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Bankruptcy Courts Order Arbitration of Truth in Lending Act Claims

A federal bankruptcy court in Alabama ordered arbitration of a debtor's claim that one of his creditors violated the Truth in Lending Act (TILA). In its ruling, the court rejected the notion that a bankruptcy court may refuse to enforce an arbitration agreement simply because the underlying dispute is a core bankruptcy proceeding.

In *Rozell v. CitiFinancial Auto Corp.*, No. 06-81483 JAC13, 2006 WL 3531284 (Bankr. N.D. Ala. Dec. 7, 2006), Rozell and CitiFinancial entered into an arbitration agreement in connection with the financing and sale of a pickup truck.

Three years later, Rozell filed for bankruptcy. As part of the bankruptcy proceeding, CitiFinancial filed a claim for the unpaid balance on the pickup truck. Rozell then filed a complaint against CitiFinancial, seeking monetary damages under TILA.

CitiFinancial filed a motion to compel arbitration of Rozell's TILA claim. The court's ruling on that motion depended on whether Congress intended to preclude a waiver of judicial remedies for the statutory rights at issue, which in turn depended on whether there was an "inherent conflict" between the Federal Arbitration Act (FAA) and the Bankruptcy Code.

As the court explained, the "inherent conflict" analysis has generally focused on "whether an action constitutes a core or non-core proceeding with some courts refusing to compel arbitration of core proceedings, but generally finding that non-core proceedings are subject to arbitration."

The court rejected the notion that a bankruptcy court may refuse to enforce an arbitration agreement simply because the underlying dispute is a core bankruptcy proceeding.

After discussing a split of authority on whether TILA claims constitute a core proceeding, the court concluded that Rozell's TILA claim was not a core proceeding because "TILA actions do not depend on the bankruptcy laws for their existence and can proceed in another court absent the bankruptcy filing."

The court further concluded that it would order arbitration even if the TILA were a core proceeding because, as the Third Circuit explained in *In re Mintze*, 434 F.3d 222 (3d Cir. 2006), "finding that a proceeding is a core proceeding does not automatically give a bankruptcy court the discretion to deny arbitration."

Another bankruptcy court recently cited *Mintze* for the principle that a "core" designation, standing alone, is not sufficient to demonstrate an "inherent conflict" between the Bankruptcy Code and the FAA. See *In re Merrill*, 343 B.R. 1 (Bankr. D. Me. 2006). However, in a subsequent decision, a federal district court within that circuit embraced the core/non-core approach, despite its overbreadth, because the approach supplies a bright line rule. See *In re Brown*, No. CA 05-5238, 2006 WL 3373333 (D.R.I. Nov. 20, 2006).

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Arbitration Agreement Covers Non-signatory Agent Who Recovered Vehicle for Lender

A federal district court in Florida ruled that a nonsignatory could invoke an arbitration agreement under the doctrine of equitable estoppel because the claims against the nonsignatory were based on the same facts and circumstances as claims being brought against signatories to the agreement.

In *Smart v. Bob Wilson Dodge Inc.*, No. 806-CV-22T-30TGW, 2006 WL 3837530 (M.D. Fla. Dec. 29, 2006), Smart financed the purchase of an automobile from Bob Wilson Dodge through Americredit Consumer Loan Corporation (“Americredit”). The contract between the parties contained an arbitration clause. After Smart defaulted on the loan, Americredit hired A-Expert Recovery (A-Expert) to recover the vehicle.

Smart subsequently sued A-Expert, Americredit, and Dodge for alleged misconduct in connection with A-Expert’s attempts to recover the vehicle. A-Expert filed a motion to compel arbitration despite being a nonsignatory to the contract containing the arbitration clause.

The broadly-worded arbitration agreement required arbitration of “any controversy, claims, suit, demand, counterclaim, cross claim, or third-party complaint, arising out of or related to this Order or the parties’ relationship.” The court concluded that A-Expert could invoke the arbitration agreement because the claims against A-Expert fell within the scope of the broadly worded agreement.

Also, Smart’s claims “assert[ed] interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract.” Accordingly, the court ordered that Smart’s claims against A-Expert be arbitrated.

New Jersey Court Rejects Typical Challenges to Vehicle Lease Arbitration Agreement

The Appellate Division of the New Jersey Superior Court upheld an arbitration agreement challenged as ambiguous and difficult to read, finding that the agreement clearly explained that the parties were giving up the right to a jury trial.

In *Fernandes v. Ramsey Nissan*, No. DC-013539-04, 2006 WL 3102615 (N.J. Super. Ct. App. Div. Nov. 2, 2006), Fernandes leased a motor vehicle from Ramsey Nissan (Ramsey). The lease agreement contained an arbitration clause.

When Fernandes brought suit, Ramsey moved for dismissal pursuant to the arbitration agreement. In opposing the motion, Fernandes argued that the arbitration agreement was unenforceable because the language was ambiguous, there was no definitive waiver of statutory claims, and the clause was in an obscure location and exceedingly difficult to read.

The court rejected each argument. First, the court held that the language was not

ambiguous because the arbitration clause clearly stated that both parties were “giving up the right to seek remedies in court, including the right to jury trial.”

In rejecting Fernandes’ argument that there was no definite waiver of statutory claims, the court found that the arbitration clause provided Fernandes with sufficient notice that all claims arising from or related to the lease would be resolved through arbitration. Also, as the court noted, the clause did not contain any limiting language that could be interpreted to exclude statutory claims.

Finally, the court held that the arbitration agreement was not obscure, hard to find, or difficult to read. The first page of the lease contained a notice, in bold print, advising the signatory that he was agreeing to arbitrate by the signing the agreement. Additionally, the arbitration clause was labeled “Agreement to Arbitrate,” located in a text box, and not in abnormally small type.

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apply. Specifically, Ornelas’ consumer protection claim did not entail the complexity and expense that attended the antitrust claim in *Kristian*. Moreover, the bar on class-wide proceedings would not preclude Ornelas from vindicating his statutory rights because his alleged damages (\$3,582) and his claims for punitive damages and attorney fees gave him sufficient incentive to pursue his claims on an individual basis.

A minority of jurisdictions have held that a bar on class-wide proceedings may be unenforceable if it operates as an exculpatory clause by insulating the party with superior bargaining power from liability for conduct that causes a small amount of damages to a large number of people. See, e.g., *Discover Bank v. Superior Court*, 113 P.3d 1100, 1110 (Cal. 2005).

The *sine qua non* of the minority rule is the notion that the small amount of damages does not provide sufficient incentive for pursuing an individual claim. The court in this case recognized that aspect of the rule, but other courts have pushed the rule beyond the limits of its reasoning.

For example, in *Vasquez-Lopez v. Beneficial Oregon, Inc.*, No. A125270, 2007 WL 294116 (Or. Ct. App. Jan. 31, 2007), the court relied on the reasoning of *Discover Bank* in holding that a bar on class-wide proceedings rendered an arbitration agreement unenforceable. However, the damages in that case were hardly small. In fact, the plaintiffs’ ultimate recovery totaled \$742,291.23. Compare *Delta Funding Corp. v. Harris*, 912 A.2d 104, 115 (N.J. 2006) (finding that the homeowner “ha[d] adequate incentive to bring her claim as an individual action”).

Fifth Circuit Holds that Expansive Arbitration Agreement Applies to All Claims that “Touch” Matters Covered by the Motor Vehicle Sales Contract

The Fifth Circuit Court of Appeals held that an arbitration clause “capable of expansive reach” applied to claims arising from the sale of an automobile because the claims “touch[ed] matters” covered by the underlying contract.

In *Ford Motor Co. v. Ables*, No. 05-60391, 2006 WL 3431602 (5th Cir. Nov. 29, 2006), Ables and several others sued Ford, alleging that a Ford dealership sold them pre-owned vehicles that were not properly certified.

Ford filed a motion to compel arbitration based on an arbitration clause in the underlying retail installment contracts. The district court denied the motion on the ground that the claims against Ford “seemingly” fell outside the scope of the arbitration agreement.

On appeal, the court started its analysis by citing the rule that “[a]rbitration should not be denied unless it can be

said with positive assurance that an arbitration clause is not susceptible of an interpretation which would cover the dispute at issue.” Applying that rule, the court noted that the arbitration clause in the retail installment contracts was “capable of expansive reach” and thus would apply to any dispute that “touch[ed]” matters covered by the contract.

Under that construction, the claims against Ford fell within the scope of the arbitration agreement because the claims touched matters covered by the contract – namely, the sale of the automobile. In opposing arbitration, Ables and the other buyers argued that the retail installment contract covered only the extension of credit and not the sale. The court rejected this argument based on Mississippi’s statutory definition of a “retail installment contract” and the contract’s express references to the sale.

The court also concluded that the principles of equitable estoppel would allow Ford, a nonsignatory, to claim the benefit of the arbitration agreement because the claimants were alleging “substantially interdependent and concerted misconduct” by Ford (a nonsignatory) and the dealership (a signatory). Accordingly, the court remanded the case with instructions to order arbitration.

As the court observed, the federal policy favoring arbitration has given rise to the rule that any ambiguities regarding the scope an arbitration agreement “must be resolved in favor of arbitration.” Some courts apply this presumption in favor of arbitrability not only to the scope but also to the existence of an arbitration agreement. See *Franklin v. Sunflower Imports, Inc.*, 145 P.3d 945 (Kan. Ct. App. 2006).

Indiana Court Refuses to Follow FTC’s “Unreasonable” Position on Arbitration of Warranty Claims

The Indiana Court of Appeals refused to follow a Federal Trade Commission (FTC) regulation stating that Magnusson-Moss Warranty Act (the Act) claims cannot be subject to binding arbitration.

In *Walker v. DaimlerChrysler Corp.*, 856 N.E.2d 90 (Ind. Ct. App. 2006), Walker appealed from an order compelling arbitration of Magnusson-Moss claims that he brought against DaimlerChrysler. On appeal, Walker relied on an FTC regulation stating that Congress did not intend to allow binding arbitration under the Act.

Before denying Walker’s appeal, the court noted that seven of the eight courts to consider whether the Act prohibits arbitration have refused to defer to the FTC’s interpretation. The court explained that a statute will not be construed as precluding arbitration unless that intent is manifested by the statute’s text, its legislative history, or an inherent conflict between arbitration and the statute’s underlying purpose. The court further explained that the United States Supreme Court has always upheld binding arbitration

when “the statute creating the right did not explicitly preclude arbitration.”

Under the test set forth in *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 842 (1984), the court would have to defer to the FTC’s interpretation unless it was “unreasonable.”

Here, the court found the FTC interpretation unreasonable for three reasons. First, the FTC incorrectly interpreted the Act’s provision granting concurrent jurisdiction to both state and federal courts as precluding arbitration. Second, the FTC incorrectly concluded that a provision for non-binding dispute resolution acted as a prohibition on binding arbitration, when in fact it was only one option for dispute resolution.

And finally, the FTC unreasonably concluded that an arbitral forum would not adequately protect consumers, when the Supreme Court has already determined that “arbitration’s advantages often would seem helpful to individuals.”

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Colorado Federal Court Upholds Bar on Class-Wide Proceedings in Motor Vehicle Lease Dispute

In ordering arbitration of a dispute arising from the lease of a motor vehicle, a Colorado federal court upheld a bar on class-wide proceedings because the claimant's alleged damages, coupled with his claims for punitive damages and attorney fees, provided sufficient incentive for pursuing the claim on an individual basis.

In *Ornelas v. Sonic-Denver T, Inc.*, No. 06-cv-00253-PSF-MJW, 2007 WL 274738 (D. Colo. Jan. 29, 2007), Ornelas leased a motor vehicle from Sonic-Denver and Toyota Motor Credit. The lease agreement contained an arbitration clause that barred class-wide proceedings.

Two years later, Ornelas sued Sonic-Denver and its affiliates, alleging that they took advantage of his inability to speak English by fraudulently inducing him to

sign a lease agreement when they knew that he intended to buy a vehicle. Sonic-Denver moved to compel arbitration.

Ornelas argued that the arbitration agreement was unenforceable because the bar on class-wide proceedings would preclude him and other members of the proposed class from vindicating their statutory rights. In support of this argument, Ornelas cited *Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006), in which the court held that a bar on class-wide proceedings was unenforceable because the incentive of a class-wide recovery was necessary to justify the high cost of proving an antitrust violation.

In this case, the court upheld the bar on class-wide proceedings because the rationale underlying *Kristian* did not

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