

COURT OF APPEALS
DIVISION ONE
OCT 15 2012

No. 68227-0

DIVISION I, COURT OF APPEALS OF THE STATE OF
WASHINGTON

SHEPLER CONSTRUCTION

Plaintiff-Respondents

v.

GARY LEONARD AND SUSAN KIRALY-LEONARD, and the marital
community thereof

Defendant-Appellant

and

PHH MORTGAGE SERVICES CORPORATION,

Defendant

ON APPEAL FROM SAN JUAN COUNTY SUPERIOR COURT
(Hon. Vickie I. Churchill)

REPLY BRIEF OF APPELLANTS

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I. INTRODUCTION

This appeal results from the summary judgment dismissal of the construction defect counterclaims brought by appellants/defendants Gary Leonard and Susan Kiraly (the Leonards) against appellee/plaintiff Shepler Construction.

The appeal raises the issue of whether dismissal is the proper remedy, when a consumer fails to follow a contractual arbitration provision and the parties subsequently litigate the claims and counterclaims for five years. Both in the context of this abstract issue and in the context of this particular case, dismissal is not the appropriate remedy. The dispositive principle is that arbitration is a waivable defense. Therefore, the superior court made a clear, prejudicial and reversible error, when it granted the dismissal in this case. The Court should reverse the summary judgment dismissal of the counterclaims and remand the case for a new trial, along with the additional relief relating to the scope and nature of the remand, as explained below.

II. ARGUMENT

A. **This Court Correctly Ruled the Arbitration Clause Was Not an Exclusive Remedy and the Underlying Claims Were Not Waived.**

Shepler asks the Court to revisit the earlier ruling in the 2009 appeal of this case that: “the arbitration clause did not provide that it was

the exclusive remedy. As noted above, the parties waived the arbitration clause by litigating, not the underlying claims.”¹ Br. of Resp’t at 34 (citing RAP 2.5(c)(2)). That ruling is a correct statement of law. There has been no intervening change in law. There is also no new evidence supporting Shepler’s theory. Rather, Jay Shepler testified at trial that the arbitration/dispute resolution clause did not warn that it was an exclusive remedy.² Shepler’s misunderstanding of the law governing arbitration clauses has induced the superior court to make a series of errors, leading to successive appeals.

1. **The Superior Court Has Twice Conducted a One-Sided Trial After Dismissing the Construction Defect Counterclaims.**

This is a dispute over a contract for the construction of a house. The trier of fact must determine the specific breaches committed by each party, the effect and dollar amount of the breaches, and the overall award. The award requires the evaluation of the construction project in light of Sheper’s failure to perform as promised. In response to Shepler’s suit, the Leonards had raised affirmative defenses³ and counterclaimed for the

¹ Shepler Constr., Inc. v. Leonard, noted at 153 Wn. App. 1035 (Table), 2009 WL 5153672 ¶ 15 n.1 (Wn. App. Dec. 21, 2009), review denied, 169 Wn.2d 1003, 234 P.3d 1172 (2010).

² RP (Aug. 8, 2011) at 106:23-107:8-13

³ Answer and Affirmative Defenses and Counterclaims at 4, CP 283-89.

failure to perform work in a workman like manner and the failure to properly prepare or execute its work pursuant to plans and specifications.⁴

Yet, the Leonards have never had the opportunity to present to the trier of fact the evidence supporting the affirmative defenses and counterclaims for construction defects. Shepler convinced the superior court to grant summary judgment dismissal of the counterclaims. In 2006, this Court in an unpublished per curiam decision reversed the summary judgment dismissal of the counterclaims. The decision held the Leonards had “created an issue of material fact about whether Shepler met its contractual obligation to perform in a workman like manner.”⁵ Dissatisfied with the result, Shepler unsuccessfully petitioned for review on the issue of whether “a party to a contract that provides for mandatory and binding arbitration [may] ignore the contract and assert a claim for construction defect directly in court?”⁶

On remand, Shepler convinced the superior court to grant summary judgment dismissal of the counterclaims for a second time. The ground for the second dismissal was their failure to comply with the arbitration clause.⁷ Compounding the error, Shepler convinced the superior court to deny the Leonards’ motion to compel arbitration, which would have

⁴ Answer and Affirmative Defenses and Counterclaims at 4-6, CP 283-89.

⁵ Susan Kiraly-Leonard v. Shepler Constr. Inc., noted at 132 Wn. App. 1054, 2006 WL 1217216, *1 (Jun. 6, 2006)), review denied, 160 Wn.2d 1014, 161 P.3d 1014 (2007).

⁶ Pet. For Review, CP 349.

⁷ Order Granting Summ. J. as Dispute Resolution Provision, CP 357-59.

ameliorated the prejudice resulting from the erroneous dismissal.⁸ The Leonards appealed from the denial of their motion to compel arbitration.

Although this Court affirmed the denial of the curative motion to compel arbitration, the decision concludes: “The arbitration clause did not provide that it was the exclusive remedy. As noted above, the parties waived the arbitration clause by litigating, not the underlying claims.”⁹

On remand, at the start of the trial, Shepler asked the superior court to define the scope of the summary judgment ruling in light of the trial exhibits that the Leonards were marking and the attendance of an expert witness for the Leonards regarding the construction defects.¹⁰ The Leonards explained that they had a defense of setoff or recoupment arising from their affirmative defenses of breach by nonperformance, the failure of consideration, the acts and omissions of third parties, the failure to mitigate and bar or reduction by payment setoff.¹¹ The Leonards relied on the declarations of Taylor, Willson, and Russell about the construction defects.¹² They also reiterated that they earlier had nominated Russell as

⁸ Shepler Constr., Inc. v. Leonard, noted at 153 Wn. App. 1035 (Table), 2009 WL 5153672 ¶ 15 (Wn. App. Dec. 21, 2009), review denied, 169 Wn.2d 1003, 234 P.3d 1172 (2010).

⁹ Shepler Constr., Inc. v. Leonard, noted at 153 Wn. App. 1035 (Table), 2009 WL 5153672 ¶ 15 (Wn. App. Dec. 21, 2009), review denied, 169 Wn.2d 1003, 234 P.3d 1172 (2010).

¹⁰ RP (Aug. 8, 2011) at 5:3-17.

¹¹ RP (Aug. 8, 2011) at 5:19-6:19. See Answer and Affirmative Defenses and Counterclaims at 4, CP 283-89.

¹² RP (Aug. 8, 2011) at 7:20-9:8.

an arbitrator under the three-person arbitration panel framework in the contract,¹³ in the event Shepler wanted to arbitrate. The Leonards asked the court to consider the construction defect evidence at least as part of their affirmative defenses in light of this Court’s decision.¹⁴ Shepler responded that “the remedy was to bar those claims,” otherwise “dispute resolution provisions become meaningless.”¹⁵

With remarkable consistency, the trial court ruled it would not consider construction defects in the second trial – not even in conjunction with the affirmative defenses.¹⁶ During the trial, the court admitted some evidence on incomplete work, but it barred the admission of any evidence in support of the defenses of improper or defective work.¹⁷

2. The Complete Bar/Dismissal Approach Defies Established Law.

The summary judgment ruling had been: “The Leonards are barred from bringing any claim before this court that should have been determined by submittal to binding arbitration under the contract’s dispute

¹³ RP (Aug. 8, 2011) at 7:14-9:8, 22:22-23:6.

¹⁴ RP (Aug. 8, 2011) at 16:23-18:15.

¹⁵ RP (Aug. 8, 2011) at 16:24-17:17; *id.* at 25:9-13, 25:20-23, 26:1-2, 26:3-6.

¹⁶ RP (Aug. 8, 2011) at 26:24-27:4.

¹⁷ RP (Aug. 9, 2011) at 205:6-21 (start of the second day of trial, confirming the Leonards could not ask witness Kevin Taylor questions about construction defects); RP at 220:20-222:6 (sustaining objections to Gary Leonard testimony about grouting and workmanship as violating the summary judgment order); RP at 235:18-21 (sustaining objections to his testimony about incorrectly installed cabinet); RP 245:10-18, 246:19-249:6 (same as to testimony about door and frame and drywall defects).

resolution provision.”¹⁸ The court further ruled: “the court ... finds the appropriate remedy for breach of a mandatory dispute resolution provision is barring of any claim that was subject to the provision.”¹⁹

The superior court adopted Shepler’s erroneous statement of the law: “A party that fails to abide by a contractual dispute resolution provision is **completely** barred from bringing suit.” (Emphasis added.)²⁰ “Any other rule would eviscerate mandatory contractual dispute resolution and defy this state’s strong public policy in favor of contractual dispute resolution provisions.”²¹ “[R]efusal is dispositive,”²² and “the proper remedy [is] to dismiss claims ...”²³

As established in the Brief of Appellant, Shepler confabulated the complete bar/dismissal remedy from the Pegasus decision. Br. of Appellant at 26. Yet, Shepler’s brief reiterates the very same “completely barred” principle once more citing the Pegasus decision without using any signal and without any qualification whatsoever. Br. of Resp’t at 20. The complete bar/dismissal remedy defies the established law allowing a party to ignore an arbitration provision and have its day in court.

¹⁸ Order Granting Pl.’s Mot. for Summ. J. at 3, CP 357-59.

¹⁹ Order Granting Pl.’s Mot. for Summ. J. at 3, CP 357-59. See also Letter from Court at 3 (Nov. 6, 2011), CP 79.

²⁰ RP (Mar. 14, 2008) at 13:17-8, Br. of Resp’t at 20.

²¹ Id.

²² Id.

²³ Br. of Resp’t at 8 (First Issue Presented).

a. Arbitration Is a Waivable Defense.

Ignoring an arbitration clause is legally permissive conduct sanctioned in the thousands of decisions holding that parties substantially invoking the litigation process have waived the right to arbitrate. Shepler substantially invoked the litigation process when it conducted discovery, successfully moved for summary judgment on the construction defect claim, tried the balance of the case to judgment, and unsuccessfully petitioned the Supreme Court to review this Court's reversal of the dismissal. Shepler abandoned the right to arbitrate by failing to move to compel arbitration and stay the suit.²⁴

It takes two or more to tango in court. The goose/gander rule applies. The arbitration acts grant a special statutory remedy: the specific performance of the arbitration provision by means of a motion to compel arbitration.²⁵ Either party may invoke the statutory remedy as a sword to prosecute claims in arbitration or as a shield to require the opposing party

²⁴ Resp. to Pl.'s Mot. for Summ. J. at 4:1-45, CP 398-406, *id.* at 5:18-22; CP 398-406 (arguing Shepler failed to move for a stay and to compel arbitration).

²⁵ "The Federal Arbitration Act was adopted in part to ... make arbitration agreements specifically enforceable." 21 Richard Lord A Treatise on the Law of Contracts at 31-33, § 57:3 (4th ed. 2010). Accord, Hill v. Garda CL NW, --- Wn. App. ---, 281 P.3d 334 (2012) (reversing order compelling class arbitration and remanding for arbitration on an individual basis); *id.* ¶¶ 8-15 (ruling the litigating case for nineteen months and engaging in discovery before moving for arbitration did result in a waiver of right to arbitration). Verbeek Properties, LLC v. GreenCo. Envtl, Inc., 159 Wn. App. 82, 89-90, 246 P.3d 205 (2010) (stating omitting a demand for arbitration from initial pleadings is not an affirmative election to forgo arbitration); *id.* (ruling that moving to compel arbitration less than two months after filing complaint did not waive arbitration).

to submit its claims to arbitration. But Shepler never invoked the statutory remedy. The litigation of the counterclaims through an appeal waived the statutory remedy. Also, the substantial litigation estopped Shepler from later asserting the arbitration provision as a defense to the counterclaims after five years of litigation when this Court reversed the dismissal of the counterclaims and remanded the case for trial.

Shepler has found no decisions holding that a dismissal with prejudice is the remedy for the violation of an arbitration provision, after the parties have substantially litigated the claims. We believe there is no authority for this proposition, because it fundamentally conflicts with the established law of litigation conduct waiver.

Instead of addressing the litigation-conduct waiver of the contractual right to arbitration, Shepler invokes several decisions construing public works construction contracts. To protect the public fisc from after-the-fact claims brought by contractors performing work on public projects, some public agencies include special provisions imposing stringent claim procedures. The claim procedures may impose a requirement that a “condition precedent” to suit is compliance with the claim procedure. The claim procedures may impose a limitation on remedies in the form of the requirement that a claim is “absolutely” or “completely” waived unless the contractor complies with the claim

procedure. Cf. Absher (construing public works contract with an “absolute waiver” clause and another clause that made dispute resolution a condition precedent to filing a lawsuit);²⁶ Mike M. Johnson, Inc.,²⁷ (construing public works contract with a “completely waives” clause, “by failing to follow the procedures of this section ..., the Contractor completely waives any claims for protested work” and a condition-precedent-to-judicial relief clause requiring “[f]ull compliance ... is a contractual condition precedent to the ... right to seek judicial relief.”).²⁸

But Shepler’s form contract does not have these bells and whistles.²⁹ Also, its dispute resolution provision provides for arbitration – not the multi-step claim process used on some public construction and commercial projects. Moreover, Shepler’s form contract does not make

²⁶ Absher Constr. Co. v. Kent Sch. Dist. No. 415, 77 Wn. App. 137, 140, 146, 890 P.2d 1071 (1995) (clause “absolutely waiving” some claims). Id. at 139-40, 146 (“[t]he dispute resolution procedures in the contract are clearly mandatory,” required compliance “before a lawsuit could be commenced” and “could not be waived except by an explicit written waiver.”) Id. at 139-140, 146.

²⁷ Mike M. Johnson, Inc. v. Cnty. of Spokane, 150 Wn.2d 375, 380, 78 P.3d 161 (2003); Realm, Inc. v. City of Olympia, 168 Wn. App. 1, 277 P.3d 697 (2012) (affirming dismissal of contractor’s claims for failure to comply with contract’s pre-suit notice); id. ¶ 12 (construing public works contract providing “these sections must be complied with in full, as a condition precedent to the Contractor’s right to seek claim resolution through any nonbinding alternative dispute resolution process, binding arbitration, or litigation”).

²⁸ Accord, Pegasus Constr. Corp. v. Turner Constr. Co., 84 Wn. App. 744, 929 P.2d 1200 (1997) (affirming arbitrator’s ruling arising from subcontract on public works project for Bellevue Community College). Shepler’s reliance on Pegasus is even more absurd, because in that case, the lawsuit was stayed pending arbitration and the arbitrator ruled neither party had complied with the contract. Id. at 747.

²⁹ Shepler testified that his counsel drafted the form agreement and he did not disclose to the Leonards that the form was specially drafted for Shepler. RP (Aug. 8, 2011) at 105:22-24, 107:11-12. The contract is attached to the complaint. CP 272-82 (complaint).

arbitration a condition precedent to litigation. Even if it had, the established law is: “A covenant in a contract providing for arbitration can be waived.” George V. Nolte & Co. v. Pieler Constr. Co., 54 Wn.2d 30, 34, 337 P.2d 710 (1959). Conduct or litigation may waive even an express condition that conspicuously requires that arbitration is “a condition precedent to” legal action. Id. at 32 (construing a second-tier subcontract incorporating a provision that submission to arbitration was condition precedent to legal action). Furthermore, this Court has distinguished the Mike M. Johnson decision’s contract with a condition precedent to litigation requirement from another commercial contract having no condition precedent.³⁰

In this case, the superior court effectively rewrote the contract to add an “absolute” or “complete” waiver provision and to add a condition precedent to suit requirement. But these terms cannot be implied by law.

b. The Arbitration Clause and Other Clauses Are Not an Exclusive Remedy or a Limitation of Remedies Provision.

Since this Court made its decision ruling that the arbitration clause did not provide it was an exclusive remedy and the underlying claims were not waived, Washington appellate courts have decided other cases

³⁰ Heights at Issaquah Ridge, Owners Ass'n v. Burton Landscape Group, Inc., 148 Wn. App. 400, 406-07, 200 P.3d 254 (2009)(distinguishing Mike M. Johnson’s “full compliance by the Contractor with the provisions of this section is a contractual condition precedent to the right to seek judicial relief” from the commercial contract before the court). Br. of Resp’t at 18, 20-21 (citing these cases).

addressing the waiver of arbitration clauses and the enforcement of exclusive remedies clauses.³¹ But none of the decisions supports the bar/dismissal remedy advocated by Shepler.

For example, this Court recently ruled there is a presumption that arbitration is the exclusive remedy in a collective bargaining agreement, unless stated otherwise in the contract (and even then the parties can waive arbitration through arbitration). But that presumption does not apply in this consumer case.³²

The supreme court in Torgerson v. One Lincoln Tower LLC affirmed the enforcement of a remedies limitation provision.³³ But that provision was wholly distinguishable from the arbitration clause in Shepler's form contract. A remedies limiting provision must be: (1) explicitly negotiated between a consumer buyer and seller and (2) set forth with particularity. 166 Wn.2d at 522 (citing Berg v. Stromme, 79 Wn.2d

³¹ See, e.g., Townsend v. Quadrant Corp., 173 Wn.2d 451, 462-64, 268 P.2d 917 (2012) (ruling that parent company's moving for summary judgment based on a contention they were not proper parties to the lawsuit and followed by moving to compel arbitration promptly after the superior court denied their motion for summary judgment did not waive arbitration); River House Dev. Inc. v. Integrus Architecture, P.S., 167 Wn. App. 221, 272 P.3d 289 (2012) (holding litigation-conduct waiver of right to arbitrate was an issue for trial court to decide, developer waived right to arbitrate by litigation-conduct waiver, and architectural firm was not equitably estopped from arguing waiver of right to arbitrate); Verbeek Properties, LLC v. GreenCo. Env'tl, Inc., 159 Wn. App. 82, 89-90, 246 P.3d 205 (2010) (stating omitting a demand for arbitration from initial pleadings is not an affirmative election to forgo arbitration; ruling moving to compel arbitration less than two months after filing complaint did not waive arbitration).

³² Garda CL NW, 281 P.2d 334 ¶ 20.

³³ 166 Wn.2d 510, 510, 514-15, 210 P.3d 318 (2009) (construing condominium purchase agreement with a "sole and exclusive remedy").

184, 194-95, 484 P.2d 380 (1971)). But the form contract provided by Shepler does satisfy those two requirements. First, the form contract does not indicate any negotiation whatsoever.³⁴ Second, the form contract does not set forth with any particularity that arbitration is the consumer's "sole and exclusive remedy."³⁵ In contrast, the contract in the Lincoln Tower LLC decision had that magic language. One Lincoln Tower LLC, 166 Wn.2d at 514-15 (2009) (construing a condominium purchase agreement with a "sole and exclusive remedy" in a default and remedies provision and repeated in capital letters in a signed separate page).

Shepler contends that the Leonards lost their rights when they failed to comply with the arbitration provision and with the other contract provisions whose effect amounted to a remedies limitation provision.³⁶ Yet, even if the contract satisfied the two legal requirements for a remedies limitation provision in a consumer contract (explicit negotiation and particularity) and it clearly does not, the contract provisions do not impose a bona fide limitation of remedies forfeiting common law remedies and the right to seek judicial relief.

³⁴ Shepler Construction, Inc. Building Agreement, CP 277-82.

³⁵ RP (Aug. 8, 2011) at 106:23-107:8-13 (Jay Shepler's testimony admitting the clause does not warn that it is an exclusive remedy). Agreement, CP 277-82.

³⁶ Br. of Resp't at 12-18 (discussing the arbitration clause, inspection and discovery of nonconforming work clause, final payment clause, and occupancy clause).

The form contract has a broad express warranty--not an exclusive, limited repair or replacement warranty.³⁷ While the arbitration clause requires the arbitrators to identify the work in need of repair or replacement and the contractor to undertake the work, the clause itself does not have the bells and whistles to constitute an exclusive remedy ousting the court from having any jurisdiction.³⁸ The attorney fees provision anticipates “court costs.” In other words, the parties anticipated litigation -- not merely arbitration. The occupancy provision requires final payment before occupancy, but the provision is not framed in terms of a condition precedent to occupancy.³⁹ Instead, the stated purpose of the occupancy clause is “to protect contractor’s property and equipment which may be on the premises” and avoid the risk to the property owner for personal property placed on the premises with the contractor’s consent.⁴⁰

The inspection and discovery of non-conforming work provision states the homeowner “shall have been deemed to waive” objections to

³⁷ CP 277. Cf. Am. Nursery Prods., Inc. v. Indian Wells Orchards, 155 Wn.2d 217, 226-27, 797 P.2d 477 (1990) (distinguishing a permissive limited remedies clause from exclusive remedies clause and discussing prior decision rejecting claim that guarantee was an exclusive replacement remedy); Holbrook, Inc. v. Link-Belt Constr. Equip. Co., 103 Wn. App. 279, 286, 12 P.3d 638 (2006) (citing authority distinguishing a warranty from a repair and replacement warranty). Compare CP 544-65 (Finding No. 27 stating “identifying a specific item of construction and requesting it be repaired or replaced is a condition precedent to invoking the dispute resolution provision”) with CP 281 (Dispute Resolution provision does not require identification of work as a condition precedent but provides “[i]f a dispute arises ...”).

³⁸ CP 281.

³⁹ CP 280.

⁴⁰ Id.

“materials and labor not satisfactory to owner ... if the same was reasonably discoverable upon physical inspection of the premises by the owner.”⁴¹ That provision, however, must be read in harmony with Shepler’s express warranty that “work to be performed ... in a workmanlike manner according to standard practices and in compliance with all applicable state and local building, electrical, and mechanical codes.”⁴² Jay Shepler testified that he did not expect the consumer to know the mechanical and building code in context of the nonconforming work provision.⁴³ Simply put, what Shepler expressly warranted could not be nullified in another clause, where there is no express and conspicuous disclaimer of warranty and no exclusive remedy provision.⁴⁴

In summary, the superior court erred when it granted summary judgment dismissal of the counterclaims and when it later failed to follow this Court’s ruling that the arbitration clause was not an exclusive remedy and the underlying claims had not been waived. Appellants’ Assignments of Error Nos. 1 and 3. There has been no intervening change in the law. Neither the arbitration clause nor the other provisions mandated the

⁴¹ CP 279.

⁴² CP 277.

⁴³ Shepler testified that he did not expect the Leonards to know the mechanical and building code and there was no disclaimer of oral warranties. RP (Aug. 8, 2011) at 106:7-19, 107:8-9.

⁴⁴ RP (Aug. 8, 2011) at 106:23-107:8-13.

dismissal of the construction defect counterclaims. This Court should reverse the dismissal and remand the case for a new trial.

B. The Leonards Did Not Waive Their Right to Litigate Claims, Nor Were They Estopped From Exercising that Right.

In addition to claiming that the failure to comply with the arbitration clause bars the Leonards from litigating their claims, Shepler contends that their failure to comply with the arbitration clause (and other conduct) *estops* them from pursuing *or waives* any claims that were subject to the arbitration/dispute resolution provision. Second and Third (Unnumbered) Issues, Issues Presented, Br. of Resp't at 9. The estoppel/waiver claims fail for several reasons.

1. No Voluntary Relinquishment of the Right to Litigate.

The Leonards did not knowingly and intentionally relinquish their construction defect counterclaims, so there was no express waiver.⁴⁵ There was no evidence to this effect. Arbitration is an affirmative defense whose remedy is specific performance, and that remedy may be waived. But the underlying counterclaims were not waived. Rather, the counterclaims were prosecuted in court.

Relying on a “finding” made in conjunction with the denial of the Leonards’ curative motion to compel arbitration, Shepler argues the

⁴⁵ Garda CL NW, 281 P.3d at 337 (waiver is the voluntary and intentional relinquishment of a known right).

“Leonards agreed the proper remedy for refusing to follow the [arbitration clause] was barring any claim that should have been resolved under the provision.”⁴⁶ But the Leonards did not agree that their counterclaim was barred—in fact they argued just the opposite. When Shepler moved for summary judgment dismissal on the basis of the arbitration clause, the Leonards responded that Shepler had impliedly waived the right to arbitrate or was estopped from asserting the clause, after failing to move to compel arbitration and stay the case.⁴⁷ The Leonards distinguished the Pegasus decision, which Shepler had relied upon, where the litigation had been stayed pending arbitration, the arbitrator had denied damages to each party, and the appellate court had affirmed the superior court’s dismissal of the case.⁴⁸ The Leonards argued: “Pegasus does not support Shepler’s argument that only they are entitled to present a case to the jury. If anything, Pegasus stands for the proposition that neither of the parties is entitled to recover, and the case should be dismissed.”⁴⁹ The Leonards further argued:

The premise of [Shepler’s] argument is that this matter has resulted in protracted litigation because of the Leonards. That premise does not stand up to scrutiny. Sheper is the plaintiff ... and never demanded arbitration at any time. ... To ask the court

⁴⁶ Br. of Resp’t at 18 n. 11 (citing Finding No. 21 in supporting of denial of the motion to compel arbitration).

⁴⁷ Resp. to Pl.’s Mot. for Summ. J. at 4:1-6:19, CP 575-80.

⁴⁸ Resp. to Pl.’s Mot. for Summ. J. at 4:15-25, CP 575-80.

⁴⁹ Id.

to penalize the Leonards for conduct Shepler engaged in is not a proper basis for summary judgment. The Leonards are entitled to trial in order to balance the equities. In the alternative, the court should follow the holding of Pegasus and dismiss the entire case. The defendants respectfully request that the court deny the ... motion for summary judgment against the Leonards alone.⁵⁰

These alternative arguments were not a stipulation that the dismissal of the counterclaims was the proper remedy.⁵¹ Further, the so-called finding has no legal effect in the context of the summary motion where Shepler had the burden of proving uncontroverted facts.⁵² Also, the affirmance of the denial of the motion to compel rendered moot the finding, which was improper in the first place since it was made after this Court accepted review.⁵³ In summary, there was no express waiver of the Leonards' right to litigate the counterclaims.

2. No Unequivocal Conduct or Statements Supporting Implied Waiver.

⁵⁰ Resp. to Pl.'s Mot. for Summ. J. at 6:13-19, CP 580.

⁵¹ Accord, Port of Seattle v. Lexington Ins. Co., 111 Wn. App. 901, 919, 48 P.3d 334 (2002) (referring to CR 8(e)(2)'s authorization of alternative pleadings and federal decision).

⁵² Duckworth v. City of Bonney Lake, 91 Wn.2d 19, 21-22, 856 P.2d 860 (1978) (summary judgment motion requires uncontroverted facts; findings of fact in conjunction with summary judgment were not considered on appeal because they were unnecessary and superfluous).

⁵³ Because the finding was improperly made after this Court accepted review, the Leonards moved to strike it below and later assigned error to it in the prior appeal. Br. of Appellant at 5 (Oct. 15, 2008) (assigning error to Finding No. 21 for being an unauthorized superior court action after the notice of appeal was filed and lacking substantial evidence). CP 451-59 (Defs.' Mot to Strike Pl.'s Proposed Findings of Fact and Conclusions of Law); CP 440-45 (Reply in Supp. of Defs.' Mot. to Strike Pl.'s Proposed Findings of Fact and Conclusions of Law and for Terms). Br. of Appellant at 44-48 (arguing RAP 7.2(a) and 8.3 prevented entry of the new findings and conclusions, which included new theories not argued and the omission of a statute of limitations ruling.)

To constitute implied waiver, there must exist unequivocal acts or conduct evidencing an intent to waive; waiver will not be inferred from doubtful or ambiguous factors.⁵⁴ Because the contract did not contain complete or absolute waiver terms and there was no order compelling arbitration, the Leonards' actions (including the prosecution of the counterclaims in litigation) cannot establish a prima facie showing of implied waiver.

3. No Unequivocal Conduct or Statements Supporting Estoppel.

The Leonards are not estopped from prosecuting their construction defect counterclaims. Equitable estoppel must be proven by clear, cogent, and convincing evidence.⁵⁵ To constitute equitable estoppel, there must be (1) a party's admission, statement or act inconsistent with its later claim, (2) action by another party in reliance on the first party's act, statement or admission, and (3) injury that would result to the relying party from allowing the first party to contradict or repudiate the prior act, statement or admission.⁵⁶ Shepler failed to prove these three requirements.

⁵⁴ 224 Westlake LLC v. Engstrom Properties LLC, --- Wn. App. ---, 281 P.3d 693, 702 (Jul. 30, 2012).

⁵⁵ Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1, 124 Wn.2d 816, 831, 881 P.2d 986 (1994).

⁵⁶ Resp. to Pl.'s Mot. for Summ. J. at 3-4 (equitable estoppel), CP 575-80. See Kramarevcky v. Dep't of Social and Health Serv., 122 Wn.2d 738, 743, 863 P.2d 535 (1993) (ruling DSHS was equitably estopped from recovering public assistance benefits it overpaid to recipients).

Shepler failed to identify how the Leonards have acted in an inconsistent manner and how Shepler relied upon and was injured by the inconsistent conduct. Shepler lost the opportunity to arbitrate, when it failed to employ the statutory remedy of specific performance. When the Leonards nominated an arbitrator, Shepler failed to disclose its own nominee, abandoning the three-contractor-arbitration panel set forth in its own contract.

In summary, the record does not support affirmance on the grounds of waiver and estoppel -- Shepler's second and third issues presented.⁵⁷

C. The Summary Judgment Dismissal Did Not Bar Evidence Supporting the Affirmative Defenses.

This Court does not need to reach the issue of the superior court's barring of the construction defect evidence supporting the affirmative defenses, if this Court decides to reverse and remand for a new trial on the ground that the superior court erroneously dismissed the counterclaim. See Assignments of Error 2 and 3, Br. of Appellants at 2-3, 29-32. If reversal and new trial are not granted on that ground, then a reversal and remand for a new trial is independently warranted by the superior court's refusal to consider the construction defect evidence supporting the affirmative defenses.

⁵⁷ Second and Third (Unnumbered) Issues, Issues Presented, Br. of Resp't at 9.

Shepler contends that the Leonards were not prevented from introducing evidence of recoupment or setoff and there was an inadequate offer of proof. Br. of Resp't at 31. Shepler is word-smithing and ignoring the merits of the assigned error. The recoupment/setoff defenses were the previously pleaded defenses listed in the Leonards brief on recoupment: breach by plaintiff, non-performance, and failure of consideration; the acts and omission by third parties; the failure to mitigate; and bar or reduction by a payment setoff.⁵⁸ The affirmative defenses are not barred by the statute of limitations.⁵⁹ For the same reason, the arbitration clause should not bar evidence supporting these defenses. The pretrial summary judgment order, the description of the testimony by the three contractors⁶⁰ and the superior court's ruling "not to consider construction defects" made before opening statements,⁶¹ along with the exclusion of construction defect evidence during trial⁶² demonstrates that the Leonards were prevented from establishing their recoupment/setoff affirmative defenses.

The declarations of the three contractors (Russell, Wilson, and Taylor) were the basis for the prior reversal by this Court and those

⁵⁸ Defs.' Brief on Recoupment at 2:7-12, Dkt. 478, Third Supplemental Designation.

⁵⁹ *Id.* (quoting Seattle First Nat'l Bank, N.A. v. Siebol, 64 Wn. App. 401, 407, 824 P.2d 1252 (1992).

⁶⁰ RP (Aug. 8, 2011) at 6:20-9:8.

⁶¹ RP (Aug. 8, 2011) at 26:24-27:6,

⁶² RP (Aug. 9, 2011) at 205:6-21; *id.* at 235:18-21; *id.* at 245:10-18, 246:19-249:6. See supra n. 17 (describing the testimony).

declarations were already in the record. They were submitted again with the trial brief.⁶³ The Wilson and Taylor declarations were marked as Trial Exhibits 38, and 39, and 60⁶⁴ and the Russell (Building Consults Group Report) was marked as Trial Exhibit 37.⁶⁵ The proposed testimony was also summarized in the trial brief.⁶⁶ “An offer of proof is not required ... if the substance of excluded evidence is apparent from the record.”⁶⁷ An offer of proof is primarily relevant to the propriety of a trial court’s order excluding evidence.

In summary, the trial court erred when it excluded the evidence about construction defects offered in support of affirmative defenses. Assignments of Error 2 and 3, Br. of Appellants at 2-3, 29-32.

D. The Post-Trial Findings Regarding the Dismissal Order and the Balance of the Record Supports Reassigning the Case to Another Judge.

The 2006 appellate decision and mandate remanded the case for a new trial.⁶⁸ The 2006 decision declined to address Shepler’s claim for damages resulting from the Leonards’ failure to abide by the arbitration clause, “[b]ecause we remand for trial ...” But instead of having a trial on

⁶³ Ex. A –D, Def.’s Trial Br., CP 33-51.

⁶⁴ Ex. List, CP 72-76.

⁶⁵ Ex. List, CP 72-76.

⁶⁶ Defs.’ Trial Br., CP 25-28, 30.

⁶⁷ State v. Ray, 116 Wn.2d 531, 539, 806 P.2d 1220 (1991).

⁶⁸ Susan Kiraly-Leonard v. Shepler Constr. Inc., noted at 132 Wn. App. 1054, 2006 WL 1217216 (Jun. 6, 2006), review denied, 160 Wn.2d 1014, 161 P.3d 1014 (2007).

the issue, the superior court decided to summarily dismiss the Leonards' counterclaims, causing this appeal.⁶⁹ Moreover, the 2011 trial and judgment reflects that Shepler did not prosecute a claim for damages for the Leonards' failure to abide by the arbitration clause in the new trial.⁷⁰

The superior court's post-trial findings demonstrate that the court has entrenched opinions that it cannot set aside. Assignment of Error No. 5 is that the post-trial Finding Nos. 2 and 27 were factually and legally incorrect. Br. of Appellants at 3; *id.* at 35-40. Finding No. 2 was the prior summary judgment and No. 27 was the Leonards' refusal to follow the dispute resolution process. The Leonards' consistent position is the Shepler never initiated the process since "Shepler never hired an independent contractor as it was required to, nor did it move to compel arbitration once it filed the lawsuit."⁷¹

Findings Nos. 2 and 27 incorporated by reference the court's post-trial "remarks about the summary judgment entered on March 31, 2008."⁷² Those remarks were the court's construction of the scope of the arbitration clause, who would invoke it, why a contractor would not invoke it, and

⁶⁹ *Id.* n. 4.

⁷⁰ Findings of Fact and Conclusions of law, CP 222-46; Judgment, CP 247-50.

⁷¹ Supplemental Br. on the Issue of Pl.'s Compliance with Dispute Resolution Provisions of the Contract at 8:13-15 (Dkt. No. 273), CP 334-42. See RP (Dec. 16, 2004) at 297:10-15 (Jay Shepler testimony admitting he did not specifically demand arbitration and notify the Leonards that he hired an arbitrator/contractor).

⁷² CP 225, 231.

how the refusal to comply with the arbitration procedure waived any claim of construction defect.⁷³ But those were not issues decided at trial. The post-trial remarks include the court's erroneous statements that Shepler never knew the heating system was in dispute for eight years, the warranty being from the manufacturer, and the Leonards having chosen the system (when in fact the Shepler recommended the system).⁷⁴ The Leonards have demonstrated why each of the statements was not supported by any evidence. Br. of Appellants at 36-40 (refuting the statements). Shepler implicitly concedes this, by failing to address the two assignments of error and the arguments in support of them.

The superior court judge has "already expressed views on disposition" of the heating system, breach of the arbitration clause, and other issues.⁷⁵ The superior court judge has been unable to set aside her predetermined views in a new trial. The transfer of the case to another judge on remand is appropriate. In light of the new evidence of the construction defects that will be provided on remand, the overall trial and evidence will be different. Therefore, a new trial is the appropriate remedy.

⁷³ CP 224-25 (citing Absher, 77 Wn. App. 137).

⁷⁴ CP 223:5-18.

⁷⁵ State v. Sledge, 133 Wn.2d 828, 846 n.9, 947 P.2d 1199 (1998).

E. The Jury Trial Issue Should Be Revisited on Remand.

The Leonards made a jury demand based on their counterclaim for damages, but the trial court struck the demand after dismissing the counterclaims.⁷⁶ The trial court has wide discretion in determining whether an action is primarily legal or equitable in nature, where an action is neither purely legal or equitable in nature.⁷⁷ Here, the trial court struck the jury demand after it erroneously dismissed the construction defect counterclaims. If those claims are resuscitated, then requisite factors favor a jury trial or at minimum revisiting the determination on remand.⁷⁸

III. CONCLUSION

The summary judgment dismissal of the counterclaims was prejudicial error. Although the superior court was provided several opportunities to correct or mitigate the erroneous ruling, it declined to do so. Given the unique circumstances of this case, this Court should reverse the dismissal order, grant the Leonards fees, remand the case for a new trial, and direct the transfer of the case to another judge, with a redetermination of whether there should be a jury trial.

⁷⁶ CP 566-67 (jury demand); CP 568-70 (motion to strike); CP 571-74 (response).

⁷⁷ Auburn Mech., Inc. v. Lydig Constr., Inc., 89 Wn. App. 893, 897, 951 P.2d 311 (ruling while subcontractor's claim against owner was legal in nature and thus subcontractor had a right to a jury trial on its quantum meruit claim), review denied, 136 Wn.2d 1009, 966 P.2d 902 (1998); id. at 893. (reversing denial of request for jury trial).

⁷⁸ Auburn Mech., 89 Wn. App. at 899; Johnson v. Perry, 20 Wn. App. 696, 699, 582 P.2d 886 (1978).

RESPECTFULLY SUBMITTED this 15th day of October, 2012.

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CERTIFICATE OF SERVICE

I, Julie Kelly, hereby certify under penalty of perjury under the laws of the state of Washington that on October 15, 2012, I served a copy of the document to which this Certificate is attached on the following parties

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| <p>K. GARL LONG, ESQ. Law Office of K. Garl Long 1215 S. Second Street, Suite A Mount Vernon, WA 98273 Garl@longlaw.biz Tele: 360-336-3322 Fax: 360-336-3122 Garl@longlaw.biz</p> | <p><input type="checkbox"/> by CM/ECF <input checked="" type="checkbox"/> by Electronic Mail <input type="checkbox"/> by Facsimile Transmission <input checked="" type="checkbox"/> by First Class Mail <input type="checkbox"/> by Hand Delivery <input type="checkbox"/> by Overnight Delivery</p> |
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s/Julie L. Kelly
Julie L. Kelly

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