EXCEPTION TO THE RULE

The Enforceability of Construction ADR Clauses

By Andrew L. Smith

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In Ohio, alternative dispute resolution (ADR) is encouraged as a method to settle disputes. Contrary to litigation, ADR allows parties the ability to plan early for possible disputes and the flexibility to customize the most time- and cost-effective resolution process for their cases through contractual provisions.

A presumption favoring ADR arises when the claim in dispute falls within the scope of the contract provision. For instance, an arbitration clause in a contract is generally viewed as an expression that the parties agree to arbitrate disagreements within the scope of the arbitration clause, and, with limited exceptions, an arbitration clause will be upheld just as any other provision in a contract should be respected.

However, there are exceptions to the enforceability of ADR clauses.

Unconscionability Exception

An ADR clause can be found unconscionable when the clause is "so one-sided as to oppress or unfairly surprise a party," as outlined in *Neubrander v. Dean Witter Reynolds, Inc.*, 81 Ohio App.3d 308, 311-312, 610 N.E.2d 1089 (1992). Unconscionability includes "an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." (*Lake Ridge Academy v. Carney*, 66 Ohio St.3d 376, 383, 613 N.E.2d 183 [1993]). The party seeking to establish an ADR clause is unconscionable must show the provision is both procedurally and substantively unconscionable. Assessing these factors is a very fact-intensive, case-by-case analysis.

- **Procedural unconscionability:** This concerns the formation of the agreement and occurs when no voluntary meeting of the minds is possible. To determine whether a contract provision is procedurally unconscionable, courts consider the following factors: the relative bargaining positions of the parties; whether the terms of the provision were explained to the weaker party; whether the party claiming that the provision is unconscionable was represented by counsel at the time the contract was executed; and the parties' age, education, intelligence, business acumen, and experience. (*Taylor Bldg. Corp. of Am. v. Benfield*, 117 Ohio St. 3d 352, 2008-Ohio-938, 884 N.E.2d 12).
- **Substantive unconscionability:** This refers to the actual terms of the agreement. Contract terms are substantively unconscionable if they are unfair and commercially unreasonable. Because the determination of commercial reasonableness varies with the content of the contract terms at issue in any given case, no generally accepted list of factors has been developed for this category of unconscionability. However, courts examining whether a particular clause is substantively unconscionable have considered the following factors: the fairness of the terms, the charge for the service rendered, the standard in the industry, and the ability to accurately predict the extent of future liability.

Demonstrating unconscionability is very difficult. By way of example, the Ohio Supreme Court, in *Taylor Bldg. Corp. of Am. v. Benfield*, 117 Ohio St. 3d 352, 2008-Ohio-938, 884 N.E.2d 12, held the following contractual clauses were not procedurally unconscionable when applied against average citizens purchasing a home from a building company:

> 15. Arbitration—In the event the issues cannot be resolved by mediation, then any claims or disputes arising out of this Construction Agreement or the alleged breach thereunder shall be settled by mandatory and binding arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association unless both parties mutually agree otherwise. Notices of the demand for arbitration shall be filed with a copy of this Construction Agreement with the American Arbitration Association and the other party to this Agreement. The site for the arbitration proceedings shall be Louisville, Kentucky (Jefferson County).
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> 16. That in the event any of the provisions of this Agreement as to mediation, arbitration or buy back, are deemed unenforceable, or in the event of an action initiated by Builder pursuant to Paragraph 6 and 9 of this Agreement, both parties agree that any and all legal actions arising out of this Construction Agreement or the alleged breach thereunder shall be tried by a judge sitting without a jury and both parties do hereby Knowingly, Voluntarily and Intentionally waive any right to a jury trial. The site for the aforementioned action shall be Louisville, Kentucky (Jefferson County).

The Ohio Supreme Court reached its conclusion, due to the following:

- The homeowners did not have to buy a home from the builder because there was a multitude of homebuilders in the local area.
- The arbitration clause appeared in standard, rather than fine, print and was not hidden. The homeowners initialed the arbitration clause and signed the contract as a whole.
- The homeowners alleged the builder's salesperson told them that invoking the arbitration clause would not be necessary because the builder "never had any disputes over the quality of its product and workmanship," and the builder was "concerned about keeping its customers happy." This did not amount to fraud or misrepresentation.
- This was not a contract of adhesion, even assuming the parties' bargaining power was unequal.

Adhesion Contract Exception

As another method to escape the mandates of an ADR clause, a party may prove the provision amounts to an adhesion contract. Where "there are strong indications that the contract at issue is an adhesion contract, and the arbitration clause itself appears to be adhesive in nature," there is "considerable doubt that any true agreement ever existed to submit disputes to arbitration," according to *Williams v. Aetna Finance Co.*, 83 Ohio St.3d 464, 473, 1998-Ohio-294, 700 N.E.2d 859.

Black's Law Dictionary (8th Ed. 2004) defines an adhesion contract as a "standard-form contract prepared by one party, to be signed by the party in a weaker position, usu[ally] a consumer, who adheres to the contract with little choice about the terms." As with unconscionability, proving a clause amounts to an adhesion contract is very difficult. In addition, inequality of bargaining power alone is insufficient to invalidate an otherwise enforceable contract clause, as outlined in *Vanyo v. Clear Channel Worldwide*, 156 Ohio App.3d 706, 2004-Ohio-1793, 808 N.E.2d 482.

Ohio Statutory Limitations

R.C. 4113.62(D)(2) limits the enforceability of ADR clauses under Ohio law. Under the statute, parties to a construction contract cannot agree to conduct ADR outside of Ohio under ar circumstances if the construction proje is located in Ohio. Such a contractual provision is deemed to violate public policy as a matter of law.

If the court does invalidate an ADR clause pursuant to R.C. 4113.62(D)(2), the ADR must take place in the county where the construction project is located, or at another location within Ohio mutually agreed to by the parties.

In Ohio, ADR is encouraged as a method to settle disputes. Parties to construction-project agreements routinely subject themselves to mandatory arbitration or pre-suit mediation. Additionally, it is very difficult to prove unenforceability of an ADR clause under Ohio common law. However, R.C. 4113.62(D)(2) provides certain limitations. Under the statute, parties to a construction contract cannot agree to conduct ADR outside of Ohio under any circumstances if the construction project is located in Ohio.

Andrew L. Smith is a partner in the Cincinnati, Ohio office of Rolfes Henry Co.
asmith@rolfeshenry.com