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Can A Company Change the Rules in the Middle of the Game?

The Fifth Court of Appeals recently issued a ruling on a case about whether a change of policy by a company could bind a *current* independent contractor to a mediation agreement and an arbitration agreement. The Court of Appeals held that it could.

Background Facts and the Trial Court

In February 2007, Ted Budd became a "Max Associate" and sold Max's products as an independent contractor. In early 2010, Max terminated the parties' relationship. Budd brought suit based on, among other things, his termination.

In response, Max filed a Motion to Compel Mediation and Arbitration and asked the trial court to dismiss Budd's lawsuit and order Budd to attend mediation and arbitration. Max argued that Budd entered into the independent contractor agreement and agreed to be bound by Max's policies and procedures, which require mediation and arbitration for these types of complaints. Further, by continuing the parties' relationship, Budd agreed to be bound by any subsequent amendments of the policies and procedures.

The trial court granted Max's Motion to Compel Arbitration and dismissed this case in favor of arbitration. Budd appealed this decision because he argued that the arbitration agreement was illusory.

Max's Amended Policies

After Budd had been working as an independent contractor for Max for six months, Max adopted a new Statement of Policies and Procedures. One of the new changes was that employee disputes would be arbitrated.

May 15, 2008, Max issued a check to Budd and on the front of the check Max included the statement, "By cashing this check I agree to abide by the current policies and procedures." Budd cashed the check. Further, Max argued that each associate was required to pay an annual renewal fee. After an associate renewed his account, Max's secure database, In support of their position that Budd agreed to this policy change, Max argued that on which was used to monitor the operations of an associate, automatically required the associate to agree to be bound by the current polices and procedures before the associate could again access his account. Budd paid his renewal fee and accessed his account and that could not have occurred, per Max, unless Budd agreed to be bound by the new policy.

A year later, and while Budd was still working as a contractor for Max, Max changed its policy *again* and added a new policy that disputes, such as Budd's, were to be mediated and then sent to arbitration. The changes were posted on Max's website and were to become effective in 30 days.

In response, Budd argued that the arbitration agreement was illusory because Max could unilaterally modify the policies and procedures at any time.

Court of Appeals

The first order of business was to determine whether there was a valid agreement.

A party seeking to compel arbitration under the Federal Arbitration Act (FAA) must (1) establish the existence of a valid arbitration agreement and (2) show that the claims asserted are within the scope of the agreement. In determining the validity of agreements to arbitrate, which are subject to the FAA, the Court of Appeals generally applies ordinary state contract law principles governing the formation of contracts.

Because the Court of Appeals could not determine what policies Max had in place at the time Budd became a "Max Associate" in February 2007, the Court of Appeals could not conclude whether the arbitration clause was part of the parties' underlying contract. Therefore, the Court of Appeals had to determine whether the agreement to arbitrate contained in the *new* policies and procedure would, therefore, be a stand-alone agreement and must be supported by "binding promises" on both sides as consideration for the agreement.

Budd did not argue that he never received notice of the changes or that his claims did not fall under the disputes that had to be mediated and arbitrated per Max's new policies. Budd's *only* argument was that the agreement to arbitrate was illusory and unenforceable because Max "could clearly have amended or deleted the arbitration agreement at any time."

The Court of Appeals held that mutual promises to submit a dispute to arbitration constitute sufficient consideration to support an arbitration agreement. However, an arbitration agreement may be illusory if a party can unilaterally avoid the agreement to arbitrate. In other words, if the employer can get out of arbitration because they don't want to go then the contract is illusory because both sides are not bound.

In sum, citing a ruling of the Texas Supreme Court, even if a party has the right to unilaterally modify or terminate an arbitration clause, if the modification or elimination of the clause does not apply retroactively so as to allow the party to avoid the promise to arbitrate, the arbitration clause is *not* illusory.

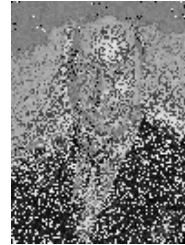
The Court of Appeals held that because Max could not unilaterally avoid arbitration of existing claims by modifying or terminating the arbitration provision, the agreement to arbitrate was not illusory. The Court of Appeals agreed with the trial court.

How Does This Apply to Me?

There is no looking back! In other words, if you have an arbitration agreement or any company policy, they can't be made retroactive so that a company or employer can change the rules on how to handle a prior claim or incident. What policies and procedures you have in place at the time of the incident will be the game rules for how you are to handle the situation even if those policies are no longer in affect.

In this case, Budd did not argue that he was unaware of the policies and procedures and that is why it was not before the trial court and Court of Appeals. However, it is not uncommon for employees to sign documents and later argue that they did not know or understand something. One way to protect the company is to actually have employees and/or contractors sign the acknowledgement agreement. A signature on a document acknowledging the new policy and their agreement could be powerful evidence.

Finally, the Court recognized the fact that Max changed its policies, but had a 30 day period before the new policy took effect. That gave employees time to read the information and decide if they were in agreement. As you add new policies, perhaps a 30 day effective day may help you if you find yourself defending the policy.



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