The Arbitration Newsletter

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The Arbitration Newsletter is published periodically by Whitaker Chalk Swindle & Schwartz PLLC, Fort Worth, Texas, to explore the rapidly developing law and practice of commercial arbitration both in the U.S. and other countries.[1]

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ARBITRATION, NURSING HOMES, AND THE "BUSINESS OF INSURANCE"

The Fredericksburg Care Company, L.P. v. Perez, No. 13-0573, 2015 Tex. LEXIS 221 (Tex. Mar. 6, 2015)[2]

In a unanimous decision in *The Fredericksburg Care Company, L.P. v. Perez*, the Texas Supreme Court recently held that §74.451 of the Texas Medical Liability Act (TMLA) is preempted by the Federal Arbitration Act (FAA).[3] TMLA §74.451 regulates the form and content of agreements to arbitrate health care liability claims. The Court held that an arbitration agreement between a patient and a Texas nursing home health provider is enforceable regardless of whether the agreement complies with §74.451.[4] As such, the TMLA §74.451 is not protected from FAA preemption by the federal McCarran-Ferguson Act (MFA).[5] Generally, when an arbitration agreement is contained within a contract affecting interstate commerce, any state laws limiting the right to arbitrate are preempted by the FAA unless the agreement falls within a federal statutory exemption from preemption.[6] The Court explained neither the statute in its entirety (TMLA) nor the specific statutory provision (§74.451) met the MFA exemption qualification.[7] Because this issue arose out of Defendant's interlocutory appeal to compel arbitration, the Texas Supreme Court remanded the case to the trial court to "proceed in a manner consistent with this opinion."[8]

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[1] Nothing in *The Arbitration Newsletter* is presented as or should be relied on as legal advice to clients or prospective clients. The sole purpose of *The Arbitration Newsletter* is to inform generally. The application of the comments in *The Arbitration Newsletter* to specific questions and cases should be discussed with the reader's independent legal counsel. My thanks to Nicole Muñoz, a 2015 graduate of Texas A&M University School of Law, for her research and drafting assistance.

[2] *The Fredericksburg Care Co., L.P. v. Perez*, No. 13-0573, 2015 Tex. LEXIS 221 (Tex. Mar. 6, 2015). On March 24, 2015, the Plaintiffs filed a motion for rehearing on which the Texas Supreme Court has yet to rule.

[3] *Id.* at *33.

[4] *See Fredericksburg*, 2015 Tex. LEXIS 221 at *33.

[5] 15 U.S.C. §§1011-1015 (2015).

[6] *Id.* at *6; *see also* 9 U.S.C. §2 (2015).

[7] *See Fredericksburg*, 2015 Tex. LEXIS 221 at *33.

[8] *Id.* at *33-34.

Fredericksburg arose from a preadmission contract signed by Elisa Zapata, a patient and nursing home resident, and The Fredericksburg Care Company, L.P. (Defendant). Zapata was under the care of the Defendant at the time of her death. When Zapata's beneficiaries (Plaintiffs) filed a negligence and wrongful death suit against Defendant, the Defendant moved to compel arbitration based on the arbitration clause contained in the preadmission agreement signed by Zapata.[9] The Plaintiffs opposed the motion to compel, arguing the arbitration clause was unenforceable because the clause's language failed to comply with §74.451 of the TMLA.[10] TMLA §74.451(a) requires any arbitration agreements entered into between patients or prospective patients and physicians or other health care providers to have a disclaimer notice in bold 10-point type that clearly and conspicuously states:

> **UNDER TEXAS LAW, THIS AGREEMENT IS INVALID AND OF NO LEGAL EFFECT UNLESS IT IS ALSO SIGNED BY AN ATTORNEY OF YOUR OWN CHOOSING. THIS AGREEMENT CONTAINS A WAIVER OF IMPORTANT LEGAL RIGHTS, INCLUDING YOUR RIGHT TO A JURY. YOU SHOULD NOT SIGN THIS AGREEMENT WITHOUT FIRST CONSULTING WITH AN ATTORNEY.**[11]

Although the Defendant admitted that the arbitration clause contained in the preadmission contract did not comply with §74.451, Defendant argued that the motion to compel should be granted because federal law, not state law, governed the enforceability of the arbitration clause since the patient-health provider transaction involved interstate commerce.[12] The Defendant further asserted that because the FAA does not require the §74.451 terms and form, the TMLA and the FAA directly conflicted with each other, and therefore, the FAA preempted §74.451.

The Plaintiffs contended that while the FAA would typically preempt §74.451, the TMLA was enacted to regulate the business of insurance, which falls within MFA's protection from FAA preemption. The MFA provides an exemption shield from federal preemption for state statutes which were enacted for the purpose of regulating the business of insurance.[13] Agreeing with the Plaintiffs, the trial court denied Defendant's motion to compel arbitration, and the court of appeals affirmed.[14]

The Texas Supreme Court granted the Defendant's petition for review in order to determine two issues: (1) whether the FAA directly preempts TMLA §74.451; and (2) whether

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[9] *Id.* at *2.
[10] TEX. CIV. PRAC. & REM. CODE §74.451(a) (2015).
[11] *Id.*
[12] *Fredericksburg*, 2015 LEXIS 221 at *5. The Texas Supreme Court previously held that "Medicare payments made to a health care provider on a patient's behalf was 'sufficient to establish interstate commerce and the FAA's application' to a case." *In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69 (Tex. 2005) (per curiam). It is undisputed that the Defendant received such payments on behalf of Elisa Zapata. *Fredericksburg*, 2015 LEXIS 221 at *5.
[13] 15 U.S.C. § 1012(b) (2015).
[14] *Fredericksburg*, 2015 LEXIS 221 at *3-4.

the MFA applied, triggering an exemption from FAA preemption.[15] In determining the first issue, the Court quickly established that the FAA applied to the preadmission contact since it is a contract affecting the interstate commerce of health care service involving Medicare funding.[16] Next, the Court referred to its decision in *In re Nexion*,[17] which held the FAA preempted the specific provision of the Texas Arbitration Act (TAA) which required an attorney to sign a client's agreement to arbitrate a personal injury claim in order to be valid – something not required by the FAA. Considering similarities between the additional TAA requirement in *In re Nexion* and the additional requirement set out in §74.451, the Court concluded "the FAA preempts section 74.451 [of the TMLA] and that the parties [Plaintiffs and Defendant] will be compelled to arbitrate—despite the arbitration clause's deficiencies under section 74.451—unless the MFA exempts the Texas law from FAA preemption."[18]

The Court then applied the three-part test that federal courts routinely use to determine if the MFA provides an applicable exemption to shield a state law from preemption by a federal statute.[19] The MFA applies if: "(1) the federal statute does not specifically relate to the 'business of insurance,' (2) the state law was enacted for the 'purpose of regulating the business of insurance,' and (3) the federal statute operates to 'invalidate, impair, or supersede' the state law."[20] The Court found the first and third elements existed in this case.[21]

In order to determine whether the second element of this three-part test could be satisfied, the Court first considered the focus and scope of the MFA in regards to what types of statutes are typically found to qualify under the MFA exemption shield.[22] The Court also identified other examples of practices that are within the scope of the MFA, including "the fixing of [insurance] rates, selling and advertising of policies, and licensing of insurance companies and their agents."[23] After analyzing the scope of the MFA exemption, the Court next analyzed the Texas statute's "overall purpose, structural framework, and effect of the entire state law."[24] To do this, the Court considered both the TMLA in its entirety[25] and TMLA §74.451 in isolation.[26] Observing that the TMLA as a whole could not satisfy the second element of the three-part test,

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[15] The Court devotes eight (8) pages of Justice Green's opinion to a thorough analysis of what constitutes the "business of insurance" that has only been summarized in this newsletter. *See Fredericksburg*, 2015 LEXIS 221 at *6-34.

[16] *Id.* at *5 (citing *In re L&L Kempwood Assocs. L.P.*, 9 S.W.3d 152, 127 (Tex. 1999) (recognizing that the FAA "extends to any contract affecting commerce, as far as the *Commerce Clause of the United States Constitution* will reach")).

[17] *In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69 (Tex. 2005) (per curiam).

[18] *Fredericksburg*, 2015 LEXIS 221 at *6.

[19] *Id.* at *7-8. Federal case law applies to interpret federal preemption law. *See Eichelberger v. Eichelberger*, 582 S.W.2d 395, 401 (Tex. 1979).

[20] *Fredericksburg*, 2015 LEXIS 221 at *7-8.

[21] *Id.* at *8.

[22] *Id.* at *12-13.

[23] *Id.* at *16-17. The Court also identified several other examples, including writing of insurance contracts and the actual performance of those contracts.

[24] *Id.* at *13.

[25] *See* TEX. CIV. PRAC. & REM. CODE §§74.001-74.452. The Texas Medical Liability Act is comprised of Chapter 74 of the Texas Civil Practices and Remedies Code.

[26] *Fredericksburg*, 2015 LEXIS 221 at *12.

the Court next examined whether §74.451, in isolation, could qualify separately.[27] Ultimately the Court determined that, even in isolation, §74.451 of the TMLA did not sufficiently concern the business of regulating insurance. Therefore, the MFA did not exempt TMLA §74.451 from FAA preemption, and the trial court should have applied the FAA in compelling arbitration of the Plaintiffs' claims.[28]

OBSERVATIONS

1. Everyone involved in this case—parties, trial court, and court of appeals—agreed the FAA applied.[29]

2. The Court carefully explained the first step to analyzing an FAA preemption issue is to determine whether the FAA applies to the transaction or contract containing an arbitration agreement; absent language adopting the FAA, the FAA will not apply to arbitration agreements that do not affect interstate commerce, and thus, would not preempt state regulations that do not affect interstate commerce, if any.[30]

3. The Texas Supreme Court's holdings in *Fredericksburg* and *In re Nexion*, lead to the conclusion that state statutes adding additional elements—not required by the FAA— to be met in order for an arbitration agreement to be valid and enforceable will be preempted by the FAA, if the FAA is applicable.[31]

4. Drafters of arbitration agreements must consider a transaction or contract as a whole to determine whether the contract or transaction affects interstate commerce, making the FAA applicable to any agreement to arbitrate contained therein, unless the parties agree otherwise.

5. Health care providers should draft preadmission arbitration agreements carefully, even to the inclusion of the TMLA §74.451(a) language out of an overabundance of caution. But if so drafting, the provider must be vigilant in compliance with the terms of such an agreement.

6. Two arbitration-related questions are not addressed in *Fredericksburg*: (1) Is a patient-nursing home preadmission agreement by nature an adhesive contract?; and (2) Is a patient-nursing home preadmission agreement a consumer contract? If either question is answered "yes," the arbitration clause drafter faces additional drafting issues.

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[27] *Id.* at *25 ("it is possible that a law, in its entirety, would fail to qualify for the MFA's exemption from preemption, but a specific statutory provision could qualify…").
[28] *Id.* at *33-34.
[29] *Id.* at *5.
[30] *Id.* ("We note, however, that if the FAA does not apply, then section 74.451 is not preempted and it is unnecessary to address whether the MFA provides an exemption from FAA preemption.").
[31] *Id.* at *5-6; *see also In re Nexion Health at Humble, Inc.*, 173 S.W.3d 67, 69 (Tex. 2005) (per curiam).