or delay payment of the above draws or any other sums owed under the Contract Documents.” *Id.*

Unfortunately, as a direct result of Schumacher and others’¹ work, John and Carolyn Spencer ended up with a house with numerous and substantial problems. At the conclusion of construction, John and Carolyn Spencer noticed defects with the home and the work performed.

¹ Davis Heating & Cooling Company, Inc. and GZG Construction, LLC were named in the Complaint. GZG Construction, LLC was voluntarily dismissed after speaking with Zach Garrison of GZG Construction, LLC and it was learned that Schumacher used his name and West Virginia contractor’s license on the project when neither he nor his company worked on that project. Thus, additional fraud allegations have acquired against Schumacher.

As this Honorable Court can see from the report and pictures from Sam Wood of Advantage Home & Environment Inspections, Inc., the problems and defects are glaring. *See Advantage Home & Environment Inspections, Inc. Report.* (A.R. 283-292) These problems are also listed and detailed in the Complaint under Section VI. Some of which include, but are not limited to the following:

1. The subject house, rather than being placed approximately 22 feet from the street, was constructed by Schumacher more than 40 feet from the street in an area that was extremely sloped and elevated. The excavation for the foundation was not deep enough and the finished home has a front porch approximately five feet off of the ground with the back door approximately ten feet off of the ground and no safe manner in which to have ingress and egress through the back door.
2. Schumacher failed to build any stairs or steps to either the front door or the back door.
3. There is no railing along the front porch even though the porch is five feet off of the ground.
4. The floor structure was not framed properly with a non-bearing interior wall improperly constructed over a double joist system and with some of the joists being damaged.
5. Support posts holding the main beam are not properly secured. Cold cracks have formed and there is a hole in the roof.
6. There is insufficient clearance between the roof and the chimney's "B Vent," creating a fire hazard and there is insufficient clearance between the exhaust flue and combustible materials in the roof again creating a fire hazard.
7. There are significant cracking along the basement floor and basement walls which are also creating risks of water and radon intrusion.

8. Gas pipes are not properly protected from rust and corrosion and have already begun to rust, the water line does not meet industry standards, there is no drain installed in the basement despite being included in the drawings, the hot water heater is without a drip leg in violation of industry standards, and the ground fault circuit interrupter and the sump pump are not properly installed and connected.

In an effort to resolve the complaints and correct the notable defects, Schumacher was contacted. *See Letter to Schumacher*. (A.R. 312-314) Schumacher took no steps whatsoever to correct any of the defects and issues with the house after it was notified of them. After it became clear Schumacher was not going to address any of the problems with the house, John and Carolyn Spencer filed their Complaint on June 28, 2013. After forcing John and Carolyn Spencer to file a lawsuit to obtain relief, Schumacher, in an attempt to circumvent the jurisdiction of the West Virginia lower court, filed a motion to dismiss attempting to have the lower court enforce its procedurally and substantively unconscionable arbitration provisions in the Contract it drafted. Schumacher continues that quest now with its appeal to this Court. As detailed below, the arbitration provisions are complete with underlying doubletalk that provides a calculated “out” for Schumacher to avoid arbitration altogether, yet stacks the deck against John and Carolyn Spencer.

III. STANDARD OF REVIEW

Schumacher claims seven errors that the trial court committed in denying the motion to dismiss and compel arbitration. The standard of review for the claimed errors is *de novo*. *Brown v. Genesis Healthcare Corp.* 228 W.Va. 646, n.12, 724 S.E.2d 250, 267, n.12 (2011), *vacated sub nom. Marmet Health Care Ctr., Inc. v. Brown*, 565 U.S. ___, 132 S.Ct. 1201 (2012) (*Brown I*) (*quoting State ex rel. Saylor v. Wilkes*, 216 W.Va. 766, 772, 613 S.E.2d 914, 920 (2005)); *Syl. Pt.*

1, Fountain Place Cinema 8, LLC v. Morris, 227 W.Va. 249, 707 S.E.2d 859 (2011); *Syl. Pt. 1, in part, State ex rel. Cooper v. Caperton*, 196 W.Va. 208, 210, 470 S.E.2d 162, 164 (1996).

III. TABLE OF AUTHORITIES

Statutes

- 1) Magnuson-Moss Warranty Act, 15 U.S. Code § 2308
- 2) West Virginia Code § 46A, West Virginia Consumer Credit and Protection Act
- 3) West Virginia Code §46-1-203, Uniform Commercial Code
- 4) Federal Arbitration Act, 9 U.S.C. §§ 1, 2 et seq.

Cases

- 1) *Brown v. Genesis Healthcare Corp.* 228 W.Va. 646, n.12, 724 S.E.2d 250, 267, n.12 (2011), *vacated sub nom. Marmet Health Care Ctr., Inc. v. Brown*, 565 U.S. ___, 132 S.Ct. 1201 (2012)
- 2) *Fountain Place Cinema 8, LLC v. Morris*, 227 W.Va. 249, 707 S.E.2d 859 (2011)
- 3) *State ex rel. Cooper v. Caperton*, 196 W.Va. 208, 470 S.E.2d 162 (1996).
- 4) *Adkins v. Labor Ready, Inc.*, 303 F. 3d 496, 500-01 (4th Cir. 2002)
- 5) *Troy Mining Corp. v. Itman Coal Co.*, 176 W.Va. 599, 346 S.E. 2d 749 (W. Va. 1986)
- 6) *Grayiel v. Appalachian Energy Partners*, 230 W.Va. 91, 736 S.E.2d 91 (2012)
- 7) *Nelson v. McGoldrick*, 127 Wash.2d 124, 896 P.2d 1258 (1995)
- 8) *Credit Acceptance Corp. v Front*, 231 W.Va. 518, 2013 WL 3155993 (2013)
- 9) *Hooters of America, Inc. v Phillips*, 173 F.3d 933 (4th Cir. 1991).
- 10) *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 116 S. Ct. 1652 (1986)

IV. ARGUMENT

Although Schumacher sets forth seven separate alleged assignments of error, essentially this appeal turns on the issue of whether or not the provision in the Contract drafted by Schumacher requiring John and Carolyn Spencer to arbitrate their claims while reserving to Schumacher the

right to file suit is enforceable or whether the arbitration provision is unenforceable as being unconscionable. Although Schumacher has argued that reserving unto it the right to file suit to enforce a mechanic's lien is "only one carve-out," it is a "carve-out" of the only true claim which Schumacher could ever seek to enforce.

Contrary to the arguments made by Schumacher in its Brief, the Circuit Court of Mason County properly determined the threshold issue of whether a valid and enforceable arbitration agreement existed between John and Carolyn Spencer and Schumacher.

"When a trial court is required to rule upon a motion to compel arbitration pursuant to the Federal Arbitration Act, 9 U.S.C. §§ 1-307 (2006), the authority of the trial court is limited to determining the threshold issues of (1) whether a valid arbitration agreement exists between the parties; and (2) whether the claims averred by the plaintiff fall within the substantive scope of that arbitration agreement."

Syllabus Point 5, *Grayiel v Appalachian Energy Partners*, 230 W.Va. 91, 736 S.E.2d 91 (2012). The trial court has the authority and duty to determine if a valid arbitration agreement exists and, if so, if the claims at issue are within the scope of the arbitration agreement.

The Circuit Court of Mason County properly invalidated the entire unconscionable arbitration provision drafted by Schumacher. While generally under the Federal Arbitration Act, 9 U.S.C. §1, et seq ("FAA"), parties who sign contracts with arbitration agreements are bound, the "savings clause" in the federal statute specifically defers rulings on issues that pertain to general contract principles to the states. Issues such as fraud, duress, and unconscionability are to be decided by state courts.

Schumacher selectively ignores FAA 9 U.S.C. §2, which allows for general principles of contract law to be enforced. The pertinent language of this code section, as quoted by this Court, states,

[a] written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, *save upon such grounds as exist at law or in equity for the revocation of any contract.*

Brown v. Genesis Healthcare Corp., 228 W. Va. 670, S.E.2d at 274 (W. Va. 2011) (citing 9 U.S.C. §2). *Emphasis added.* The United States Supreme Court, in dealing with this section of the FAA noted,

[u]nder the savings clause, ‘generally applicable contract defenses, such as fraud, duress, or *unconscionability*, *may be applied to invalidate arbitration agreements without contravening §2[.]*’

Doctor’s Associates, Inc. v. Casarotto, 517 U.S. 681 (1986). *Emphasis added.*

The Circuit Court of Mason County utilized this Court’s clear guidelines for what will constitute unconscionable provisions when it ruled that all of the arbitration provisions were unconscionable. *Brown v. Genesis* holds

[t]he doctrine of unconscionability means that, because of an overall and gross imbalance, one-sidedness, or lop-sidedness in a contract, a court may be justified in refusing to enforce the contract as written.

Brown v. Genesis Healthcare Corp., 228 W. Va. at 680, 724 S.E.2d at 284 (W. Va. 2011) (citing *McGinnis v. Cayton*, 173 W. Va. 102, 113, 312, S.E.2d 765, 776 (W. Va. 1984)). Additionally,

[t]he concept of unconscionability must be applied in a flexible manner, taking into consideration all of the facts and circumstances of a particular case. . . [a]n analysis of whether a contract term is unconscionable necessarily involves an inquiry into the circumstances surrounding the execution of the contract and the fairness of the contract as a whole.

Brown v. Genesis Healthcare Corp., 228 W. Va. 680, S.E.2d at 284 (W. Va. 2011) (citing *Troy Mining Corp. v. Itman Coal Co.*, 176 W. Va. 599, 346 S.E. 2d 749 (W. Va. 1986)). *Brown's* standard for unconscionability that includes two component parts: procedural unconscionability and substantive unconscionability acknowledges there does not need to be an equal finding of procedural and substantive unconscionability, rather, the two component parts are viewed on a sliding scale where far more of one component may be found and still constitute unconscionability. *Id.* (citing *McGinnis*, 173 W. Va. at 114, 312 S.E.2d at 777 (W. Va. 1986)).

The lower court correctly held that Schumacher's arbitration provisions are procedurally unconscionable. Procedural unconscionability, is described as:

[I]nequities, improprieties, or unfairness in the bargaining process and the formation of the contract. Procedural unconscionability has been described as the lack of a meaningful choice, considering all the circumstances surrounding the transaction including '[t]he manner in which the contract was entered,' whether each party had 'a reasonable opportunity to understand the terms of the contract,' and whether 'the important terms [were] hidden in a maze of fine print[.]'" Procedural unconscionability involves a "variety of inadequacies, such as . . . literacy, lack of sophistication, hidden or unduly complex contract terms, bargaining tactics, and the particular setting existing during the contract formation process. Determining procedural unconscionability also "requires the court to focus on the 'real and voluntary meeting of the minds' of the parties. . ." *Id.* (citing *McGinnis*, 173 W. Va. At 114, 312 S.E.2d at 777 (W. Va. 1986), *Nelson v. McGoldrick*, 127 Wash.2d 124, 896 P.2d 1258 (Wash. 1995)).

Circumstances with a tendency to indicate uneven bargaining power are those that give credence to an argument that an arbitration clause is unconscionable. *Id.* at 684, 288.

The lower court found that Schumacher has a significantly higher level of sophistication when it comes to forming and negotiating contracts. John and Carolyn Spencer were looking for a home that catered to specific needs. Their limited alternatives to meet these needs with regard to

choosing a home builder made the bargaining process that much more lopsided. As illustrated below, the terms of the arbitration clause are muddled in a manner that gives Schumacher an upper hand when negotiating its unconscionable provisions.

Any number of problems can arise for the purchaser of a home whereas the seller remains fairly secure in knowing it will only need judicial intervention if payment is not made. Knowing this, Schumacher places a maze of language with an arbitration clause in the Contract. John and Carolyn have no experience in dealing with complex, complicated contracts and did not have the ability to fully understand the rights given up by arbitration. Even if John and Carolyn had understood these rights, they did not have the ability to negotiate terms with Schumacher that protected their interests on critical issues. The severely unequal footing between the parties made a fair bargaining exchange impossible and there could be no “real and voluntary meeting of the minds.” *Brown v. Genesis Healthcare Corp.*, 228 W. Va. 680, 724 S.E.2d at 284 (citing *McGinnis*, 173 W. Va. At 114, 312 S.E.2d at 777 (W. Va. 1986), *Nelson v. McGoldrick*, 127 Wash.2d 124, 896 P.2d 1258 (Wash. 1995)).

In addition to being procedurally unconscionable, Schumacher’s arbitration clause is substantively unconscionable. Substantive unconscionability involves unfairness in the contract itself, unreasonably favorable terms to the more powerful party in the bargaining process. *Id.* at 228 W.Va. at 683, 724 S.E.2d at 287. This Court has examined several important case regarding substantive unconscionability. In those instances, the more powerful party either: (1) reserves the right to judicial action while requiring that the other party arbitrate any matter that may arise or (2) is not likely to need judicial oversight because they will only have one claim (usually the collection of money by a business from a customer). *Brown v. Genesis Healthcare Corp.*, 228 W.

Va. at 661, 724 S.E.2d at 265 (W. Va. 2011); *Grayiel v. Appalachian Energy Partners*, 230 W.Va. 91, 736 S.E.2d 91 (W.Va. 2012).

In the subject Contract Schumacher actually reserved the right to avoid arbitration for matters involving a mechanic's lien. The pertinent language of the arbitration provision is first mentioned in section 27 of the Contract. The language, created by Schumacher for Schumacher, provides various guidelines for arbitration which are noticeably in its favor to a trained eye. Even with this favor imbalance, Schumacher made sure to include in the end of section 27, "[t]he arbitration paragraph shall not be interpreted as waiver of Schumacher's mechanic's lien rights." Reserving the right to file a mechanic's lien is further noted in section 32 and 35.

In essence, Schumacher reserves its ability to go through the process of collecting unpaid debt. Schumacher would not take another route to resolve any indebtedness by John and Carolyn, so this contravention of the arbitration provision is, to the trained eye, a glaring "out" for Schumacher. Schumacher will not be required to submit claims arising from non-payment to arbitration. As the Court can see this raises a serious question of fairness as what other claims will Schumacher need to send to arbitration? Schumacher would not need judicial intervention for anything other than the collection of money. With mechanic's liens being the most effective action to take on this matter, Schumacher knows in advance it will not need arbitration.

On the other hand, John and Carolyn Spencer can and do have numerous claims against Schumacher. There is an inherent unfairness when one party (usually a business) is significantly less likely to need the use of arbitration. *Grayiel v. Appalachian Energy Partners* 230 W. Va. 91, 736 S.E.2d 91 (2012).

Mr. and Mrs. Spencer have asserted claims against Schumacher for civil conspiracy, actual fraud, constructive fraud, innocent misrepresentation, negligent misrepresentation, breach of

express warranty, breach of implied warranty, negligence, breach of the West Virginia Consumer Credit and Protection Act, and breach of the Uniform Commercial Code.²

In *Kirby v Lion Enterprises, Inc.*, 233 W.Va. 159, 756 S.E.2d 493 (2014), this Court, in remanding a case, noted that “the trial court may consider the context of the arbitration clause within the four corners of the contract, or consider any extrinsic evidence detailing the formation and use of the contract,” at 756 S.E.2d 500, citing *State ex rel. Richmond American Homes of West Virginia, Inc. v Sanders*, 228 W.Va. 125, 717 S.E.2d 909. In his concurring opinion, Justice Ketchum noted that the subject contract in *Kirby* lacked any modicum bilaterally or mutuality of obligation, at 756 S.E.2d 502. Justice Ketchum further noted that the contract in *Kirby* required that any arbitration be held in Uniontown, Pennsylvania even though the house in dispute had been constructed in Fairmont, West Virginia and that the trial court could weigh if the arbitration provision imposed unreasonably burdensome costs upon the homeowner.

In this case, apparently in recognition of the unconscionability of the subject contract mandating that arbitration be held exclusively in Stark County, Ohio, Schumacher has expressly agreed to arbitrate the claims of Mr. and Mrs. Spencer in Mason County, West Virginia where they reside and where the subject home is located (Petitioner’s Brief, page 3). This stipulation by Schumacher does not make the unconscionable provision in the Contract requiring arbitration to be in Stark County, Ohio somehow now “conscionable.” The enforcement of arbitration would further impose unreasonably burdensome costs upon and would have a substantial deterrent effect upon John and Carolyn Spencer seeking to enforce and vindicate their rights and protections and

² Counsel for the Respondent must confess to a typographical error. The reference in the Complaint to West Virginia Code § 4-6-1-203 was intended to, was intended to be, and should have been, a reference to West Virginia Code § 46-1-201(b)(20), which general defines “Good faith” as meaning “honesty in fact and the observance of reasonable commercial standards of fair dealing.”

to obtain statutory and common-law relief and remedies afforded unto them under West Virginia law that exists for the benefit and protection of the public.

V. CONCLUSION

Based on the foregoing, it is evident that the Circuit Court of Mason County committed no reversible error in denying Schumacher's motion to dismiss and compel arbitration.

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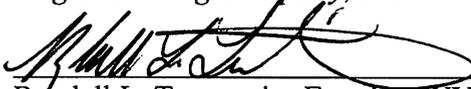
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CERTIFICATE OF SERVICE

The undersigned counsel does hereby certify that service of the foregoing RESPONSE TO PETITION FOR APPEAL has been made this the 19th day of August, 2014 by serving the same, postage prepaid, in the United States mail, to the following counsel of record.

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