IN THE MATTER OF AN INDEPENDENT REVIEW PROCESS
BEFORE THE INTERNATIONAL CENTRE FOR DISPUTE RESOLUTION

AFILIAS DOMAINS NO. 3 LIMITED,
Claimant
v.
INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS,
Respondent

ICDR Case No. 01-18-0004-2702

AMICUS VERISIGN, INC.'S APPENDIX OF LEGAL AUTHORITY

ICANN INDEPENDENT REVIEW PROCESS

June 26, 2020

LIST OF LEGAL AUTHORITIES

AUTHORITY NO.	DESCRIPTION
AA-1	*Avila v. Spokane School Dist.*, 852 F.3d 936 (9th Cir. 2017)
AA-2	*Ball Mem'l Hosp., Inc. v. Mut. Hosp. Ins., Inc.*, 784 F.2d 1325 (7th Cir. 1986)
AA-3	*Ballard v. MacCallum*, 15 Cal. 2d 439 (1940)
AA-4	*Bank of Am., N.A. v. Moglia*, 330 F.3d 942 (7th Cir. 2003)
AA-5	*Benton v. Hofmann Plastering Co.*, 24 Cal. Rptr. 268 (Ct. App. 1962)
AA-6	Black's Law Dictionary (Assignment) (11th ed. 2019)
AA-7	*Brewer Corp. v. Point Ctr. Fin., Inc.*, 223 Cal. App. 4th 831 (2014)
AA-8	Cal. Civ. Code § 1442
AA-9	*Cal. Ins. Guarantee Assn. v. Workers' Comp. Appeals Bd.*, 203 Cal. App. 4th 1328 (2012)
AA-10	*City of Cleveland v. Cleveland Elec. Illuminating Co.*, 538 F. Supp. 1306, 1318 (N.D. Ohio 1980)
AA-11	*Continental Cas. Co. v. Ryan Inc. E.*, 974 So. 2d 368, 376 (Fla. 2008)
AA-12	*Creditors Adjustment Bureau, Inc. v. IBT Media Inc*., 2019 WL 3082845 (N.D. Cal. July 15, 2019)
AA-13	*Dubuque Stone Prods. Co. v. Fred L. Gray Co.*, 356 F.2d 718 (8th Cir. 1966)
AA-14	*Edwards v. Symbolic Int'l Inc.*, 414 F. App'x 930 (9th Cir. 2011)
AA-15	*In re Foreman*, 850 N.E.2d 387 (Ill. App. 2006)
AA-16	*Johnson v. J.G. Wentworth Originations, LLC*, 391 P.3d 865 (Or. App. 2017)
AA-17	*Maples v. SolarWinds, Inc.*, 50 F. Supp. 3d 1221 (N.D. Cal. 2014)
AA-18	*McCown v. Spencer*, 8 Cal. App. 3d 216 (1970)
AA-19	*Merchants Serv. Co. v. Small Claims Court of City & Cty. of San Francisco*, 35 Cal. 2d 109 (1950)

AUTHORITY NO.	DESCRIPTION
AA-20	*Milenbach v. Comm'r*, 318 F.3d 924 (9th Cir. 2003)
AA-21	*Modern Law of Contracts* § 21:6
AA-22	*MRO Commc'ns, Inc. v. Am. Tel. & Tel. Co.*, 2015 F.3d 1351 (9th Cir. 1999)
AA-23	*Neuroaxis Neurosurgical Assocs., PC v. Costco Wholesale Co.*, 919 F. Supp. 2d 345 (S.D.N.Y. 2013)
AA-24	*One Call Prop. Servs. Inc. v. Sec. First Ins. Co.*, 165 So. 3d 749 (Fla. Dist. Ct. App. 2015)
AA-25	*Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430 (3d Cir. 1997)
AA-26	*Restatement (First) of Contracts* § 166 (1932)
AA-27	*Restatement (Second) of Contracts* § 316 (1981)
AA-28	*Restatement (Second) of Contracts* § 322 (1981)
AA-29	*Sierra Equity Grp., Inc. v. White Oak Equity Partners, LLC*, 650 F. Supp. 2d 1213 (S.D. Fla. 2009)
AA-30	*Spingola v. Whitewater Mountain Resorts of Connecticut, Inc.*, 2002 WL 31894720 (Conn. Super. Ct. Dec. 10, 2002)
AA-31	*Springfield Int'l Rest., Inc. v. Sharley*, 44 Or. App. 133(1980)
AA-32	*STS Refills, LLC v. Rivers Printing Sols., Inc.*, 896 F. Supp. 2d 364 (W.D. Pa. 2012)
AA-33	*Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961)
AA-34	*Thomas-Bonner Co. v. Hooven, Owens & Rentscheller*, 284 F. 377 (S.D. Ohio 1920)
AA-35	*Travertine Corp. v. Lexington-Silverwood,* 683 N.W.2d 267 (Minn. 2004)
AA-36	International Institute for the Unification of Private Law (UNIDROIT), Principles of International Commercial Contracts, Chapter 9 (2016)
AA-37	*U.S. Anchor Mfg., Inc. v. Rule Indus., Inc.*, 7 F.3d 986 (11th Cir. 1993)
AA-38	Upcounsel, "Transfer of Rights Contract: Everything You Need to Know," (https://www.upcounsel.com/transfer-of-rights-contract)
AA-39	*Wonsey v. Life Ins. Co. of N. Am.*, 32 F. Supp. 2d 939 (E.D. Mich. 1998)

LEGAL AUTHORITY AA-1

KeyCite Yellow Flag - Negative Treatment
Distinguished by Duncan v. Eugene School District 4J, D.Or., January 6, 2020

852 F.3d 936
United States Court of Appeals, Ninth Circuit.

Barbara AVILA; Miguel Avila, Plaintiffs–Appellants,
v.
SPOKANE SCHOOL DISTRICT 81, Defendant–Appellee.

No. 14-35965
|
Argued and Submitted December 5, 2016, Seattle, Washington
|
Filed March 30, 2017

Synopsis
Background: Student's parents brought action against public school district, alleging that district violated Individuals with Disabilities Education Act (IDEA) by failing to identify student's disability or assess him for autism. The United States District Court for the Eastern District of Washington, No. 2:10-cv-00408-EFS, Edward F. Shea, Senior District Judge, 2014 WL 5585349, granted district's motion to dismiss on statute of limitations grounds. Parents appealed.

The Court of Appeals, Christen, Circuit Judge, held that as a matter of first impression, IDEA's two-year statute of limitations requires courts to apply the discovery rule without limiting redressability to the two-year period that precedes the date when the parent or agency knew or should have known about the alleged action that forms the basis of the complaint.

Reversed and remanded.

Procedural Posture(s): On Appeal; Motion to Dismiss.

Attorneys and Law Firms

***937** Mark A. Silver (argued) and Jeffrey A. Zachman, Denton US LLP, Atlanta, Georgia; Richard D. Salgado, Dentons US LLP, Dallas, Texas; for Plaintiffs–Appellants.

Gregory Lee Stevens (argued), Stevens Clay P.S., Spokane, Washington, for Defendant–Appellee.

Appeal from the United States District Court for the Eastern District of Washington, Edward F. Shea, District Judge, Presiding, D.C. No. 2:10–cv–00408–EFS

Before: M. Margaret McKeown, Richard C. Tallman, and Morgan Christen, Circuit Judges.

OPINION

CHRISTEN, Circuit Judge:

The Avilas, parents of a student in Spokane School District 81, appeal the district court's order dismissing their claims that the District violated the Individuals with Disabilities Education Act (IDEA), 20 U.S.C. § 1400 *et seq.* The Avilas argue that the district court misapplied the statute of limitations in 20 U.S.C. § 1415(f)(3)(C) to their claims that the District failed to identify their child's disability or assess him for autism in 2006 and 2007. [1]

In a question of first impression for this court, we conclude that the IDEA's statute of limitations requires courts to bar only claims brought more than two years after the parents or local educational agency "knew or should have known" about the actions forming the basis of the complaint. Because the district court barred all claims "occurring" more than two years before the Avilas filed their due process complaint, we remand so that the district court can determine when the Avilas knew or should have known about the actions forming the basis of their complaint.

***938 BACKGROUND**

Appellants Barbara and Miguel Avila are the parents of G.A., a student in Spokane School District 81. In 2006, when G.A. was five, the Avilas asked the District to evaluate him for special education services based on "[b]ehavior" issues. One of the reasons for this request was a preschool teacher's concern that G.A. might be "showing slight signs of autism." In December 2006, a school psychologist evaluated G.A. and concluded that although he displayed some "behaviors of concern," G.A.'s behavior was not severe enough to qualify for special education services under the IDEA. G.A.'s mother was given a copy of the evaluation report and signed a form stating that she agreed with the evaluation results.

In the fall of 2007, G.A. enrolled in kindergarten. A private third-party physician diagnosed him with Asperger's Disorder in October 2007, and the Avilas requested that the District reevaluate G.A.'s eligibility for special education services. A school psychologist concluded in a reevaluation dated April 14, 2008 that G.A. was eligible for special educational services under the category of autism and, from April 2008 until February 2009, the Avilas and representatives from the District met multiple times to discuss an Individualized Education Program (IEP) for him. [2] The Avilas and the District initially disagreed, but eventually signed an IEP in February 2009. G.A. then began attending ADAPT, a specialized program in the District for students with autism.

About a year later, the District reevaluated G.A., assessing his behavior, speech and language, occupational therapy needs, and academic achievements, including reading, writing, and mathematics. The District then drafted another IEP. The Avilas did not agree with the reevaluation's findings and did not sign it. Instead, they requested an Independent Educational Evaluation (IEE) at the District's expense. *See* Wash. Admin. Code § 392–172A–05005(1). The District denied this request.

The Avilas filed a request for a due process hearing with the Washington State Office of Administrative Hearings on April 26, 2010. As required by law after the denial of a parent's request for an IEE, the District also initiated a due process hearing with the Washington State Office of Administrative Hearings to consider whether the District's reevaluation was sufficient. *See* Wash. Admin. Code § 392–172A–05005(2)(c). Ultimately, the ALJ ruled that the District's reevaluation was appropriate and that the Avilas were not entitled to an IEE at the District's expense. In a separate order, the ALJ ruled in favor of the District on all other claims. Specifically, he concluded that eleven of the Avilas' pre-April 2008 claims were time-barred. These claims consisted of nine procedural claims concerning the District's alleged failure to give prior written notice to the Avilas and two substantive claims. The substantive claims alleged that the District denied G.A. a free appropriate public education (FAPE) by failing to identify him as a child with a disability in 2006, and that the District failed to assess his suspected disability in 2006 and 2007. The ALJ concluded that no statutory exceptions applied and held that the Avilas' claims were time-barred, reasoning "[t]he Parents['] due process complaint was filed on April 26, 2010 and any complaint by Parents regarding the District actions or inactions occurring prior to April 26, 2008 ***939** are barred by the statu[t]e of limitations." [3]

The Avilas timely appealed both decisions to the United States District Court for the Eastern District of Washington, where their appeals were consolidated. The consolidated appeal addressed seven of the claims the ALJ deemed time-barred: five of their prior written notice claims and the two substantive claims arguing denials of G.A.'s right to a FAPE.

The district court agreed with the ALJ's determination that neither exception to the statute of limitations applied and affirmed the ALJ's decision that the IDEA's two-year limitations period barred the Avilas' claims arising before April 26, 2008. The district court also affirmed the ALJ's ruling that the April 2010 reevaluation was appropriate, that the IEP provided G.A. with a FAPE, and that the Avilas were not entitled to an IEE at the District's expense. The Avilas timely appealed to this court. They argue that the district court improperly applied the IDEA's statute of limitations to their two substantive claims. They do not appeal the district court's ruling that their five remaining prior written notice claims lack merit.

JURISDICTION AND STANDARD OF REVIEW

The district court had jurisdiction pursuant to 20 U.S.C. § 1415(i)(2)(A) and 28 U.S.C. § 1331. We have appellate jurisdiction pursuant to 28 U.S.C. § 1291.

Our court reviews de novo the district court's conclusions of law, including the question whether a claim is barred by a statute of limitations. *See* *Butler v. Nat'l Cmty. Renaissance of Cal.*, 766 F.3d 1191, 1194 (9th Cir. 2014).

DISCUSSION

I. The IDEA's statute of limitations requires courts to apply the discovery rule.

A. Statutory overview

"The IDEA provides federal funds to assist state and local agencies in educating children with disabilities, but conditions such funding on compliance with certain goals and procedures." *Ojai Unified Sch. Dist. v. Jackson*, 4 F.3d 1467, 1469 (9th Cir. 1993). The IDEA seeks "to ensure that all children with disabilities have available to them a free

appropriate public education." 20 U.S.C. § 1400(d)(1)(A). "A FAPE is defined as an education that is provided at public expense, meets the standards of the state educational agency, and is in conformity with the student's IEP." *Baquerizo v. Garden Grove Unified Sch. Dist.*, 826 F.3d 1179, 1184 (9th Cir. 2016) (citing 20 U.S.C. § 1401(9)). Upon request of a parent or agency, a local educational agency must "conduct a full and individual initial evaluation" to determine whether a child has a disability and the child's educational needs. 20 U.S.C. § 1414(a)(1)(A)–(C). If a child is determined to have a disability, a team including a local educational agency representative, teachers, parents, and in some cases, the child, formulates an IEP. [4] ***940** § 1414(d)(1)(B). The local educational agency must conduct a reevaluation of the child if it "determines that the educational or related services needs, including improved academic achievement and functional performance, of the child warrant a reevaluation," or if a reevaluation is requested by the child's parents or teacher. § 1414(a)(2)(A).

The IDEA permits parents and school districts to file due process complaints "with respect to any matter relating to the identification, evaluation, or educational placement of the child, or the provision of a free appropriate public education to such child." § 1415(b)(6)(A). The state educational agency or local educational agency hears due process complaints in administrative due process hearings. § 1415(f)(1)(A). If a party disagrees with the administrative findings and decision, the IDEA allows for judicial review in state courts and federal district courts. § 1415(i)(2)(A).

B. The IDEA's statute of limitations

Prior to 2004, the IDEA did not include a statute of limitations for due process hearings or complaints. *See* 20 U.S.C. § 1415(b)(6) (1999); *S.V. v. Sherwood Sch. Dist.*, 254 F.3d 877, 879 (9th Cir. 2001) ("The IDEA specifies no limitations period governing either a plaintiff's request for an administrative hearing *or* the filing of a civil action."). Congress amended the IDEA in 2004 to add a two-year statute of limitations period that is now codified in two different provisions of the IDEA: 20 U.S.C. § 1415(b)(6)(B) and 20 U.S.C. § 1415(f)(3)(C). [5] Our circuit has not addressed these amendments, but in *G.L. v. Ligonier Valley School District Authority*, 802 F.3d 601 (3d Cir. 2015), the Third Circuit described § 1415(b)(6)(B) and § 1415(f)(3)(C) as alike "in almost all respects" except for one glaring ambiguity: "§ 1415(b)(6)(B)'s two-year limitations period runs backward instead of forward from the reasonable discovery date." *Id.* at 610.

The Avilas contend that § 1415(f)(3)(C) requires this court to apply a discovery rule to IDEA claims, meaning that the statute of limitations is triggered when "a plaintiff discovers, or reasonably could have discovered, his claim." *See O'Connor v. Boeing N. Am., Inc.*, 311 F.3d 1139, 1147 (9th Cir. 2002). The District does not dispute that the discovery rule should apply to trigger the statute of limitations, but argues that the district court *did* apply the discovery rule and that the Avilas' claims are barred because they failed to file suit within two years after they knew or should have known about their claims.

C. Analysis

The application of the IDEA's statute of limitations is a question of first impression for this court: we have not squarely addressed the "knew or should have known" standard in the IDEA or the seemingly contradictory provisions in § 1415(b)(6)(B) and § 1415(f)(3)(C). In the first federal appellate decision addressing how § 1415(b)(6)(B) and § 1415(f)(3)(C) should be reconciled, the Third Circuit concluded that the IDEA's statute of limitations requires courts to apply the discovery ***941** rule described in § 1415(f)(3)(C). *Ligonier*, 802 F.3d at 625. The statutory text of the IDEA, including its language and context, persuade us that the Third Circuit's approach in *Ligonier* is correct and that the IDEA's statute of limitations requires courts to apply the discovery rule described in § 1415(f)(3)(C). The Department of Education's interpretation of the 2004 statutory amendments and the associated legislative history support this reading of the statute.

"When interpreting a statute, we are guided by the fundamental canons of statutory construction and begin with the statutory text." *United States v. Neal*, 776 F.3d 645, 652 (9th Cir. 2015) (citing *BedRoc Ltd., LLC v. United States*, 541 U.S. 176, 183, 124 S.Ct. 1587, 158 L.Ed.2d 338 (2004)). "The plainness or ambiguity of statutory language is determined by reference to the language itself, the specific context in which the language is used, and the broader context of the statute as a whole." *Geo–Energy Partners–1983 Ltd. v. Salazar*, 613 F.3d 946, 956 (9th Cir. 2010) (quoting *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341, 117 S.Ct. 843, 136 L.Ed.2d 808 (1997)). "If the statutory text is ambiguous, we employ other tools, such as legislative history, to construe the meaning of ambiguous terms." *Benko v. Quality Loan Serv. Corp.*, 789 F.3d 1111, 1118 (9th Cir. 2015).

Read in isolation, § 1415(f)(3)(C) appears straightforward. Entitled "Timeline for requesting hearing," it states:

> A parent or agency shall request an impartial due process hearing within 2 years of the date the parent or agency knew or should have known about the alleged action that forms the basis of the complaint, or, if the State has an explicit time limitation for requesting such a hearing under this subchapter, in such time as the State law allows.

§ 1415(f)(3)(C). However, an ambiguity arises when § 1415(f)(3)(C) is read in conjunction with § 1415(b)(6)(B). The latter states, under the heading "Types of procedures," that the IDEA allows:

> [An opportunity for any party to present a complaint] which sets forth an alleged violation that occurred not more than 2 years before the date the parent or public agency knew or should have known about the alleged action that forms the basis of the complaint, or, if the State has an explicit time limitation for presenting such a complaint under this subchapter, in such time as the State law allows....

§ 1415(b)(6)(B).

The Third Circuit's *Ligonier* decision recognized that litigants have advanced various interpretations of the IDEA's statute of limitations: (1) the occurrence rule suggested by § 1415(b)(6)(B), under which the statute of limitations begins to run on the date the injury occurs; (2) the discovery rule provided in § 1415(f)(3)(C); or (3) the "2+2" rule. *Ligonier*, 802 F.3d at 607, 612–15. Under the 2+2 rule, the statute of limitations is triggered when a plaintiff knew or should have known of his claim, but the scope of redressable harm is limited to the "two years *before* the reasonable discovery date through the date the complaint was filed, which could be up to two years *after* the reasonable discovery date, for a maximum period of relief of four years." *Id.* at 607.

We first conclude that Congress did not intend the IDEA's statute of limitations to be governed by a strict occurrence rule. Both § 1415(b)(6)(B) and § 1415(f)(3)(C) include language pegging the limitations period to the date on which the parent or agency "knew or should have known about the alleged action that forms the basis of the complaint," not the date on which the ***942** action occurred. *See* § 1415(b)(6)(B), (f)(3)(C). If Congress intended a strict occurrence rule, there would have been no need to include the "knew or should have known" language in § 1415(b)(6)(B) and § 1415(f)(3)(C).

The text of the two provisions also undercuts the 2+2 rule. Both § 1415(b)(6)(B) and § 1415(f)(3)(C) allow the two-year statute of limitations to be replaced by "an explicit time limitation ... in such time as the State law allows." § 1415(b)(6)(B), (f)(3)(C). If states adopt their own statutes of limitations pursuant to these provisions, § 1415(b)(6)(B) and § 1415(f)(3)(C) provide that the federal exceptions to the statute of limitations still apply, *see* 20 U.S.C. § 1415(b)(6)(B), (f)(3)(C)–(D), and it would make little sense to incorporate the federal exceptions for equitable tolling if § 1415(b)(6)(B) were a remedy cap rather than a preview of the statute of limitations set forth in § 1415(f)(3)(C). *See Ligonier*, 802 F.3d at 615. We hold that the text of the IDEA cannot support the "2+2" construction of the statute.

The next question is how to reconcile these two seemingly conflicting provisions. Looking to "the specific context in which the language is used and the broader context of the statute as a whole," *Geo–Energy Partners–1983*, 613 F.3d at 956, § 1415(b) provides an overview of the other provisions of § 1415, including § 1415(f), while § 1415(f)(3)(C) addresses in more specific language the allowable period for requesting a due process hearing. *See Ligonier*, 802 F.3d at 616–18. Section 1415 is entitled "Procedural Safeguards," with subsection (a) mandating that any state educational agency that receives federal assistance under the subchapter must establish and maintain certain procedures. Subsection (b), entitled "Types of procedures," broadly outlines the many procedures state educational agencies are required to adopt, including the opportunity for any party to present a complaint regarding the identification, evaluation or educational placement of the child, or the provision of a FAPE. § 1415(b).

In contrast, § 1415(f), entitled "Impartial due process hearing," describes in detail the procedures required whenever a parent or local education agency files a due process complaint under subsection (b)(6) or (k). Section 1415(f)(2) addresses evaluations and recommendations to be prepared in advance of a due process hearing. Section 1415(f)(3), entitled "Limitations on hearing," is divided into "Persons conducting hearing," "Subject matter of hearing," and "Timeline for requesting hearing." § 1415(f)(3)(A)–(C). It is this last provision, located in the subsection that expressly limits the right to a due process hearing, which specifies that the hearing must be requested within two years from the date the parent or agency knew or should have known about the alleged action that forms the basis of the complaint. § 1415(f)(3)(C). Thus, the structure of § 1415 supports the conclusion that "§ 1415(b)(6)(B), though poorly penned, was intended merely as a synopsis of § 1415(f)(3)[(C)]'s" "knew or should have known" benchmark for the statute of limitations. *See* *Ligonier*, 802 F.3d at 618.

We have considered that Congress might have intended different limitations periods for presenting complaints and requesting due process hearings, but that possibility is inconsistent with the overall statutory scheme. Read that way, subsections (b) and (f) cannot be harmonized because § 1415(b) would bar a complaint arising from conduct occurring more than two years before the discovery date, but § 1415(f) would preserve the right to request a due process hearing concerning the same conduct. Our task is to harmonize ***943** the statutory scheme as a whole, and our interpretation of § 1415 as having just one applicable limitations period is consistent with the Department of Education's position that the two provisions provide the same limitations period, discussed *infra*. *See U.S. W. Commc'ns, Inc. v. Hamilton*, 224 F.3d 1049, 1053 (9th Cir. 2000) (stating the duty to harmonize statutory provisions is "particularly acute" when the provisions are enacted at the same time and are part of the same statute).

Other sources of statutory interpretation confirm this reading. First, the broader context of the IDEA shows that it has a wide-ranging remedial purpose intended to protect the rights of children with disabilities and their parents. One express purpose of the IDEA is "to ensure that all children with disabilities have available to them a free appropriate public education that emphasizes special education and related services designed to meet their unique needs and prepare them for further education, employment, and independent living." 20 U.S.C. § 1400(d)(1)(A). As the Supreme Court stated, "[a] reading of the [IDEA] that left parents without an adequate remedy when a school district unreasonably failed to identify a child with disabilities would not comport with Congress' acknowledgment of the paramount importance of properly identifying each child eligible for services." *Forest Grove Sch. Dist. v. T.A.*, 557 U.S. 230, 245, 129 S.Ct. 2484, 174 L.Ed.2d 168 (2009). The broad purpose of the IDEA is clear and has been acknowledged repeatedly by our court. *See* *E.M. ex rel. E.M. v. Pajaro Valley Unified Sch. Dist. Office of Admin. Hearings*, 758 F.3d 1162, 1173 (9th Cir. 2014) (citing *Forest Grove*, 557 U.S. at 244–45, 129 S.Ct. 2484); *Michael P. v. Dep't of Educ.*, 656 F.3d 1057, 1060 (9th Cir. 2011) (same); *Compton Unified Sch. Dist. v. Addison*, 598 F.3d 1181, 1184 (9th Cir. 2010) (same). Cutting off children's or parents' remedies if violations are not discovered within two years, as the occurrence rule and the 2+2 rule would do, is not consistent with the IDEA's remedial purpose. *See* *Ligonier*, 802 F.3d at 619–20 (concluding that applying the occurrence or 2+2 rules would go against the broad remedial purpose of the IDEA and serve as a *sub silentio* repeal of prior court decisions confirming the intent of the IDEA).

In commentary addressing its enabling regulations, the Department of Education (DOE) stated that it interprets § 1415(b)(6)(B) and § 1415(f)(3)(C) to provide the same limitations period. Assistance to States for the Education of Children with Disabilities and Preschool Grants for Children with Disabilities, 71 Fed. Reg. 46,706 (Aug. 14, 2006). The DOE's interpretation necessarily rejects the 2+2 rule, which assumes that § 1415(b)(6)(B) and § 1415(f)(3)(C) provide two different limitations periods, although the agency's interpretation does not offer any guidance on whether the discovery rule or occurrence rule should prevail. As the Third Circuit noted, the DOE's interpretation of its own regulation should be respected if "it has the 'power to persuade.' " *Ligonier*, 802 F.3d at 621 (quoting *Gonzales v. Oregon*, 546 U.S. 243, 256, 126 S.Ct. 904, 163 L.Ed.2d 748 (2006) and *Skidmore v. Swift & Co.*, 323 U.S. 134, 140, 65 S.Ct. 161, 89 L.Ed. 124 (1944)). The DOE's rejection of the 2+2 rule is in accord with the text of § 1415(f)(3)(C), our contextual reading of § 1415(b) as providing an overview of procedures required by the IDEA, and the IDEA's broader statutory scheme.

The IDEA's legislative history is in accord. When the 2004 IDEA amendments were crafted, the House of Representatives' initial proposal was for a one-year statute of limitations that relied on the occurrence rule and required that a complaint ***944** "set forth a violation that occurred not more than one year before the complaint is filed." H.R. Rep.

108–77, at 36 (2003). The Senate version of the bill included the wording that later became § 1415(f)(3)(C). S. Rep. 108–185, at 222 (2003) ("A parent or public agency shall request an impartial due process hearing within 2 years of the date the parent or public agency knew or should have known about the alleged action that forms the basis of the complaint...."). Considering the two draft bills, the Third Circuit concluded:

> The conference committee then incorporated the Senate's version at § 1415(f) and the House's version in the summary listing at § 1415(b). When it did so, however, it omitted to change the backward-looking framework of the House's version to the forward-looking framework of the Senate's. Thus was created the problem we grapple with today.

Ligonier, 802 F.3d at 623. This legislative history suggests that Congress intended to adopt the discovery rule, not the occurrence rule, in the final version of the 2004 amendments. *See id.*

The text and purpose of the IDEA, the DOE's interpretation of the Act, and the legislative history of the 2004 amendments all lead us to the same conclusion. We hold the IDEA's statute of limitations requires courts to apply the discovery rule without limiting redressability to the two-year period that precedes the date when "the parent or agency knew or should have known about the alleged action that forms the basis of the complaint." § 1415(f)(3)(C).

II. The district court erred by concluding that the IDEA's two-year statute of limitations necessarily barred claims arising in 2006 and 2007.

Having concluded that the IDEA's statute of limitations is triggered when "the parent or agency *knew or should have known* about the alleged action that forms the basis of the complaint," we turn to the Avilas' claims. *See* § 1415(f)(3)(C) (emphasis added). In dismissing the Avilas' complaint, the district court cited the correct standard from § 1415(f)(3)(C), but concluded, "Parents' due process complaint was made April 26, 2010. Accordingly, unless an exception is shown, the Court finds any alleged misconduct prior to April 26, 2008, was not timely raised by Parents." In other words, apart from considering the two express exceptions to the IDEA's statute of limitations, the district court barred the Avilas' claims arising before April 26, 2008 based on when the actions complained of occurred, rather than applying the discovery rule.

The district court found that Ms. Avila signed forms agreeing with the 2006–2007 evaluation results, but this does not end the inquiry because the Avilas' awareness of the evaluations does not necessarily mean they "knew or had reason to know" of the basis of their claims before April 26, 2008. *Cf. A.G. v. Paradise Valley Unified Sch. Dist. No. 69*, 815 F.3d 1195, 1205 (9th Cir. 2016) (holding that parents' consent to a disabled child's placement does not waive later challenges to the placement under Title II of the Americans with Disabilities Act and § 504 of the Rehabilitation Act, "at least where the issue is one that requires specialized expertise a parent cannot be expected to have"). Other courts have held that the "knew or had reason to know date" stems from when parents know or have reason to know of an alleged denial of a free appropriate public education under the IDEA, not necessarily when the parents became aware that the district acted or failed to act. *See, e.g.*, *Somoza v. N.Y. City Dep't of Educ.*, 538 F.3d 106, 114 (2d Cir. 2008) (holding that ***945** the "knew or should have known" date occurred when parent viewed a child's rapid improvement in a new program); *Draper v. Atlanta Indep. Sch. Sys.*, 518 F.3d 1275, 1288 (11th Cir. 2008) (holding the "knew or should have known date" occurred after new evaluation and declining to hold that "famil[ies] should be blamed for not being experts about learning disabilities").

Because the district court barred the Avilas' pre-April 2008 claims based on when the District's actions occurred, we remand to the district court to make findings and address the statute of limitations under the standard we adopt here, namely when the Avilas "knew or should have known about the alleged action[s] that form[ ] the basis of the complaint." *See* § 1415(f)(3)(C).

Each party shall bear its own costs.

REVERSED and REMANDED.

All Citations

852 F.3d 936, 341 Ed. Law Rep. 646, 17 Cal. Daily Op. Serv. 3045, 2017 Daily Journal D.A.R. 3060

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Footnotes

1 The Avilas' claim that the District violated the IDEA by failing to assess their child for dyslexia and dysgraphia is addressed in an unpublished memorandum disposition filed concurrently with this opinion.

2 The IDEA requires IEPs, which are "written statement[s] for each child with a disability," as part of its mandate of ensuring students are provided with a free appropriate public education. *See* 20 U.S.C. §§ 1401(9)(D), 1414(d).

3 There are two express exceptions to the IDEA's two-year statute of limitations: (1) when a local educational agency misrepresents that it has resolved issues underlying a claim; and (2) when a local educational agency withholds necessary information. 20 U.S.C. § 1415(f)(3)(D). The Avilas do not argue that either of these exceptions apply.

4 An IEP includes the following: 1) a statement about the child's level of academic achievement; 2) "measurable annual goals"; 3) a description of how the child's progress towards the goals will be measured; and 4) a statement of the special education and other services to be provided. 20 U.S.C. § 1414(d)(1)(A).

5 The events underlying this action took place from 2006 to April 2010, and the applicable version of the IDEA was in effect from 2004 to October 2010. *See* *Amanda J. ex rel. Annette J. v. Clark Cty. Sch. Dist.*, 267 F.3d 877, 882 n.1 (9th Cir. 2001) (applying the 1994 version of IDEA to events that took place in 1995, despite 1997 revision of IDEA). The 2010 amendments do not materially affect the analysis or outcome of this case. *See* Pub. L. No. 111–256, 124 Stat. 2643 (2010) (amending the IDEA to change references from "mental retardation" to "intellectual disabilities").

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-2

KeyCite Yellow Flag - Negative Treatment
Disagreed With by Reazin v. Blue Cross and Blue Shield of Kansas, Inc., 10th Cir.(Kan.), March 29, 1990

784 F.2d 1325
United States Court of Appeals,
Seventh Circuit.

BALL MEMORIAL HOSPITAL, INC., et al., Plaintiffs-Appellants,
v.
MUTUAL HOSPITAL INSURANCE, INC., doing business as Blue Cross of Indiana, and Mutual Medical Insurance, Inc., doing business as Blue Shield of Indiana, Defendants-Appellees.

No. 85–1481.
|
Argued Nov. 6, 1985.
|
Decided March 4, 1986.
|
Rehearing En Banc Denied April 7, 1986. *

Synopsis
Hospitals brought antitrust action against nonprofit providers of health care financing for consumers, which planned to implement a “preferred provider organization” in the state. The United States District Court for the Southern District of Indiana, Indianapolis Division, 603 F.Supp. 1077, William E. Steckler, J., denied hospitals' motion for preliminary injunction to enjoin implementation of the PPO, subsequently entered partial final judgment disposing of hospitals' state law claims while reserving their antitrust claims, and issued certificate permitting immediate appeal of state law issues. On hospitals' appeal, the Court of Appeals, Easterbrook, Circuit Judge, held that: (1) nonprofit providers lacked market power, and were therefore entitled to adopt PPO plan without further scrutiny under the Sherman Anti-Trust Act, and (2) nonprofit providers did not violate Indiana statute governing establishment of PPO plans by conducting one-sided negotiations requiring hospitals to lower their bids without feedback from nonprofit providers on others' bids or by taking price into account in determining hospitals which would be permitted to participate in PPO plan.

Affirmed.

Will, Senior District Judge, filed opinion concurring in the judgment.

Procedural Posture(s): On Appeal; Motion for Preliminary Injunction.

Attorneys and Law Firms

***1329** Douglas B. McFadden, McFadden, Borsari, Evans & Sill, Washington, D.C., for plaintiffs-appellants.

James W. Rankin, Kirkland & Ellis, Chicago, Ill., for defendants-appellees.

Before FLAUM and EASTERBROOK, Circuit Judges, and WILL, Senior District Judge. *

Opinion

EASTERBROOK, Circuit Judge.

The provision of health care financing services has become increasingly competitive. Hospitals and physicians (the providers of service) have begun to offer financing packages, much as automobile manufacturers sometimes finance their own products. In health care, where the need for service often depends on events beyond anyone's control, financing often is combined with insurance to spread the risks.

Sometimes the financing and insurance package is part of a new method of supplying the service; the health maintenance organization (HMO) is both a method of joining physicians in a firm and a method of financing their service by selling memberships for stated monthly prices. The physicians at HMOs are paid salaries rather than fees for each service they render. Sometimes the financing is independent of the method of supplying the service. Several hospitals in Indiana that use traditional organization (most physicians are independent contractors rather than employees), and pay each provider per service, also have begun to offer financing to patients.

One package is the preferred provider organization (PPO). In exchange for a ***1330** stated monthly payment, the hospital promises to pay the costs of patients who use particular providers. Patients who use providers other than the “preferred” ones must pay part or all of the fees themselves. These copayments are meant to induce patients to stick with the preferred providers—perhaps more often to request their physicians to stick with the preferred providers. [1] This may send extra business to these providers, who in exchange may agree to take less for each case. The assembler of the PPO plan

may pass the savings along to the purchasers of the coverage. A PPO plan specifies in advance the fee it will pay a provider for any given medical service.

The purchasers of the service are not necessarily the patients. Employers often supply health care coverage for employees, and they are intensely interested in reducing the price of any given level of care. These employers may shop among different plans assembled by different HMOs and hospitals. They also consider traditional insurance packages. Blue Cross and Blue Shield of Indiana (the Blues) offer a service benefit plan that has attracted a substantial following from both employers and individual purchasers of insurance. Providers sign up as members of the Blues' plan, and they promise to accept as payment the "usual, customary, and reasonable" fee for a service as the Blues determine that fee to be, case by case. Other sellers of insurance agree to pay stated amounts per type of service rendered or to pay a stated percentage of the provider's bill. These plans have attracted fewer subscribers. Some large employers simply hire insurance companies to administer the employers' own plans; the administrator receives the bills, the employer determines what it will pay, and the administrator sends the money on to the providers. Administered self-insurance has been growing at the expense of other plans.

Patients and employers must choose among these plans. Once they have chosen a plan, they may have little control over their care. Choosing a PPO plan or HMO may lock a person into a particular provider. On the other hand, the choice among plans is relatively free in advance, and patients may shop among plans that are compatible with their needs and with their physicians' limitations (each physician will have privileges at a subset of local hospitals). This case is about the choice among financing packages.

I

The plaintiffs in this case are 80 acute-care hospitals (the Hospitals). All 80 provide care on a fee for service basis, and all 80 receive payments from many insurance plans and administered self-insurance plans as well as from patients. Some of the 80 also offer PPO plans; others are preparing to do so. Forty of the 80 plaintiffs have appealed.

The Blues have been losing market share in Indiana for some years. In 1980 the Blues insured almost two million of Indiana's 5.5 million population. By 1984 they insured only about 1.45 million people. This is still a large share; at some of the Hospitals more than 80% of all patients are covered by the Blues, and throughout Indiana about 50% of all hospitals' revenues come from payments made by the Blues. This may be a misleading figure because it includes payments the Blues made as administrators of self-insurance plans and of Indiana's Medicare plan. The Blues say that they are much smaller—they insure only about 27% of all patients in Indiana and distributed in 1982 only about $450 million in Indiana on behalf of privately-insured patients, while Indiana's hospitals received ***1331** some $2.2 billion from all sources. By all accounts the Blues are large in relation to the next-largest private supplier of health insurance in Indiana, which underwrites about 3% of all private insurance in the state. Just how "large" the Blues are turns out not to matter, so we do not pursue the question.

All agree that however large the Blues may be, they are losing business. Concerned about this, the Blues decided to offer a PPO of their own, in addition to their traditional service benefit plans. The Blues also decided to merge, eliminating the longstanding practice of one plan's underwriting hospitals' services and another's underwriting physicians' services. The Blues asked for bids from all acute-care hospitals in Indiana and invited each to bid a percentage discount from its regular fees. That PPO plan and merger precipitated this case. The hospitals that offer PPO plans saw the Blues' decision as a threat to their success. All hospitals saw a PPO plan as a threat to revenues—those who participated in the plan might collect less per service rendered, and those outside the plan might lose volume.

Ninety-one of Indiana's 115 acute-care hospitals submitted bids, and the Blues signed up 61 of the 91. Forty-two of the 80 plaintiffs are among the 61. Eleven plaintiffs did not bid, and 27 bid but were not selected. All 80 remain eligible to participate in the regular service benefit plan offered by the Blues, which is the Blues' most popular product. All hospitals in Indiana also may provide services to patients covered by the Blues' PPO, but the Blues will reimburse only 75% of the hospitals' fees; the patients must pay the rest. The Blues will reimburse 100% of the agreed charges when insureds use hospitals within the PPO.

The Blues wanted to put their PPO into effect early in 1985. The Hospitals began this suit on November 14, 1984, seeking injunctive relief against the Blues' proposed PPO under sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2, and provisions of Indiana law.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

The district court set the case for a hearing on the Hospitals' request for a preliminary injunction. The court told the Hospitals they could present as much evidence as they wanted, and the hearing lasted 11 days in February 1985. More than 30 witnesses testified; more than 400 exhibits were introduced. On March 1, 1985, the district court denied the request for a preliminary injunction. The Blues' PPO immediately went into effect. The court later entered a partial final judgment disposing of the Hospitals' claims under state law, while reserving their antitrust claims; it issued a certificate under Fed.R.Civ.P. 54(b) permitting immediate appeal of the state law issues. We therefore have before us the denial of preliminary relief under the Sherman Act and the final judgment under state law.

The district court made extensive findings of fact. 603 F.Supp. 1077 (S.D.Ind.1985). The most important of these concern the Hospitals' claim that the Blues have (and abused) "market power," the ability to raise price significantly higher than the competitive level by restricting output. See *NCAA v. University of Oklahoma,* 468 U.S. 85, 104 S.Ct. 2948, 2965–67 & n. 38, 82 L.Ed.2d 70 (1984); *United States v. E.I. du Pont de Nemours & Co.,* 351 U.S. 377, 391, 76 S.Ct. 994, 1005, 100 L.Ed. 1264 (1956); William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases,* 94 Harv.L.Rev. 937 (1981). The court found that the Blues do not have the power to restrict output in the market or to raise price because they furnish a fungible product that other people can and do supply easily.

The court treated the product as "health care financing." The Blues, other insurance companies, hospitals offering PPOs, HMOs, and self-insuring employers all offer methods of financing health care. Employers and individual prospective patients easily may switch from one financing package to another; nothing binds an employer or patient to one plan. To put it differently, even though everyone wants medical insurance, and the demand for this service ***1332** as a whole may be inelastic (meaning that purchases fall less than 1% in response to a 1% increase in price, which makes the increase profitable), when customers are not tied to particular sellers each seller may perceive the demand as highly elastic (meaning that customers will quickly switch if any one supplier raises price, which makes the increase unprofitable). The court concluded: "Consumers are extremely price sensitive and will readily switch on the basis of price from one company or form of financing to another. Consequently, no competitor ... has the power to control prices...." Finding 8, 603 F.Supp. at 1080.

The market in health care financing is competitive, the court concluded, not only because customers can switch readily but also because new suppliers can enter quickly and existing ones can expand their sales quickly. More than 1000 firms are licensed to sell health insurance in Indiana, and more than 500 sell this insurance currently. According to the district court, all can expand on a moment's notice. "Entry barriers into the market for health care financing are extremely low. All that is needed to compete in Indiana, for example, is sufficient capital to underwrite the policies and a license from the Indiana Insurance Commissioner." Finding 11, 603 F.Supp. at 1080. Of the 500 firms now selling insurance, many operate nationwide and have (or can attract) plenty of capital against which to write policies—if the price is right. The court listed "Prudential, Aetna, Metropolitan and Equitable, each of which [has] premium income and assets in the tens of billions and operates nationally." Finding 12, 603 F.Supp. at 1080. The court also observed that firms may elect self-insurance, and HMOs may expand, in response to an increase in the price of insurance.

Buyers' willingness to switch and sellers' ability to enter and expand rapidly, the district court concluded, means that "a firm's share of premium revenues reflects no more than its ability to compete successfully in meeting consumer demands." Finding 14, 603 F.Supp. at 1081. The Blues cannot exclude competitors, cannot raise prices without losing business quickly; the Blues' size therefore indicates only their success in offering the package of price and service that customers prefer, not any market power.

The district court also found that PPO plans "contain cost by promoting price competition among hospitals" (Finding 18, 603 F.Supp. at 1081) and that many of the large national insurers, as well as the larger hospitals in Indiana, are offering or planning to offer PPO plans. "By thus offering financing arrangements to consumers to pay for hospital services, these hospitals [offering PPOs] are vertically integrating into the health care financing market" (Finding 20, 603 F.Supp. 1082).

The PPO program will enable the Blues to offer lower premiums, the court found; it estimated the savings at 10–20% for 1985. Finding 32, 603 F.Supp. at 1083. These savings come from the increased utilization of hospital services made possible by the patients' incentives to use the selected providers, and from "utilization controls and

procedures ... intended to generate savings by eliminating needless in-patient admissions and unnecessary operations." Finding 39, 603 F.Supp. at 1084. Insurance creates "moral hazard." Once a person has insurance, he wants the best care regardless of cost—for someone else bears the cost. When, as happens often, the physician rather than the patient makes the important choices, the physician may be inclined to provide all the service for which insurance will pay, knowing that his patient will not resist this recommendation (at least not on account of expense). Yet if every physician supplies more or better care, price must rise, which patients as a group must pay in higher insurance bills. The "utilization controls" to which the district court referred are a method of counteracting moral hazard by limiting each insured's access to care. These limits may restore the appropriate level of care and save cost. Moving patients from one hospital to another also may save cost. It may be cheaper to operate one hospital at 95% ***1333** of capacity and another at 55%, rather than each at 75%; the less-used hospital can close a wing and reduce its staff.

In light of its conclusions on the benefits of PPOs, the district court thought that a preliminary injunction would injure rather than promote the public interest. "The public ... would forfeit the benefits of competition and the opportunity for decreased health care costs. Competition would be restrained in the health care financing market because Blue Cross/Blue Shield cannot offer its product to the public.... Competition would also be restrained in the hospital services market because hospitals would not have to compete against one another on the basis of price for Blue Cross/Blue Shield insureds. In addition, the public would lose the improved hospital utilization control which the PPO would sponsor." Finding 43, 603 F.Supp. at 1084. Because the Blues lack market power, too, the district court thought the Hospitals had no reasonable chance of success on the merits of their antitrust claims. With the public interest and the law coinciding, the court concluded, the Blues must prevail.

The court also made findings pertinent to the Hospitals' claim that the PPO violates state law. We postpone recitation of these to the discussion of state law, and we turn to the antitrust argument.

II

The Hospitals insist that the public interest is on their side and that they are likely to prevail on the merits. These are related considerations. See *Lawson Products, Inc. v. Avnet, Inc.,* 782 F.2d 1429, 1433–34 (7th Cir.1986); *American Hospital Supply Corp. v. Hospital Products Ltd.,* 780 F.2d 589, 593–94 (7th Cir.1986); *Roland Machinery Co. v. Dresser Industries, Inc.,* 749 F.2d 380, 387–88 (7th Cir.1984). The district court, when exercising its discretion in evaluating and weighing the factors of traditional injunction analysis, seeks to hold to a minimum the sum of two potential costs: the cost of denying an injunction if the plaintiff is ultimately determined to be entitled to relief, and the cost of granting an injunction if the defendant is ultimately determined to have violated no legal command.

These costs usually fall on the parties. They are also likely to be short term costs, so that a mistake is not catastrophic. In antitrust litigation, by contrast, third parties may feel substantial effects. This suit is between hospitals and an insurer, but the principal effect of the PPO plan is on the price patients pay for insurance. A mistaken grant of an injunction may elevate this price, harming the consumers that antitrust laws are designed to protect. If there is a mistake, it may last a long while. Antitrust cases are notoriously extended. Sometimes preliminary injunctions in antitrust cases condemn the proposed action, and the defendant abandons it rather than face the costs and uncertainties of lengthy litigation. The Third Circuit took judicial notice of this effect of preliminary injunctions in holding that targets of tender offers may not seek relief on antitrust grounds. *H.H. Robertson Co. v. Guardian Industries Corp.,* No. 85–3232 (3d Cir.1986).

As a rule a court need not dwell on the costs to consumers of mistaken injunctions, because plaintiffs have no reason to seek remedies that will injure the beneficiaries of the antitrust laws. The plaintiffs may be consumers themselves or may have interests identical to those of consumers. At other times, however, the plaintiff's interests do not coincide with those of consumers. For example, in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.,* 429 U.S. 477, 97 S.Ct. 690, 50 L.Ed.2d 701 (1977), the plaintiff operated bowling establishments in competition with the defendant Brunswick, which acquired additional establishments in violation of § 7 of the Clayton Act. The plaintiff suffered injury in fact because the price bowling establishments could charge to consumers fell after the acquisition; had Brunswick not acquired the lanes, they would have gone bankrupt and disappeared. Pueblo therefore had been injured as a result of a violation—but ***1334** not because the violation had raised prices to consumers. The Supreme Court held that Pueblo had not suffered "antitrust injury," which means injury from higher prices or lower

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

output, the principal vices proscribed by the antitrust laws. Whenever the plaintiff and consumers have divergent rather than congruent interests, there is a potential problem in finding "antitrust injury." If, as in *Brunswick* itself, the plaintiff and the defendant are competitors, the plaintiff gains from higher prices and loses from lower prices—just the opposite of the consumers' interest. When the plaintiff is a poor champion of consumers, a court must be especially careful not to grant relief that may undercut the proper functions of antitrust.

Brunswick was a suit for damages, but an injunction would have been even worse than damages. If a court had issued an injunction compelling Brunswick to divest the establishments, which would have gone bankrupt, prices would have risen to consumers' detriment. Because injunctions may injure consumers just as surely as damages may, the "antitrust injury" rule applies to requests for damages and injunctions alike. *Midwest Communications, Inc. v. Minnesota Twins, Inc.,* 779 F.2d 444, 452–53 (8th Cir.1985); *Schoenkopf v. Brown & Williamson Tobacco Corp.,* 637 F.2d 205 (3d Cir.1980).

The risk that consumers and plaintiffs may have divergent interests arises when, as in *Brunswick,* the plaintiff and the defendant are horizontal rivals. Then the plaintiff wants higher prices, consumers want lower prices. The books contain examples of firms that invoke the antitrust laws to obtain shelter from competition rather than to promote competition. One example from our court is *ECOS Electronics Corp. v. Underwriters Laboratories, Inc.,* 743 F.2d 498, 501 (7th Cir.1984), *cert. denied,* 469 U.S. 1210, 105 S.Ct. 1178, 84 L.Ed.2d 327 (1985). See William J. Baumol & Janusz A. Ordover, *Use of Antitrust to Subvert Competition,* 28 J.L. & Econ. 247 (1985), for further examples.

The equitable remedy of preliminary injunctions has always stressed the importance of ensuring that preliminary injunctions not injure the public at the same time as they assist the plaintiff. Given the risk that business rivals may seek to use antitrust to stifle rather than promote competition, district courts should pay particular attention to the public interest in such litigation. Thus in attempting to weigh the equities of granting or denying a preliminary injunction in the antitrust setting, the pro or anti-competitive effects on the market at large should be an important factor in the district court's analysis.

Some of the Hospitals offer PPO plans of their own. The district court found that Methodist Hospital has signed up more than 10,000 insureds in a PPO that includes seven hospitals and that Methodist Hospital has marketed this plan across the state (Finding 21, 603 F.Supp. at 1082). Many other plaintiff Hospitals "have developed or are developing" their own PPO plans (Finding 20, *ibid.*). Moreover, the district court also found that the public interest lies in the continuation of the Blues PPO, as we discussed above.

We start with a proposition established by *Brillhart v. Mutual Medical Insurance, Inc.,* 768 F.2d 196 (7th Cir.1985): the Blues are financial intermediaries, purchasing agents for the consumers of medical services. See also *Kartell v. Blue Shield of Massachusetts, Inc.,* 749 F.2d 922 (1st Cir.1984), *cert. denied,* 471 U.S. 1029, 105 S.Ct. 2049, 85 L.Ed.2d 322 (1985). The Blues, as financial intermediaries, may drive any bargains open to the consumers of services. The Rule of Reason rather than the *per se* rule supplies the standard of analysis.

The analysis of the adoption of the PPO plan must begin with an assessment of market power. Market power is a necessary ingredient in every case under the Rule of Reason. See *Polk Bros., Inc. v. Forest City Enterprises, Inc.,* 776 F.2d 185, 191 (7th Cir.1985) (collecting cases). Unless the defendants possess market power, it is unnecessary to ask whether their ***1335** conduct may be beneficial to consumers. Firms without power bear no burden of justification. The Hospitals say that the Blues have a large share of the market for medical insurance in Indiana, and that this establishes market power.

In many cases a firm's share of current sales does indicate power. Sales may reflect the ownership of the productive assets in the business. Market power comes from the ability to cut back the market's total output and so raise price; consumers bid more in competing against one another to obtain the smaller quantity available. When a firm (or group of firms) controls a significant percentage of the productive assets in the market, the remaining firms may not have the capacity to increase their sales quickly to make up for any reduction by the dominant firm or group of firms.

In other cases, however, a firm's share of current sales does not reflect an ability to reduce the total output in the market, and therefore it does not convey power over price. Other firms may be able, for example, to divert production into the market from outside. They may be able to convert other productive capacity to the product in question or import the product from

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

out of the area. If firms are able to enter, expand, or import sufficiently quickly, that may counteract a reduction in output by existing firms. And if current sales are not based on the ownership of productive assets—so that entrants do not need to build new plants or otherwise take a long time to supply consumers' wants—the existing firms may have no power at all to cut back the market's output. To put these points a little differently, the lower the barriers to entry, and the shorter the lags of new entry, the less power existing firms have. When the supply is highly elastic, existing market share does not signify power. *Will v. Comprehensive Accounting Corp.,* 776 F.2d 665, 672 n. 3 (7th Cir.1985); *United States v. Waste Management Inc.,* 743 F.2d 976 (2d Cir.1984).

The district court found that each of the factors suggesting that market share does not imply market power is present in the market for medical insurance. New firms may enter easily. Existing firms may expand their sales quickly; the district court pointed out that insurers need only a license and capital, and that firms such as Aetna and Prudential have both. There are no barriers to entry—other firms may duplicate the Blues' product at the same cost the Blues incur in furnishing their coverage. See George J. Stigler, *The Organization of Industry* 67–70 (1968) (defining barriers to entry as differentials in the long-term costs of production); cf. Harold Demsetz, *Barriers to Entry,* 72 Am.Econ.Rev. 47 (1982) (showing that not all barriers, as so defined, injure effective competition). The Blues and other nonprofits may have an edge because of the lower tax Indiana places on premiums paid to them, but this sort of advantage is not pertinent here. Other mutual insurance carriers (including Prudential) can get the same tax break. A PPO plan does not exploit the tax advantage as compared with any other plan the Blues could offer. The tax benefits may or may not be desirable as a matter of state policy, but this is no concern of antitrust law.

The Blues do not own any assets that block or delay entry. The insurance industry is not like the steel industry, in which a firm must take years to build a costly plant before having anything to sell. The "productive asset" of the insurance business is money, which may be supplied on a moment's notice, plus the ability to spread risk, which many firms possess and which has no geographic boundary. Cf. *Hood v. Tenneco Texas Life Insurance Co.,* 739 F.2d 1012, 1019 (5th Cir.1984) (insurance industry marked by ease of entry); *Alabama Association of Insurance Agents v. Board of Governors,* 533 F.2d 224, 250–51 (5th Cir.1976) (financial services in general are competitive because of the ease of moving money), modified, 558 F.2d 729 (1977), *cert. denied,* 435 U.S. 904, 98 S.Ct. 1448, 55 L.Ed.2d 494 (1978). The district court emphasized that every firm can expand its sales quickly if the price is right, that no ***1336** firm has captive customers, and that many firms want to serve this market. The conclusion that the Blues face vigorous and effective competition is not clearly erroneous. See also *National Bancard Corp. v. VISA U.S.A., Inc.,* 779 F.2d 592, 604–05 (11th Cir.1986) (defining a market of "all payment devices" on basis of a conclusion that one financial service is a ready substitute for another).

Still, the Hospitals say, the conclusion is legally irrelevant. Ease of entry and the absence of barriers do not matter if the defendant has a large market share. The Hospitals are wrong. Market share is just a way of estimating market power, which is the ultimate consideration. When there are better ways to estimate market power, the court should use them. See *Waste Management, supra.* Market share reflects current sales, but today's sales do not always indicate power over sales and price tomorrow. *United States v. General Dynamics Corp.,* 415 U.S. 486, 94 S.Ct. 1186, 39 L.Ed.2d 530 (1974), illustrates the point. The sellers of a large share of all current sales of coal in the midwest merged. The Court held, however, that share did not demonstrate power, because current deliveries of coal were largely committed under long term contracts. The pertinent competitive criterion was the ability to make future commitments of coal, and existing deliveries actually restricted the ability to make such commitments. The real "owners" of the coal currently being delivered were the recipients under the contracts, not the sellers. One of the firms in the merger had committed all of its economically-recoverable coal, and so its disappearance by merger did not remove from the market any competitive force that could be preserved by enjoining the merger. The Court concluded that because market shares did not reflect tomorrow's ability to compete, they did not supply a reason to forbid the merger.

Other cases, many from this circuit, have said that market share is simply an indication of power and possesses no other significance. *Will v. Comprehensive Accounting Corp., supra,* 776 F.2d at 672 n. 3; *United Airlines, Inc. v. CAB,* 766 F.2d 1107, 1115 (7th Cir.1985); *Kaiser Aluminum & Chemical Corp. v. FTC,* 652 F.2d 1324, 1341 (7th Cir.1981); *Juneau Square Corp. v. First Wisconsin National Bank of Milwaukee,* 624 F.2d 798, 813 (7th Cir.), *cert. denied,* 449 U.S. 1013, 101 S.Ct. 571, 66 L.Ed.2d 472 (1980). *Waste Management, supra,* and *Broadway Delivery Corp. v. United Parcel Service of America, Inc.,* 651 F.2d 122 (2d Cir.1981), *cert. denied,* 454 U.S. 968, 102 S.Ct. 512, 70 L.Ed.2d 384 (1982), express the same point in the Second Circuit, and almost every other

circuit has a similar holding. Cf. *du Pont, supra* (sole maker of cellophane lacks market power because of competition from other flexible wrappings).

The inquiry in each case is the ability to control output and prices, an ability that depends largely on the ability of other firms to increase their own output in response to a contraction by the defendants. Indeed it is usually best to derive market share *from* ability to exclude other sources of supply. This is the method the Department of Justice adopted in its Merger Guidelines. Cf. Landes & Posner, *supra;* George J. Stigler & Robert A. Sherwin, *The Extent of the Market,* 28 J.L. & Econ. 555 (1985). If the definition of the market builds in a conclusion that there are no significant additional sources of supply and no substitutes from the consumers' perspective, then the market share indicates power over price. But a calculation of the Blues' share of current coverage in Indiana does not capture the possibility of new entry and expanded sales by rivals, and this is why the district court properly held that the geographic market "is regional, if not national" (Finding 9, 603 F.Supp. 1080). This larger market may not seem useful from the perspective of consumers in Indiana, who must obtain their insurance from firms offering it there. It is highly pertinent, however, from the perspective of the Blues' rivals and potential rivals, and therefore from the perspective of constraints on the Blues' ability to raise price. ***1337** The Blues' rivals, whose mobility is not restricted, protect consumers, whose mobility is restricted.

The district court therefore did not commit a legal error or make a clear error in finding the facts. So far as the record stands, the Blues lack market power and are therefore entitled to adopt a PPO plan without further scrutiny under the Sherman Act.

The merger of the two plans does not alter the analysis or independently violate the antitrust laws. The district court found that the plans "have for more than thirty years acted as one company" (Finding 2, 603 F.Supp. at 1079). It is therefore appropriate to treat them as if they had been one corporation all along. A merger, like a cartel, may "deprive[ ] the marketplace of the independent centers of decisionmaking that competition assumes and demands," and the joinder of previously independent firms "suddenly increases the economic power moving in one particular direction." *Copperweld Corp. v. Independence Tube Corp.,* 467 U.S. 752, 104 S.Ct. 2731, 2741, 81 L.Ed.2d 628 (1984). But the two Blue plans offered complementary products (insurance against hospitals' costs and insurance against physicians' costs); they did not compete by offering substitute products. Their merger did not change the conditions of competition in the market. The district court was entitled to treat them as a single firm under *Copperweld.* 7 Phillip E. Areeda, *Antitrust Law* ¶ 1464f (1986). Even if the two plans' formal separation makes treatment under *Copperweld* inappropriate, the merger of firms that were jointly controlled does not call for close scrutiny. *United States v. Citizens & Southern National Bank,* 422 U.S. 86, 95 S.Ct. 2099, 45 L.Ed.2d 41 (1975).

III

The Hospitals try to avoid this conclusion by urging that § 2 of the Sherman Act imposes an additional test—that the Blues act without anticompetitive intent. Relying on *United States v. Aluminum Co. of America,* 148 F.2d 416 (2d Cir.1945), the Hospitals insist that any firm with a large market share has an obligation not to augment that share at the expense of rivals and may not drive hard bargains.

Although the district court did not make findings concerning the Blues' intent, the Hospitals say that the record reeks of bad intent. The Blues evidently wanted to drive down the price they paid to the providers, which entails bad intent; more, the Blues engaged in calculated planning to preserve or enlarge their market share. The Hospitals quote from a report that a consulting firm rendered to the Blues in 1981: "The market is mature with little growth opportunity left. The [Blues] dominate the marketplace and recently have been losing shares.... The competition will move to increase market share at the [Blues'] expense. Market strategy for this market might be to segment the market." In January 1983 the Blues circulated an internal report stating in part:

> *The Proposition:* That [the Blues] use its market position and its control over substantial sums of health care dollars to negotiate lower fees for provider services ... Blue Cross plans that enjoy major discounts in their hospital reimbursement contracts do have considerable advantage over competitors. It appears that these discount arrangements reinforce what is a common perception among both political leaders and businessmen. Which is that our control of so many health care dollars should put us in a position to negotiate lower prices for provider services....
>
> *The Recommended Response:* [The Blues are] in a unique position to serve as a broker between what might appear

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

to be the conflicting interests of financially threatened providers and cost conscious group purchasers.... We also control an overwhelming share of the marketplace in key areas.... In short, the time seems right for an aggressive new stance in the financing of health care benefits.... The growth of competitive forces poses a grave threat, and will grow worse without counteraction.

***1338** *Res ipsa loquitur,* the Hospitals say. If the Blues lack market power, how come their own planning documents talk this way? The Hospitals say that the district court should have inferred power from intent, and that given this intent to prevent competition the district court also was required to enjoin the adoption of the PPO.

We assume without deciding that a court sometimes may infer market power from a sufficiently clear demonstration that a firm believes that it possesses power. Even so, an argument about evil intent in antitrust requires us to ask: "intent to do what?" The Hospitals seem to think that intent to get the best price is a bad intent. They cite *Mandeville Island Farms v. American Crystal Sugar Co.,* 334 U.S. 219, 68 S.Ct. 996, 92 L.Ed. 1328 (1948), to show that a monopsonistic depression of price is as bad as a monopolistic increase in price. True enough, see *United States v. Capitol Service, Inc.,* 756 F.2d 502 (7th Cir.), *cert. denied,* 474 U.S. 945, 106 S.Ct. 311, 88 L.Ed.2d 288 (1985), but *Mandeville* was a conspiracy to depress prices, and price-fixing cartels are unlawful independent of their efficacy. See *Arizona v. Maricopa County Medical Society,* 457 U.S. 332, 102 S.Ct. 2466, 73 L.Ed.2d 48 (1982). The Blues are a single firm, and the acts of single firms are judged by a different standard under § 2.

Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals—sometimes fatally. The firm that slashes costs the most captures the greatest sales and inflicts the greatest injury. The deeper the injury to rivals, the greater the potential benefit. These injuries to rivals are byproducts of vigorous competition, and the antitrust laws are not balm for rivals' wounds. The antitrust laws are for the benefit of competition, not competitors. *Brunswick, supra,* 429 U.S. at 488, 97 S.Ct. at 697, quoting from *Brown Shoe Co. v. United States,* 370 U.S. 294, 320, 82 S.Ct. 1502, 1521, 8 L.Ed.2d 510 (1962); *Brunswick Corp. v. Riegel Textile Corp.,* 752 F.2d 261, 266 (7th Cir.1984), *cert. denied,* 472 U.S. 1018, 105 S.Ct. 3480, 87 L.Ed.2d 615 (1985); *ECOS Electronics, supra.* The antitrust laws protect efficient production for the benefit of consumers. *Reiter v. Sonotone Corp.,* 442 U.S. 330, 342, 99 S.Ct. 2326, 2332, 60 L.Ed.2d 931 (1979); *NCAA, supra,* 104 S.Ct. at 2966 n. 49.

Sometimes injury to rival firms can be a presursor to injury to consumers; after knocking rivals out of the market, a firm may curtail output and raise price. Section 2 may be used to prevent this conduct. Yet it must be used with the greatest caution. Action that injures rivals *may* ultimately injure consumers, but it is also perfectly consistent with competition, and to deter aggressive conduct is to deter competition. Thus the plaintiff faces a stiff burden in any § 2 litigation. "It is not enough that a single firm appears to 'restrain trade' unreasonably, for even a vigorous competitor may leave that impression. For instance, an efficient firm may capture unsatisfied customers from an inefficient rival, whose own ability to compete may suffer as a result. This is the rule of the marketplace and is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster. In part because it is sometimes difficult to distinguish robust competition from conduct with long-run anti-competitive effects, Congress authorized Sherman Act scrutiny of single firms only when they pose a danger of monopolization. Judging unilateral conduct in this manner reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur." *Copperweld, supra,* 104 S.Ct. at 2740.

So "intent to harm rivals" is not a useful standard in antitrust. See also *Barry Wright Corp. v. ITT Grinnell Corp.,* 724 F.2d 227, 232 (1st Cir.1983): " '[I]ntent to harm' [rivals] without more offers too vague a standard in a world where executives may think no further than 'Let's get more business,' and long-term effects on consumers depend in large measure on competitors' responses." Neither is "intent to do more business," which amounts ***1339** to the same thing. Vigorous competitors intend to harm rivals, to do all the business if they can. To penalize this intent is to penalize competition. See also 7 Areeda, *Antitrust, supra* at ¶ 1506.

What of other "intents"? One intent reflected in the Blues' documents is to buy medical care for less. Again, though, this is just another description for hard bargaining. Even a monopolist may bargain hard. See *MCI Communications Corp. v. AT&T,* 708 F.2d 1081 (7th Cir.), *cert. denied,* 464 U.S. 891, 104 S.Ct. 234, 78 L.Ed.2d 226 (1983), which holds that a dominant firm may slash prices to marginal cost in an effort to capture patronage. Other courts have held that monopolists may raise prices to customers, may charge what the traffic will bear, so long as they came by their market power lawfully.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

E.g., *Berkey Photo, Inc. v. Eastman Kodak Co.,* 603 F.2d 263, 296–98 (2d Cir.1979), *cert. denied,* 444 U.S. 1093, 100 S.Ct. 1061, 62 L.Ed.2d 783 (1980). Even the largest firms may engage in hard competition, knowing that this will enlarge their market shares. E.g., *Foremost Pro Color, Inc. v. Eastman Kodak Co.,* 703 F.2d 534 (9th Cir.1983), *cert. denied,* 465 U.S. 1038, 104 S.Ct. 1315, 79 L.Ed.2d 712 (1984); *Telex Corp. v. IBM Corp.,* 510 F.2d 894 (10th Cir.), *cert. dismissed,* 423 U.S. 802, 96 S.Ct. 8, 46 L.Ed.2d 244 (1975). *Alcoa,* which seemed to suggest the opposite, has been limited by the Second Circuit in *Berkey, supra,* 603 F.2d at 272–75, and does not now assist the Hospitals.

Bad intent in antitrust law must mean something other than the intent reflected in the Blues' memos and the consultant's report. We need not decide just what it means—if it means anything. The Supreme Court hinted in *Aspen Skiing Co. v. Aspen Highlands Skiiing Corp.,* 472 U.S. 585, 105 S.Ct. 2847, 2857–59, 86 L.Ed.2d 467 (1985), that intent "is merely relevant" to the question whether the large firm seeks to exclude competition on a "basis other than efficiency". The focus must be on the objective basis, not the mental state. The First Circuit held in *Grinnell* that "intent" is a useless and confusing term best discarded in favor of analysis of objective indicators. See also *Deauville Corp. v. Federated Department Stores, Inc.,* 756 F.2d 1183 (5th Cir.1985). The Second Circuit in *Berkey* reformulated intent to ask whether the large firm intended to "transfer" power from one market to another or to do something smaller firms could not do. Neither approach would assist the Hospitals—the Blues are not trying to get a monopoly in a second market, and the record establishes that "small" firms, including some of the plaintiffs, can offer PPO plans. More than a dozen PPO plans are operating or organizing in Indiana. Still another approach is to ask whether the defendant intends to (and can) raise its rivals' costs of doing business. See *Litton Systems, Inc. v. AT&T,* 700 F.2d 785 (2d Cir.1983), *cert. denied,* 464 U.S. 1073, 104 S.Ct. 984, 79 L.Ed.2d 220 (1984). See also 3 Phillip Areeda & Donald F. Turner, *Antitrust Law* ¶ 626 (1978); Steven C. Salop & David T. Scheffman, *Raising Rivals' Costs,* 73 Am.Econ.Rev. 267 (1983); Richard S. Markovits, *The Limits to Simplifying Antitrust,* 63 Tex.L.Rev. 41, 58–60 (1984). When a firm finds a way to confront its rivals with higher costs, it may raise its own prices to consumers without drawing increased output from them. See *Aspen Skiing, supra.* Exclusive dealing arrangements and boycotts sometimes may raise rivals' costs. Cf. *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.,* 472 U.S. 284, 105 S.Ct. 2613, 86 L.Ed.2d 202 (1985). But the Blues have not insisted that hospitals in the Blues' PPO refrain from joining other PPOs, so rivals have access to hospitals on the same basis as the Blues. Some hospitals participate in more than three different PPO plans. Finding 34, 603 F.Supp. at 1683.

The Hospitals urge on us a version of an argument that the Blues' PPO will raise rivals' costs. The argument, which the parties call the "cost-shifting" argument, starts from the premise that hospitals raise just enough revenue to break even each year. The hospitals offer discounts to the Blues in order to participate in their PPO. ***1340** They therefore receive less revenue from patients covered by the PPO. To break even they must obtain more revenue from other patients. This means they must "shift" to their other patients their costs of operation. When the hospitals raise their prices to other insurance plans (including the hospitals' own PPO plans), these plans will be unable to compete with the Blues. The Blues' PPO will have raised its rivals' costs, in violation of § 2.

The district court did not address this argument explicitly. It apparently treated the cost-shifting argument as an attack on price discrimination, to which it correctly replied that discrimination is not forbidden. Finding 46, 603 F.Supp. at 1084. This does not dispose of a claim that PPOs raise rivals' costs. Still, we can construct from the findings an answer sufficient for the time being. An argument that the Blues are shifting costs to rivals must start from the proposition that the Blues have market power. Why else would hospitals give the Blues a price break that injures rivals? The district court found that the Blues lack power, a finding we have held is not clearly erroneous. The cost-shifting argument also assumes that the price charged to the patients in the Blues' PPO plan is below the appropriate measure of cost; the Hospitals contend that they must raise prices elsewhere to subsidize these patients. But the district court found that the PPO genuinely saves on the costs of care, and this too is not clearly erroneous. If the discounts given on patients covered by the PPO are justified by reductions in cost, there is nothing to "shift" to other patients.

We do not imply by this discussion that the Blues must demonstrate that the prices charged to the PPO patients are "cost-justified." That has been a notorious quagmire in litigation under the Robinson-Patman Amendments to § 2 of the Clayton Act, 15 U.S.C. § 13. There is certainly no burden of justification in the absence of market power—no rational hospital sells below cost to a buyer without market power (the Hospitals do not say that they are themselves engaged in predatory pricing). It is also hard to see why, if

the Hospitals can raise their prices to other buyers of their services, they do not do so whether or not they join the Blues' PPO plan. We have held that large firms may drive hard bargains, and this does not imply that district courts should become little versions of the Office of Price Administration and assess the "cost-justification" for prices charged to these large customers. The Robinson-Patman amendments sometimes require this investigation, but they are limited to price discrimination affecting "commodities of like grade and quality" (15 U.S.C. § 13(a)). Medical services are not "commodities." The Supreme Court has repeatedly stated that the control of price discrimination poses substantial risks to competition, which often works through "discriminatory" chiseling down of prices. E.g., *Great Atlantic & Pacific Tea Co. v. FTC,* 440 U.S. 69, 80–81, 99 S.Ct. 925, 933, 59 L.Ed.2d 153 (1979); *United States v. United States Gypsum Co.,* 438 U.S. 422, 450–59, 98 S.Ct. 2864, 2880–84, 57 L.Ed.2d 854 (1978); *Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, 133, 98 S.Ct. 2207, 2217, 57 L.Ed.2d 91 (1978). We have entered this bog only because here the district court *did* find that there were justifications for the lower price, and this is enough to demonstrate that it did not abuse its discretion in declining to issue a preliminary injunction against the PPO plan.

IV

The Blues say that once we have agreed with the district court that the Hospitals are unlikely to prevail, we should bring the litigation to an immediate conclusion. Antitrust litigation may be exceptionally expensive, and we could avoid further expense by directing the district court to grant judgment to the Blues. The Blues offer two arguments.

First, they say, the Hospitals had every opportunity to offer evidence at the hearing on their request for a preliminary injunction. They have nothing more to show, ***1341** and so there is no point in further proceedings. It may be that the district judge will come to this conclusion, but we do not direct him to do so.

The district court is best equipped to determine what additional evidence the Hospitals have to offer and how it might affect the findings of fact. The Hospitals may have an uphill battle to show the district judge evidence that calls his findings into question, but we do not think that we should prohibit the district judge from allowing the Hospitals that opportunity. Evidence on cost-shifting, for example, was poorly developed. Did hospitals that joined the Blues' PPO raise prices to their non-PPO patients (by more than hospitals outside the Blues' PPO did)? Have the hospitals that joined the Blues' PPO lost patients as a result? Did anyone else? Did other insurers have to raise their prices (which cost-shifting implies)? Questions of this sort, which now lack answers, will be important if the district judge should be converted by further evidence to the view that the Blues have market power.

Second, the Blues argue that their PPO is protected by the "state action" doctrine of *Parker v. Brown,* 317 U.S. 341, 63 S.Ct. 307, 87 L.Ed. 315 (1943). That doctrine excludes from the antitrust laws closely supervised private conduct that implements clearly articulated state policies. See *Southern Motor Carriers Rate Conference, Inc. v. United States,* 471 U.S. 48, 105 S.Ct. 1721, 1727, 1730, 85 L.Ed.2d 36 (1985). See also *Cantor v. Detroit Edison Co.,* 428 U.S. 579, 96 S.Ct. 3110, 49 L.Ed.2d 1141 (1976). Indiana has a policy favoring PPOs, the Blues say, which meets this standard. This appears to say that (a) Indiana favors PPOs over other methods of organization, (b) the Blues' PPO is the favored kind, and (c) the state supervises the PPO contracts with hospitals as well as the insurance contracts with the purchasers of service. The district court did not discuss this contention, and it did not make the findings about the nature of Indiana's law and the Blues' PPO that would be necessary to resolve it. We therefore do not consider this argument further. The district judge should do so if he deems resolution of the question necessary.

V

Although more proceedings may be in store on the Hospitals' antitrust arguments, the district court entered a final judgment rejecting their arguments under state law. The principal law in question, Ind.Code § 27–8–11–3, became effective on December 31, 1984. Subsection (a) allows insurers to establish PPO plans. The other pertinent provisions state:

> (b) Before entering into any agreement ... an insurer shall establish terms and conditions that must be met by providers wishing to enter into an agreement with the insurer.... These terms and conditions may not discriminate unreasonably against or among providers.... [N]either differences in prices among hospitals or other institutional providers produced by a process of individual negotiation nor price differences among other providers in different

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

geographical areas or different specialties constitutes unreasonable discrimination.

(c) No hospital, physician, pharmacist, or other provider ... willing to meet the terms and conditions offered to it by an insurer may be denied the right to enter into an agreement....

The Hospitals' strongest argument is that the Blues have discriminated unreasonably among providers, contrary to the prohibition of subsection (b). Before assessing the legal contentions, however, we review the procedures by which the parties negotiated the PPO contracts.

The Blues announced the terms of their plan and invited all 115 general acute care hospitals to submit bids, expressed as percentages of their existing prices. Findings 26 and 27, 603 F.Supp. at 1082–83. In response to comments from the hospitals, the Blues revised some of the terms of the proffered contracts and asked for renewed bids. Findings 35 and 36, 603 F.Supp. at 1083–84. The terms included utilization controls and other changes designed to reduce ***1342** the cost of service. There followed negotiating sessions with each of the 91 hospitals that submitted a bid. Although the district court did not make findings on this question, the parties agree that the Blues gave each hospital little if any information about the bids made by other hospitals in the area and suggested that each hospital bid a greater discount. The Blues never proposed a particular discount or said what discount would be sufficient; they simply waited for hospitals to bid less.

From among the hospitals that got this far, the Blues selected those that bid the lowest prices and were "conveniently located" for the Blues' insureds. Finding 30, 603 F.Supp. at 1083. Although the decision to exclude a hospital was almost always based on price, in two cases geography played a role. Again this is a subject on which the district court was silent but the parties largely agree. The Blues excluded Winona Memorial Hospital, despite its acceptable price, because another hospital in the same city was better located. The Blues excluded St. Joseph's Hospital of Ft. Wayne for two reasons —they deemed its bid of 80% of prior prices a "low-ball" that was sure to be increased, and they concluded that it was not as conveniently located as Parkview Hospital in the same city.

The Blues defend this geographic selectivity by relying on the provision in § 3(b) stating that "price differences among other providers in different geographical areas or different specialties" do not constitute "unreasonable discrimination." The statute, say the Blues, "is not a model of drafting clarity" but is "plainly [designed] to permit the insurer to select its PPO hospitals based, not only on price, but also on the geographic accessibility needs of its insureds." This is not persuasive.

The clause in question states an exception to the rule of § 3(b) that plans not "unreasonably discriminate" among hospitals. The exception covers "differences in prices among *hospitals or other institutional providers* produced by a process of individual negotiation" and "price differences among *other providers* in different geographical areas or different specialties". Read as a whole, this means that specified differences in price are not "unreasonable discrimination." The specified differences are: for hospitals, differences individually negotiated; for other providers (such as physicians), differences by location or specialty. There is no linguistic support for reading this clause to allow geographic price schedules for "hospitals or other institutional providers", let alone to allow geographic distinctions unrelated to price. Perhaps the legislative history of the statute might supply such a reason, but Indiana does not publish the legislative history of its laws, and the parties have not provided us with any other access to that history.

The reading we have given the language makes more than linguistic sense. Hospitals do so much business that it is (relatively) easy to negotiate individually with them about price. There are thousands of other providers, however, and individual price negotiations might be prohibitively difficult. The statute therefore authorizes the insurer to promulgate price schedules and allows these to make distinctions on the basis of geography (medical care may be less costly in rural areas than in cities) and specialty (a specialist in a given procedure may charge more than a general practitioner, reflecting the specialist's greater expertise and the lower risk of error). The language of the statute thus serves useful functions without authorizing non-price discrimination among hospitals on the basis of geography.

Still, this does not carry the day for the Hospitals. That the Blues' reliance on the price proviso is unwarranted simply returns us to the general principle: A PPO plan's terms must not "unreasonably discriminate" among hospitals. The Hospitals argue as if all distinctions on the basis of geography are "unreasonable," but they do not say why. In some cases the savings in cost may depend on the ability to direct patients to a particular hospital, the better to use its facilities fully. This may require reducing the number of hospitals in the ***1343** PPO plan in a given city. The Hospitals reply by invoking §

3(c), which says that no provider "willing to meet the terms and conditions offered to it ... may be denied the right to enter into an agreement". These "terms," the Hospitals say, are the ones written in the contract, not the criteria the Blues use to choose among bidding hospitals, and therefore § 3(c) forbids geographic distinctions. The Blues rejoin that § 3(c) cannot be given so broad a reading, for then the statute would also exclude all distinctions on the basis of price, which the legislature plainly has authorized.

We need not decide whose reading of § 3(c) is correct. The Hospitals were allowed to put on all the evidence they desired, and they showed only two instances of the use of geography. We need not determine whether § 3 *allows* every use of geography; it is enough to determine whether the Hospitals have demonstrated a legal flaw in these two uses. They have not. Winona Memorial Hospital is not a plaintiff. The plaintiff Hospitals may not urge a wrong done to a stranger to the litigation as a ground of relief for themselves. *Secretary of State of Maryland v. Joseph H. Munson Co.,* 467 U.S. 947, 104 S.Ct. 2839, 2846–48, 81 L.Ed.2d 786 (1984). St. Joseph's Hospital, a plaintiff, was excluded for two reasons: price and location. It has not established that but for the consideration of location it would have been given a PPO contract. The district court did not make findings of fact on the question, but it does not appear to be a seriously disputed issue. The Hospitals insist that the Blues are not entitled to refer to price in deciding which hospitals to include in the program, but if the Blues may use price at all they may determine which prices quoted to them are bona fide.

The Hospitals do not disagree with the Blues' contention that they determined St. Joseph's bid to be a low-ball quote, too low to be justified by its costs (on which the Blues had data) and therefore too low to be sustained. One witness testified without contradiction that St. Joseph's bid was well below that of any other hospital, and another testified that the Blues feared that "at the first opportune time [St. Joseph's] would be asking for an unreasonably high increase". Unless a court must evaluate the propriety of every pricing decision made by an insurance company—and there is no support for that in § 3—this testimony is enough to show that location was not dispositive in St. Joseph's case. Consequently, there is support in the record for the district court's conclusion that the Hospitals have not established a violation of § 3.

This conclusion holds, however, only if price is a legitimate ground for excluding a hospital from a PPO. The Hospitals say that it is not, relying on § 3(c). On their reading of the statute, only a Hospital's failure to meet the terms and conditions of the PPO plan as a whole may be a reason for exclusion. They submit that price may be a "term" only if the same price is offered to all hospitals by contract. This cannot be right. It would nullify the explicit authorization in § 3(b) for the use of individually-negotiated prices. More, it would make hash of the idea of a PPO. A "preferred" provider is one to which the insurer seeks to funnel business, partly in the search for operating efficiencies, partly in the search for lower prices. If high-price bidders had to be designated as "preferred" providers, it would be difficult to contain costs. An insurer could not cut out of its system the high-price providers, and there would be no reason for hospitals to bid against one another for inclusion. The requirement that hospitals bid in order to get the plan's business is the principal source of the incentive to cut costs, and the prospect of getting more business by becoming a "preferred" provider is the principal benefit to a hospital. We do not think that Indiana took back in § 3(c) the authorization to establish PPO plans granted by §§ 3(a) and (b).

The Hospitals' last argument under § 3 is that the Blues may not take advantage of the price proviso of § 3(b) because they did not engage in "individual negotiation", as the statute requires. Officials ***1344** of the Blues met separately with officials of each hospital, but the hospitals did all the talking about price. The Hospitals say that "negotiation" means "discussion whereby parties mutually interested seek to resolve differences with the purpose of arriving at agreement." *Barrick Realty Co. v. Bogan,* 422 N.E.2d 1306, 1308 (Ind.App.1981). A one-sided meeting in which the hospital talks price and the Blues listen is not negotiation under this definition, the Hospitals say. They insist that the Blues had to propose acceptable prices or at least reveal what other hospitals were bidding, so that each could see the competition.

The problem with this position is that few bargainers reveal their reservation prices. If the Blues had said: "A discount of 10% is enough to ensure your participation in the program," few hospitals would have offered discounts of 12%. If the Blues had said: "Your competition has bid discounts of 8% and 7%," few hospitals would have offered discounts steeper than 9%. See *United States v. United States Gypsum Co., supra,* in which the Supreme Court concluded that the exchange of price information among rivals would tend to stabilize or increase prices. It is unlikely that Indiana meant to require a form of disclosure that would have this effect. Often the most effective negotiation, from the buyer's

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

perspective, is to sit back and say: "Do more," without saying how much more. The seller's uncertainty induces it to bid down to marginal cost. This is hard bargaining, and it is negotiation notwithstanding its tendency to drive down prices. Competition has that effect.

A rule requiring a buyer to tell the seller how low is low enough would reduce the power of competition. See *Great Atlantic & Pacific Tea Co. v. FTC, supra,* 440 U.S. at 80–81, 99 S.Ct. at 933. In *A&P* the Supreme Court held that a buyer may obtain a discriminatorily low price from a seller without informing the seller that a higher price would have fetched the business anyway. It held that a requirement to tell the seller how low is low enough would be antithetical to the purposes of the antitrust laws. The price one will accept is usually a negotiator's closely guarded secret. See *Federal Open Market Committee v. Merrill,* 443 U.S. 340, 361–64, 99 S.Ct. 2800, 2812–14, 61 L.Ed.2d 587 (1978). Perhaps an insurer could satisfy the Hospitals' demand for price quotes by naming an unreasonable price, hoping to nudge each hospital closer to the one it really had in mind, but the statute does not require the observance of useless forms. Cf. *Trans Alaska Pipeline Rate Cases,* 436 U.S. 631, 653, 98 S.Ct. 2053, 2065, 56 L.Ed.2d 591 (1978).

"Individual negotiation" therefore means a process of dickering one hospital at a time, as opposed to announcing a price schedule for groups of hospitals. It contrasts with the geographic price schedules § 3(b) allows for "other providers" and specialists. The statute does not require the courts to supervise the handling of each individual negotiation. This conclusion disposes of the Hospitals' arguments under § 3. The Blues did not violate the statute by conducting one-sided negotiations or by taking price into account.

Although we reject the Hospitals' claims of discrimination based on price and location, our decision does not rest on any final construction of the statute; we have held only that no plaintiff hospital established that locational considerations were the cause of its exclusion from the Blues' PPO plan. Because we have been able to decide this case without finally settling on a construction of § 3, we deny the Hospitals' motion that we certify this question to the Supreme Court of Indiana.

VI

The Hospitals rely on a second statute, Ind.Code § 34–4–12.6–2(a). This part of the Peer Review Act provides that all proceedings of physicians reviewing the work of other physicians shall be confidential. The PPO contracts, the Hospitals tell us, violate this statute because they grant the Blues access to each hospital's records and statistical information "without restriction." The district court gave two replies: ***1345** first that the PPO Act preempts conflicting laws, see Ind.Code § 27–8–11–2; second that the PPO agreement "does not require preferred hospitals to breach any peer confidence under" § 12.6–2(a). Conclusions 26 and 28, 603 F.Supp. at 1087. The second of these grounds is all we need consider. The Blues distributed to each hospital material in question-and-answer form explaining the PPO contracts. Answer 89 states: "In no case would we [the Blues] be entitled by the contract language to access which you cannot legitimately provide because of statutory requirements placed upon you." The contract, as the parties construe it, therefore does not violate § 12.6–2(a). There will be time for further consideration of preemption if the Blues should retract this assurance and seek access to information covered by the Peer Review Act.

VII

The district court not only construed the Indiana statutes but also held that the PPO contracts do not breach the provider agreements the Blues have with hospitals participating in their service benefit insurance plan. The Hospitals say that the declaration that there has been no breach must be set aside because the district court heard no evidence on the issue. Yet the Hospitals do not inform us what evidence the district court needed to hear, and they say that "as of the close of the evidence no breach had yet occurred."

The Hospitals do not refer us to any language in their provider contracts that is inconsistent with any obligations in the PPO contracts. The Blues point out that hospitals who have joined the PPO plan have agreed to the terms of the contract, and hospitals who have not joined simply proceed under the terms of the old contracts without modification. If a patient covered by PPO insurance goes to a hospital that is not a member of the PPO, the Blues reimburse 75% of the hospital's charges. The patient must pay the remainder. The Blues assert, without contradiction from the Hospitals, that their basic contracts provide for the care of patients with copayments of this character.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

The very existence of the PPO therefore cannot be deemed an anticipatory breach of the contracts of the hospitals outside the PPO. Perhaps some cases will arise in which obligations the Blues have assumed under the PPO will produce violations of the existing non-PPO contracts. We do not interpret the district court's judgment as ruling out this prospect. All the district court was entitled to hold—all it did hold—is that the PPO plan is not an inevitable violation of existing contracts. More specific claims of breach may be raised in cases presenting them.

VIII

One procedural issue requires our attention. During discovery the Hospitals requested access to the Blues' data on prices bid by each hospital and the calculations the Blues performed to decide which hospitals to include in the PPO. The Blues replied that the data are trade secrets, that they had pledged confidentiality to the hospitals, and that they feared the Hospitals could use the comparative price information to raise their prices or collude in future years. See *United States v. United States Gypsum Co., supra.* The district court agreed that the data are sensitive and offered the Hospitals access under a protective order restricting access "only to trial counsel to this lawsuit who are engaged in the preparation for trial ... and who have neither represented nor [will] represent for 18 months any hospital, the Indiana Hospital Association, or any other entity in connection with the Blue Cross PPO on any matter other than the trial of the case."

Counsel for the Hospitals refused to take the information with these strings attached. Witnesses for the Blues testified, based on portions of these data, about how the Blues decided which hospitals to include in the PPO. The Hospitals now say that their lack of access to the data prevented them from examining these witnesses or trying the case effectively, and they ***1346** ask for a new trial at which they will be able to use the data.

The price data are unquestionably relevant, and parties are entitled to information as important as this was. *Deitchman v. E.R. Squibb & Sons, Inc.,* 740 F.2d 556 (7th Cir.1984). The price data are also unquestionably sensitive trade secrets of the Blues. Hospitals armed with the data could use it to advantage in the next round of negotiations. Access to the data could turn an antitrust suit into the basis of effective collusion, a concern we have expressed above. See also *General Leaseways, Inc. v. National Truck Leasing Ass'n,* 744 F.2d 588, 597 (7th Cir.1984). Confidential information is customarily made available, if at all, under a protective order, and the district court has substantial discretion to decide which information should be protected and to frame the order. *Seattle Times Co. v. Rhinehart,* 467 U.S. 20, 104 S.Ct. 2199, 2206–09, 81 L.Ed.2d 17 (1984); *E.I. du Pont de Nemours Powder Co. v. Masland,* 244 U.S. 100, 103, 37 S.Ct. 575, 576, 61 L.Ed. 1016 (1917).[2]

Counsel for the Hospitals balked at this protective order, they said, because it "restricts us [as] lawyers undertaking representations in future matters."[3] But the district court had reason to think the restriction necessary. Counsel for the Hospitals regularly represented them in price negotiations with the Blues. When counsel act as the negotiators, they become business agents of the Hospitals, and there is little difference between providing information to the president of a hospital and providing it to the hospital's lawyer-agent.

The protective order did not prevent the Hospitals from retaining a separate law firm for the purpose of inspecting and using the data. It simply prevented the particular lawyers who had seen the data from working for a hospital as business agents during the next 18 months—the ensuing contract year and negotiation season. The Hospitals are represented by more than one firm, and they could have chosen from them (or still other firms) lawyers to examine and use the data while leaving the Hospitals' regular firms free to serve in dual legal and business roles as before. The district court therefore did not abuse its discretion in framing the order.

AFFIRMED.

WILL, Senior District Judge, concurring in the judgment.

I concur with the court's opinion because I read it as consistent with the traditional standards for granting or denying a preliminary injunction. Recently, in *Lawson Products, Inc. v. Avnet, Inc.,* 782 F.2d 1429 (7th Cir.1986), this court reaffirmed the continuing viability of the traditional standards, despite the wide-ranging revisions suggested in dictum by the opinions in *Roland Machinery Co. v. Dresser Industries, Inc.,* 749 F.2d 380 (7th Cir.1984) and *American Hospital Supply Corp. v. Hospital Products Limited,* 780 F.2d 589 (7th Cir.1986). In those cases, the court, while professing merely to review the law of preliminary injunctions, devised a novel "sliding scale" method of analysis. While intellectually diverting, the formula—and the heightened standard of appellate review which accompanied it—have been criticized as virtually abolishing the customary discretion of the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

trial judge in deciding preliminary injunction motions. *See* ***1347** *American Hospital,* 780 F.2d at 608 (Swygert, J., dissenting) ("in this circuit, despite vigorous protestations to the contrary, the standard of review of the grant or denial of a preliminary injunction is effectively *de novo* "); *Roland,* 749 F.2d at 396–404 (Swygert, J., dissenting).

The *Lawson* court, recognizing the possibility of conflicting interpretations, read *Roland* and *American Hospital* as "in harmony with the traditionally flexible and discretionary responsibilities of the district judge, sitting as chancellor in equity, in preliminary injunction matters." At 595. I heartily concur.

In the present case, Judge Steckler's fine opinion gave thorough consideration to all the relevant factors: the adequacy of a legal remedy, the balance of harms, the public interest, and the plaintiffs' likelihood of success on the merits. I scarcely think the quality of justice dispensed in his court would have been improved had he invoked the formula "grant the preliminary injunction if but only if P x Hp > (1–P) x Hd." *See American Hospital,* 780 F.2d at 593. At best, I suspect it would have diverted him from the equitable nature of the task at hand.

There is an old and wise saying: "if it ain't broke, don't fix it." As evidenced by Judge Steckler's decision and opinion, the traditional standards "ain't broke." I view today's decision, like the recent decision in *Lawson,* as an attempt to "bury with kindness" the legal revisionism undertaken in *Roland* and *American Hospital* and therefore I concur.

All Citations

784 F.2d 1325, 54 USLW 2493, 1986-1 Trade Cases P 66,974

Footnotes

* See 788 F.2d 1223.

* The Honorable Hubert L. Will, Senior District Judge for the Northern District of Illinois, is sitting by designation.

1 People who cannot divert to preferred providers are unlikely customers of PPO plans. When a person's physician has privileges only at non-PPO hospitals, the incentives created by the plan have less effect, if they have any. Because the PPO plan adds a new option and does not withdraw any old one, patients who lack a choice among hospitals are best off sticking with their existing financing scheme. Throughout this opinion, when we discuss patients' incentives we refer only to those patients who have options or can persuade physicians to take advantage of these options.

2 The data were not introduced into evidence, and therefore the presumption that evidentiary matters will be available to the public does not apply. See *In re Continental Illinois Securities Litigation,* 732 F.2d 1302 (7th Cir.1984) (announcing a presumption of availability). The D.C. Circuit has concluded that the panel in *Continental Illinois* got its history wrong, see *In re Reporters Committee for Freedom of the Press,* 773 F.2d 1325 (D.C.Cir.1985) (no presumption of access), but this is not the occasion to resolve the question.

3 Counsel cited Disciplinary Rule 2–107, which says that counsel shall "not enter into an agreement that restricts his right to practice law" as part of a "settlement of a controversy or suit". The protective order was not part of a "settlement," and we therefore need not consider whether it "restricts [the] right to practice law" within the meaning of the rule.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-3

15 Cal.2d 439
Supreme Court of California.

BALLARD et al.
v.
MacCALLUM et al.

L. A. 16750.
|
April 26, 1940.

Synopsis
In Bank.

Action by Willa Ballard and another, as administrators of the estate of William Alpheus Ballard, also known as W. A. Ballard, deceased, against Emilie G. MacCallum and others, to cancel a trust created by decedent as trustor and to obtain a reconveyance of the corpus of the estate. From a judgment for the defendants, plaintiffs appeal.

Affirmed.

****693** ***440** Appeal from Superior Court, Los Angeles County; Percy Hight, judge.

Attorneys and Law Firms

William L. Kuehn and Franz R. Sachse, both of Los Angeles, for appellants.

Phillip N. McCaughan, of Long Beach, for respondent Emilie G. MacCallum.

Edmund Nelson and Hugo Steinmeyer, both of Los Angeles, for respondent Bank of America Nat. Trust & Savings Ass'n.

Opinion

GIBSON, Justice.

This is an action by the administrators of the estate of William A. Ballard to cancel a trust created by decedent as trustor, and to obtain a reconveyance of the corpus of the estate. The trial court gave judgment for defendant and plaintiffs appealed. The appeal involves the interpretation of two instruments, one denominated a 'contract of annuity for life' and the other a 'declaration of trust'.

On January 14, 1935, decedent, then eighty-five years of age, executed the annuity contract under which he agreed to convey certain property to the California First National Bank of Long Beach as trustee, for the benefit of defendant Emilie G. MacCallum. In consideration therefor she agreed to pay him the sum of $110 per month during his natural life and also to pay all taxes, assessments and insurance premiums, and to keep the property in repair. It is stated that time is of the essence of the contract and that if the payment or charges be not paid as provided therein the interest of Miss MacCallum shall be forfeited and the property shall revert to Ballard. The trustee is authorized by Ballard to convey the property to Miss MacCallum upon his death, if the agreement is fully kept.

It is further provided that in the event of default in payments by the beneficiary, which default shall continue for ten (10) days after notice in writing given by the trustor or trustee, or in the event of default in discharging liens or encumbrances which shall continue for thirty (30) days after such notice in writing, or in the event of failure to pay any of the taxes or assessments in the time provided by law, the trustor, 'at his option, after thirty (30) days' notice' may declare the agreement cancelled, and the trustee shall then reconvey the real property to the trustor. The contract declares that all of the obligations of the beneficiary are ***441** 'conditions precedent to be faithfully kept and performed * * * strictly in accordance with the terms of this agreement' to entitle her to continue in possession of the property.

A declaration of trust was contemporaneously executed by the California First National Bank of Long Beach as trustee, and decedent as trustor, for the benefit of Miss MacCallum, to carry out the terms of the annuity contract, which was incorporated by reference. The declaration provides ****694** that 'in the event of the failure of the Beneficiary hereunder to make the payments as and when provided for under the agreement', or any other default by the beneficiary, 'providing further that said default has not been cured in accordance with the terms of said agreement', then the trustee shall reconvey the property to the trustor, 'and said trust, upon such reconveyance, shall absolutely cease and determine * * *'. It is further provided that in the event of the death of the trustor, 'this trust shall ipso facto cease and determine at the time of such demise, and the entire trust property shall be by said Trustee conveyed and delivered so far as it may then be able, to Emilie G. MacCallum, a single woman, provided the payments and obligations of said agreement * * * be fully performed until the death of said Trustor'.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Defendant Bank of America succeeded the First National Bank of Long Beach as trustee. On December 22, 1936, Ballard died intestate and plaintiffs duly qualified as administrators of the estate. Thereafter plaintiffs brought this action to compel the reconveyance of the property to the estate.

Four causes of action were set forth in the complaint. The first was based upon the alleged failure of Miss MacCallum to make payments and to perform other obligations of the contract. The second alleged incompetency of Ballard and undue influence of Miss MacCallum at the time of the execution of the contract and declaration of trust. The third cause of action alleged that the consideration for the contract and declaration of trust was wholly inadequate. The fourth alleged that the consideration had failed by reason of nonperformance of defendant MacCallum. The complaint contained no allegation that notice of the alleged default or nonperformance by Miss MacCallum was ever given to her.

At the trial defendant objected to the introduction of evidence on the ground that the annuity contract and declaration ***442** of trust provide for termination only after notice of default given to the beneficiary, and that the complaint failed to state a cause of action because no such notice was alleged. The court sustained this objection as to the first and fourth causes of action. After trial on the second and third causes, the court found against plaintiffs on the issues raised and rendered judgment for defendants.

As already stated, the determination of this appeal depends upon the proper construction of these two instruments. No question is raised as to the sufficiency of the evidence to justify the findings in favor of defendants on the other issues.

An inspection of the provisions of the two instruments discloses the controversy between plaintiffs and defendant MacCallum as to their effect. Certain language suggests that if the beneficiary fails in her obligation to make the monthly payments or to meet other charges against the property, the right shall *automatically* cease, that is, they shall be forfeited and the land shall revest in the trustor and his successors without any action on their part. This inference may be drawn, for example, from the provision that all of the rights 'shall cease and determine and be forfeited * * * and the property shall revert', and the provision that each and all of the terms of the agreement are 'conditions precedent' and must be strictly performed by the beneficiary to entitle her 'to continue in possession'. Other language justifies the opposite inference, namely, that there is no automatic forfeiture or divestment of rights of the beneficiary upon default, but that written notice of default, followed by failure to cure the same for a specified period, is a prerequisite to the power to forfeit rights of the beneficiary and to retake the property. This is the normal effect of the provisions of the agreement that in case of default for ten days or thirty days after notice in writing, the trustor at his option may cancel the agreement. This view is reinforced by the statement in the trust instrument providing for termination of the trust upon default, 'and, providing further, that said default has not been cured in accordance with the terms of said agreement'.

Faced with these contradictory provisions the trial court adopted the latter view, holding that the mere default by the beneficiary did not immediately terminate all her rights, but gave the trustor an election to serve notice of default and ***443** thereby terminate after the failure to cure the same within the required period. This interpretation of the trial court, if reasonable, must be upheld.

Plaintiffs attack the judgment on several grounds. They first call attention to the ****695** familiar rule that inconsistencies in an instrument should if possible be reconciled so as to give effect to every part of the agreement. They contend that the court has given effect only to the provisions requiring notice prior to cancellation, and has ignored the provisions for automatic forfeiture upon default. Their suggested reconciliation is to treat the trust as terminable by the trustor during his lifetime only after notice of default, but to hold it subject to forfeiture without notice if at the death of the trustor the beneficiary has not fully performed. In support of their theory they lean heavily upon the provision that performance by the beneficiary is a 'condition precedent'. They also argue that the trial court's construction of the instruments is inequitable, in that it permits the beneficiary to reap the benefits of the contract even though it is alleged that she did not perform on her part.

We may first notice the argument based on the so-called equities of the case, and here it is important to grasp the distinction between what the contract contemplates and what may happen by reason of unforeseen circumstances. There is nothing inequitable in a bargain merely because it turns out better for one party than the other. The fact that the trustor died shortly after the agreement was made, so that the actual obligations of the beneficiary were slight, was simply one of the contemplated possibilities. He might have lived a considerable time and her obligations might have been quite large. These uncertainties are inherent in any agreement of this character. The original agreement gave the trustor the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

assurance of support for the rest of his life in exchange for a transfer of his property, and its fairness is not open to question.

Nor is it necessarily inequitable that defendant claims rights in the property despite failure to make her required payments. She was still obligated to pay at decedent's death and the remedy of forfeiture after notice was concededly available if she refused. If she has not yet paid she can still be held liable. In short, the contract itself provides an ample remedy for any default on the part of defendant and the ***444** agreement as thus interpreted is not therefore rendered inequitable by any alleged failure of defendant to perform.

Next we have the assertion that the court fails to give effect to the whole of the contract. The answer is, of course, that where the agreement contains inconsistent provisions, it is impossible to give each its full effect, and plaintiffs' argument is nothing more than a plea that we choose those favorable to them. The suggestion that the provisions differ depending on whether the trustor is living or dead is without any support in the text of the agreement, and the distinction has no relevant connection with the objects of the parties.

In the face of these plain contradictions in the instruments, a fundamental rule of construction becomes applicable. the interpretation sought by plaintiffs is one which would lead to the forfeiture of property rights by reason of the mere failure to make payments strictly on time. In this state, by a long line of decisions, we have recognized such forfeitures in instalment contracts for the purchase of land and in conditional sales of goods. But aside from these special situations, our courts follow the accepted doctrine that equity will relieve even against an express provision for forfeiture. See Civ.Code, §§ 3275, 3369; Ebbert v. Mercantile Trust Company, 213 Cal. 496, 2 P.2d 776; Hopkins v. Woodward, 216 Cal. 619, 15 P.2d 499; Henck v. Lake Hemet Water Co., 9 Cal.2d 136, 69 P.2d 849; 20 Cal.L.Rev. 194; 21 Cal.L.Rev. 516; 18 Cal.L.Rev. 681; 52 Harv.L.Rev. 129.

In the instant case we are not required to apply this doctrine and grant relief from express and unmistakable language compelling a forfeiture. The problem here is much simpler. We have two possible constructions, one of which leads to a forfeiture and the other avoids it. In such a case the policy and rule are settled, both in the interpretation of ordinary contracts and instruments transferring property, that the construction which avoids forfeiture must be made if it is at all possible. See Hawley v. Kafitz, 148 Cal. 393, 83 P. 248, 3 L.R.A.,N.S., 741, 113 Am.St.Rep. 282; Henck v. Lake Hemet Water Co., supra; Restatement, Property, sec. 45, comment i.

The interpretation urged by plaintiffs could give rise to great injustice in the operation of this contract. Under their theory the beneficiary could keep on paying monthly sums to ***445** the trustor and all the expenses of maintaining the property for a period of years, and yet the slightest subsequent failure in the prompt performance ****696** of any one of her obligations would automatically terminate all of her rights and deprive her of the only return provided for her performance. In the Ebbert case, supra [213 Cal. 496, 2 P.2d 777], this court found that the terms of the contract were to this effect, and that the provision for forfeiture expressly applied 'irrespective of the kind or extent of default in performance, or the amount of beneficial performance already received'. There it became necessary to overturn the very language of the agreement in order to avoid such a grossly inequitable result. Here it is only necessary to reconcile the conflicting provisions of the instruments in favor of those which avoid the inequitable forfeiture urged by plaintiffs.

The judgment is affirmed.

We concur: WASTE, C. J.; CURTIS, J.; SHENK, J.; CARTER, J.; HOUSER, J.; EDMONDS, J.

All Citations

15 Cal.2d 439, 101 P.2d 692

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-4

KeyCite Yellow Flag - Negative Treatment
Distinguished by Cook Inc. v. Boston Scientific Corp., 7th Cir.(Ill.), June 19, 2003

330 F.3d 942
United States Court of Appeals,
Seventh Circuit.

BANK OF AMERICA, N.A., Creditor-Appellant,
v.
Alex D. MOGLIA, Trustee-Appellee.

No. 02-2517.
|
Argued Jan. 21, 2003.
|
Decided June 2, 2003.

Synopsis
Adversary proceeding was brought for determination of creditors' respective interests in corpus of "rabbi trust" that Chapter 7 debtor established prepetition in order to create source of funding for its otherwise unfunded employee benefit plans. The Bankruptcy Court, Ronald Barliant, J., ruled that it had jurisdiction over proceeding, that trust corpus was included in property of estate, and that secured creditor's security interest in general intangibles did not extend to trust corpus, 2002 WL 571661. Appeal was taken. The United States District Court for the Northern District of Illinois, Marvin E. Aspen, Senior District Judge, affirmed, 278 B.R. 778, and appeal was taken. The Court of Appeals, Posner, Circuit Judge, held that: (1) creditor's security interest in general intangibles of debtor did not extend to corpus of rabbi trust; (2) clause in trust agreement creating rabbi trust, that prohibited settlor from granting any creditor a security interest in trust corpus, was enforceable under Illinois law; and (3) trustee of rabbi trust was not "account debtor" of Chapter 7 debtor under Illinois law.

Affirmed.

Attorneys and Law Firms

***943** Larry J. Nyhan, Sidley Austin Brown & Wood, Chicago, IL, Alan C. Geolot (argued), Sidley Austin Brown & Wood, Washington, DC, for Appellant.

Jon C. Vigano, D'Ancona & Pflaum, Chicago, IL, Steven B. Towbin (argued), Kathleen H. Klaus, Shaw, Gussis, Fishman, Glantz, Wolfson & Towbin, LLC, Chicago, IL, for Trustee-Appellee.

Robert V. Shannon, Bell, Boyd & Lloyd, Chicago, IL, for Debtor.

Before POSNER, KANNE, and DIANE P. WOOD, Circuit Judges.

Opinion

POSNER, Circuit Judge.

Outboard Marine Corporation is in Chapter 7 bankruptcy, and among its holdings are the assets, currently worth some $14 million, in what is known as a "rabbi trust." Bank of America, as the agent of Outboard's secured creditors, claims a security interest in these assets, while the trustee in bankruptcy claims them for the unsecured creditors. The security agreement on which Bank of America relies covers all Outboard's "general intangibles," a term of great breadth in commercial law, see UCC § 9-102(a)(42) and official comment 5(d), and broadly defined in the agreement as well to include, ***944** besides a number of irrelevant enumerated items, "all other intangible personal property of every kind and nature." The term describes the assets of the rabbi trust, but the bankruptcy court, seconded by the district court, held that they nevertheless were not subject to the security agreement, and so ruled for the trustee. The ruling was a final, appealable order because it resolved a discrete dispute that, were it not for the continuing bankruptcy proceedings, would have been a stand-alone dispute between Bank of America and the trustee as the representative of the general creditors. *In re Golant,* 239 F.3d 931, 934 (7th Cir.2001); *In re Rimsat, Ltd.,* 212 F.3d 1039, 1044 (7th Cir.2000). "A judgment does not lose its finality merely because there is uncertainty about its collectibility, corresponding to uncertainty about how many cents on the dollar the creditor will actually receive on his claim once all the bankrupt's assets are marshaled and compared with the total of allowed claims, and the priorities among those claims are determined. Thus the fact that the bankruptcy proceeding continues before the bankruptcy judge does not preclude treating an interlocutory order by him-interlocutory in the sense that it does not terminate the entire proceeding-as final for purposes of appellate review. (And if it is final for those purposes, then so is the district court's affirmance of his order.)" *In re Szekely,* 936 F.2d 897, 899 (7th Cir.1991).

A rabbi trust, so called because its tax treatment was first addressed in an IRS letter ruling on a trust for the benefit

of a rabbi, Private Letter Ruling 8113107 (Dec. 31, 1980); see also IRS General Counsel Memorandum 39230 (Jan. 20, 1984), is a trust created by a corporation or other institution for the benefit of one or more of its executives (the rabbi, in the IRS's original ruling). See, e.g., *Westport Bank & Trust Co. v. Geraghty,* 90 F.3d 661, 663-64 (2d Cir.1996); *Hills Stores Co. v. Bozic,* 769 A.2d 88, 99 (Del.Ch.2000); Kathryn J. Kennedy, "A Primer on the Taxation of Executive Deferred Compensation Plans," 35 *John Marshall L.Rev.* 487, 524-27 (2002). The main reason (recited at the outset of the trust document in this case) for such a trust is that, should the control of the institution change, the new management might reduce the old executives' compensation, or even fire them; the trust, which consistent with this purpose is not funded until the change of control occurs, cushions the fall.

But as the IRS explained in the letter ruling, unless an executive's right to receive money from the trust is "subject to substantial limitations or restrictions," rather than being his to draw on at any time (making it income to him in a practical sense), the executive must include any contribution to the trust and any interest or other earnings of the trust in his gross income in the year in which the contribution was made or the interest obtained. See *McAllister v. Resolution Trust Corp.,* 201 F.3d 570, 572-73, 575 (5th Cir.2000). The "substantial limitations or restrictions" condition was satisfied in the transaction on which the IRS ruled. The trust agreement provided that the rabbi would not receive the trust assets until he retired or otherwise ended his employment by the congregation. Until then the corpus of the trust and any interest on it would be owned by the congregation, see *Maher v. Harris Trust & Savings Bank,* 75 F.3d 1182, 1185 (7th Cir.1996); *Goodman v. Resolution Trust Corp.,* 7 F.3d 1123, 1125 (4th Cir.1993), so the rabbi would have neither legal nor equitable right to the money. Cf. 26 U.S.C. § 457(f)(1)(A). And, what is key in this case, the trust instrument provided that "the assets of the trust estate shall be subject to the claims of [the congregation's] creditors as if the ***945** assets were the general assets of [the congregation]."

The word "creditors" is not defined either in the IRS's letter ruling or in the trust agreement in this case; but a "Model Rabbi Trust" agreement approved by the IRS states that the assets of the trust are subject to the claims of the settlor's "general creditors," Rev. Proc. 92-64, 1992-2 C.B. 422 (July 28, 1992), a term invariably used to refer to a debtor's *unsecured* creditors. See, e.g., *United States v. Munsey Trust Co.,* 332 U.S. 234, 240, 108 Ct.Cl. 765, 67 S.Ct. 1599, 91 L.Ed. 2022 (1947); *Dewsnup v. Timm,* 502 U.S. 410, 431-32, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992) (dissenting opinion); *In re Merchants Grain, Inc.,* 93 F.3d 1347, 1352 (7th Cir.1996); *United States v. One-Sixth Share,* 326 F.3d 36, 44 (1st Cir.2003); *United States v. Watkins,* 320 F.3d 1279, 1283 (11th Cir.2003); *United States v. $20,193.39 U.S. Currency,* 16 F.3d 344, 346 (9th Cir.1994); Douglas G. Baird, *The Elements of Bankruptcy* 12, 101, 154, (3d ed.2001). The cases assume rather than hold that "general creditor" means "unsecured creditor," but what else could it mean? What work does "general" do unless to distinguish unsecured from secured creditors? Bank of America has no answer to that question.

Outboard is conceded to have established a bona fide rabbi trust, so that its contributions to the trust and the income that those contributions generated were not includible in the executives' gross income. Therefore, if the validity of a rabbi trust depends on its assets' being reserved for the employer's unsecured creditors, we can stop right here and affirm; the Bank of America, as a secured creditor, would have no right to the assets-otherwise the trust's beneficiaries would not have received the favorable tax treatment accorded the beneficiaries of a rabbi trust, and they did receive it. But it is uncertain whether such a reservation actually is essential to the favorable tax treatment of a rabbi trust. All that the tax law requires is that there be substantial limitations on the beneficiaries' access to the trust assets, and a reservation of the assets in the event of bankruptcy to both the secured and the unsecured creditors of the settlor, rather than to the unsecured creditors, might well be thought substantial. For the reservation would keep those assets, most of them at any rate, out of the beneficiaries' hands-though this is provided that the limitation were coupled with a limitation on the beneficiaries' having free access to the assets of the trust before they leave their employment with the grantor. Without such a limitation, the reservation of creditors' rights would be illusory-the beneficiaries would pull the money out of the trust as soon as insolvency loomed on the horizon-and indeed the trust's assets might well be taxable as income to the beneficiaries. But we recall that, consistent with this concern, the assets of the rabbi trust were owned by the congregation until the rabbi's employment ended.

We say that a limitation to all, rather than just to the unsecured, creditors "might be" rather than "would be" substantial enough to satisfy the Internal Revenue Service because executives often are creditors of their firm; if they were secured creditors and their security interest embraced the assets of the trust, their claims to those assets would be

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

superior to those of the firm's unsecured creditors, which would tend to make the limitation that is fundamental to the favorable tax treatment of the rabbi trust-that the creditors have a superior claim to the beneficiaries-illusory. But the trust instrument in this case took care of that concern by providing that Outboard's executives could not obtain a security interest in the trust's assets.

***946** Even if the executives would not have sacrificed their favorable tax treatment had the trust instrument reserved the assets of the trust for all the company's creditors, secured and unsecured alike, in the event of bankruptcy, the instrument did not do this; it reserved those assets for the unsecured creditors. It states (we italicize the key terms) that the "Trust Corpus ... shall remain at all times subject to the claims of the *general creditors* of [Outboard]. Accordingly, [Outboard] shall not create a *security interest* in the Trust Corpus in favor of the Executives, the Participants [a term that apparently refers to retired executives] or *any creditor*." In the event of insolvency, the trustee "will deliver the entire amount of the Trust Corpus only as a court of competent jurisdiction, or duly appointed receiver or other person authorized to act by such court, may direct to make the Trust Corpus available to satisfy the claims of the Company's *general creditors.*"

This couldn't be clearer: secured creditors have no claim to the trust assets. And judges usually interpret written contracts (the instrument creating the rabbi trust in this case was an agreement nominally between Outboard and the trustee of the trust, Northern Trust Company, but realistically between Outboard and the executives who were the beneficiaries of the trust, see *Westport Bank & Trust Co. v. Geraghty, supra,* 90 F.3d at 663-64) according to the conventional meaning of their terms, that is, literally. This is especially appropriate in the case of a negotiated contract involving substantial stakes between commercially sophisticated parties, as in this case, who know how to say what they mean and have an incentive to draft their agreement carefully. Such a style of interpretation protects the parties against the vagaries of the litigation process-a major reason for committing contracts to writing-without too great a risk of misinterpretation.

But literal interpretation of written contracts, even when the parties are sophisticated and the stakes substantial, is merely presumptively the right approach to take. Even sophisticated lawyers and businessmen sometimes stumble in their use of language, or use language that is specialized to their trade and departs from normal usage, or fail to anticipate contingencies that may make the language of the contract yield absurd results if it is read literally, and if these circumstances are evident to the court the contract will not be interpreted literally. Bank of America argues in this vein that *of course* all that Outboard intended to do in the passages of the trust agreement that we quoted was to create a rabbi trust, that is, a grantor trust that would enjoy a favorable tax status, and so if a rabbi trust does not necessarily forfeit its favorable tax status by reserving the trust assets for secured as well as unsecured creditors, neither does the trust agreement. The security agreement, which we quoted at the beginning of this opinion, contains no language to suggest that the assets of the rabbi trust would be excluded from Bank of America's security interest just because they are pledged to any creditor and not just to unsecured creditors.

This argument is not negligible but neither is it sufficiently compelling to rebut the presumption in favor of literal interpretation to which we referred. Rather the contrary. The language of the Model Rabbi Trust would make it natural for Outboard to assume that to create a valid rabbi trust it would *have* to reserve the trust's assets for its general creditors, which undoubtedly it would understand to mean its unsecured creditors. The assumption may have been incorrect, more precisely may have been excessively cautious; but it provides the best guide to the meaning that Outboard and the executives ascribed to the agreement. The executives in particular would tend to favor the ***947** cautious approach rather than jeopardize their tax benefits for the sake of Outboard's secured creditors. And though they might benefit indirectly, and Outboard directly, from the company's being able to pledge more of its assets to secure a loan to the company, this benefit-since the assets in a rabbi trust are likely to be only a small fraction of the company's total assets-would probably be outweighed by the risk of forfeiting favorable tax treatment by departing from the template of the Model Rabbi Trust.

The trust agreement does not merely reserve the trust's assets for the general creditors, moreover; it forbids Outboard to create a security interest in favor not only of the executives (which might make the trust illusory and forfeit the beneficiaries' favorable tax treatment) but also of any creditor. So even if Outboard thought that the term "general creditors" includes secured creditors, the agreement explicitly forbids the creation of a security interest in the trust assets. The trust instrument took as it were the extra step to make clear that the parties *really* intended to reserve the trust assets for Outboard's unsecured creditors. The security agreement, as we said, does not exclude the assets in the rabbi trust;

but to determine what assets it does include (because they are not listed in the agreement), one must look beyond the security agreement. And when one looks one finds the trust instrument, which excludes those assets. It is important to note in this connection that the rabbi trust was funded before the security agreement between Outboard and Bank of America was executed. Had it been funded after, Outboard's contribution of assets to the trust would have been subject to the security agreement regardless of the terms of the trust. For Outboard could not be permitted to impair the bank's security interest by putting some of the assets covered by the agreement into a trust that the bank could not reach.

Bank of America has a second string to its bow: it argues that Illinois law, which the parties agree governs the interpretation of the trust agreement, will enforce a contractual antiassignment provision, such as the provision in the trust instrument that forbids assigning a security interest in the assets of the rabbi trust to creditors, against an assignee only if the provision states that the assignor has no power, and not merely no right, to assign. So, the argument continues, because the trust instrument does not say in so many words that any attempt by Outboard to create a security interest in the trust assets would be void, ineffectual, etc., the creation of such an interest is not prohibited although a party (including any third-party beneficiaries, which Outboard's general creditors may or may not be, see *Exchange National Bank v. Harris,* 126 Ill.App.3d 382, 81 Ill.Dec. 277, 466 N.E.2d 1079, 1084 (1984); *Town & Country Bank v. James M. Canfield Contracting Co.,* 55 Ill.App.3d 91, 12 Ill.Dec. 826, 370 N.E.2d 630, 634-35 (1977)-we needn't decide), could sue for damages in the event of a breach of the provision.

Clauses in conveyances, or in other instruments contractual or otherwise that create property rights, that forbid the recipient of the property to sell it free and clear-or in legal jargon that create a "restraint on alienation"-are traditionally disfavored. *Gale v. York Center Community Co-op., Inc.,* 21 Ill.2d 86, 171 N.E.2d 30, 33 (1961); *Avon-Avalon, Inc. v. Collins,* 643 So.2d 570, 574 (Ala.1994). Sometimes they are disfavored because they are thought to create monopoly, concentrate wealth, or cater to "the capricious whims of the conveyor." *Gale v. York Center Community Co-op., Inc., supra,* 171 N.E.2d at 33. But more often and more realistically it is because they can increase transaction costs by preventing subsequent purchasers or assignees from knowing ***948** what they are getting. Cf. Gregory S. Alexander, "The Dead Hand and the Law of Trusts in the Nineteenth Century," 37 *Stan. L.Rev.* 1189, 1258-60 (1985). A legal requirement that the restraint be express, recorded, or otherwise readily ascertainable by potential purchasers and assignees minimizes, and often eliminates, those additional costs, cf. *Noblesville Redevelopment Comm'n v. Noblesville Limited Partnership,* 674 N.E.2d 558, 562-63 (Ind.1996); if the recipient's purchaser knows exactly what he is (not) getting, a refusal to enforce the restriction merely confers a windfall on him.

The requirement of express and readily ascertainable notice is satisfied here. When Bank of America made its credit agreement with Outboard, it knew, if it bothered to read the trust agreement along with the other documents that defined Outboard's assets, as it should have done and no doubt did do, that the security interest it was acquiring would not cover the assets (currently some $14 million) in the rabbi trust. Nothing would have been added to the trust agreement but empty verbiage had it said "and not only is Outboard forbidden to create a security interest in these assets in favor of any creditor, but if it tries to do so its action shall be null, void, and of no effect." Of course, if Illinois required those magic words, as many states still do, see *Rumbin v. Utica Mutual Ins. Co.,* 254 Conn. 259, 757 A.2d 526, 530-33, 535 (2000), and cases cited there, to rebut the presumption of nonassignability, then Bank of America could argue persuasively that it had relied on their absence when it signed the security agreement. But Illinois does not require them. *In re Nitz,* 317 Ill.App.3d 119, 250 Ill.Dec. 632, 739 N.E.2d 93, 96, 101 (2000); *Henderson v. Roadway Express,* 308 Ill.App.3d 546, 242 Ill.Dec. 153, 720 N.E.2d 1108, 1113 (1999); see also *CGU Life Ins. Co. v. Singer Asset Finance Co.,* 250 Ga.App. 516, 553 S.E.2d 8, 15 (2001).

Illinois's approach implements the modern view, expressed in *Restatement (Second) of Contracts* § 322(2) (1981), that an antiassignment provision in a contract is unenforceable against an assignee "unless a different intention is manifested." Magic words are not required: "Where there is a promise not to assign but no provision that an assignment is ineffective, the question whether breach of the promise discharges the obligor's duty depends on all the circumstances." *Id.,* comment c. The circumstances here weigh heavily in favor of enforcing the antiassignment provision when we consider the alternative remedy that is all that a "magic words" state would allow in the absence of the magic words-a suit for damages for breach of the provision. If the credit agreement between Outboard and Bank of America violated it by creating a security interest in the trust assets, then the contract breaker, and therefore the defendant in such

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

a suit, would be Outboard, which is to say the trustee, while the plaintiffs would be the general creditors-the trustee also. Enough said.

The Bank of America has one last argument, this one thoroughly frivolous-that the trustee under the trust agreement, who, remember, was in the event of Outboard's solvency to seek directions from a court concerning the disposition of the trust assets, was an “account debtor” of Outboard, that is, someone who owed Outboard money. UCC § 9-105(1)(a) (now superseded by UCC § 9-102(a)(3), unchanged however so far as bears on this case). An antiassignment clause is ineffective against an assignment of the debt of an account debtor. UCC § 9-318(4) (now, and again with immaterial changes, UCC § 9-406(d)(1)). Accounts and other simple written promises to pay are important collateral in modern commercial transactions, and their value as collateral is maximized ***949** by stripping them of encumbrances, such as an antiassignment clause unlikely to be noticed in the haste of transacting. The trust agreement was not that kind of instrument. And in any event the trustee owed Outboard nothing. The trustee was the debtor in a sense (an odd sense-one doesn't usually think of a trustee as the debtor of the trust's beneficiaries, though of course he holds its assets on their behalf) of the executives so long as Outboard was solvent, and after that he was the “debtor” in the same odd sense of Outboard's creditors. But he was never Outboard's “debtor.”

Bank of America, a large, responsible, and well represented enterprise, should not have made the account-debtor argument. Nor should it have treated a district court decision (*Lomas Mortgage U.S.A., Inc. v. W.E. O'Neil Construction Co.,* 812 F.Supp. 841 (N.D.Ill.1993)) as an authoritative statement of Illinois law. Not only has the Supreme Court instructed us not to give special weight to a district judge's interpretation of state law even if it is the state in which he sits, *Salve Regina College v. Russell,* 499 U.S. 225, 230-31, 111 S.Ct. 1217, 113 L.Ed.2d 190 (1991); *Beanstalk Group, Inc. v. AM General Corp.,* 283 F.3d 856, 863 (7th Cir.2002), but we have repeatedly reminded the bar that district court decisions cannot be treated as authoritative on issues of law. “The reasoning of district judges is of course entitled to respect, but the decision of a district judge cannot be a controlling precedent. E.g., *Colby v. J.C. Penney Co.,* 811 F.2d 1119, 1124 (7th Cir.1987); *Anderson v. Romero,* 72 F.3d 518, 525 (7th Cir.1995). The law's coherence could not be maintained if district courts were deemed to make law for their circuit, let alone for the nation, since district courts do not have circuit-wide or nationwide jurisdiction.” *FutureSource LLC v. Reuters Ltd.,* 312 F.3d 281, 283 (7th Cir.2002).

AFFIRMED.

All Citations

330 F.3d 942, 30 Employee Benefits Cas. 1705

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-5

207 Cal.App.2d 61
District Court of Appeal, First District, Division 1, California.

Charles J. BENTON, Plaintiff and Appellant,
v.
HOFMANN PLASTERING COMPANY, Alvin G. Coelho, Anita K. Coelho et al., Defendants and Respondents.

Civ. 19713.
|
Aug. 21, 1962.

Synopsis

Action against plastering contractor and lathing subcontractor for declaratory and other relief. From an adverse judgment of the Superior Court, Alameda County, Joseph A. Murphy, J., the plaintiff appealed. The District Court of Appeal, Bray, P. J., held that provision in lathing contracts executed by plastering contractor and lathing subcontractor, prohibiting the assignment of lathing subcontracts and any money due under them without written consent of plastering contractor, was valid and enforceable, and plastering contractor's right to monies under the lathing subcontracts was superior to that of plaintiff, who was the assignee of the lathing contracts and who had advanced money for the performance of the contracts to the subcontractor.

Judgment affirmed.

Attorneys and Law Firms

****269 *63** Francis T. Cornish, Berkeley, for appellant.

****270** Lindsay & Pettis, Warren G. Reid, Oakland, for respondent Hofmann Plastering Co.

Merrill, Commons, Hooper & Miller, Oakland, for respondent Coelho.

Opinion

BRAY, Presiding Justice.

Plaintiff Benton sued defendants Hofmann Plastering Company and Coelho in declaratory relief and for judgment against Hofmann for moneys advanced to defendant Coelho to enable Coelho to perform certain lathing contracts with Hofmann, to recover from Hofmann proceeds paid to Coelho under contracts assigned to plaintiff, to recover certain sums from Coelho, and to foreclose a deed of trust executed by Coelho and wife to Benton to secure advances.

Hofmann cross-complained claiming Coelho and Benton were partners, and sought damages for a breach of two lathing contracts by Coelho and for defective performance of a third.

Coelho then cross-complained [1] against Benton claiming partnership between him and Benton, seeking dissolution of partnership, appointment of receiver, and cancellation of deed of trust for lack of delivery and execution, and coercion.

Plaintiff appeals from the denial of most of the relief sought by him.

QUESTIONS PRESENTED.

Although there were many issues presented by the pleadings, the parties at trial limited the issues to be determined. They were:

1. The character of the Benton-Coelho agreement as to whether it was an agreement for advances to be repaid only from proceeds of contracts or for advances under a continuing obligation of Coelho's part to repay all moneys advanced.

2. Whether the assignments of proceeds from the Coelho-Hofmann contracts to Benton prevailed over their assignments to Hofmann.

3. Is plaintiff bound by the settlement of the Eden Office Building contract?

4. The validity of the deed of trust from Coelho to Benton.

5. Findings.

***64** 1. THE BENTON-COELHO AGREEMENT.

Defendant Coelho was engaged in the business of installing lathing in connection with various building contracts. Benton had advanced him money to aid in the financing of many of these projects. There is a dispute as to whether the money so advanced constituted a loan or an investment. We are not concerned with that question other than as an aid in interpreting the agreement which Benton and Coelho entered into December 21, 1953. It provided that in consideration of past and future advances by Benton, Coelho assigned to Benton the proceeds of all contracts which Coelho had entered into and which he might enter into for the performance of which contracts Benton had advanced or

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

would advance moneys to Coelho. Coelho agreed that upon all jobs financed by Benton, Coelho would impress upon the invoices on such jobs a rubber stamp provided by Benton which read 'Moneys due under the within job are assigned to Charles J. Benton pursuant to agreement evidenced by formal writing dated December ——, 1953.' Apparently this condition was met.

The agreement provided: 'The signed imprint of said stamp upon any invoice shall conclusively establish as between the parties * * * that Benton has advanced money to Coelho to finance him in the performance of the job represented by the invoice so imprinted, and that said advances have been made pursuant to the formula set forth in this memorandum of agreement.

'Upon making any advance such as Benton * * * shall hereafter make to Coelho to enable Coelho to finance any lathing job, all moneys due to Coelho or thereafter to become due to Coelho by virtue of ****271** the contract to which said advance relates are by virtue of any such advance assigned by Coelho to Benton. Upon request from Benton Coelho shall execute any formal document appropriate to evidence the assignment.'

The parties agreed that the advances should be repaid as follows: 'After all expenses for labor and materials used in the performance of each lathing job have been paid, as much of said proceeds advanced by Benton or paid for said lathing job as remain shall be paid to Benton until Benton shall have received the full amount of all advances on that contract. Should said proceeds be insufficient for that purpose, *any deficiency shall be paid to Benton out of the proceeds of other lathing jobs until Benton shall have received the entire principal advanced on each lathing job completed*. [Emphasis added.]

***65** 'If after all labor and materials have been paid and Benton has been reimbursed all moneys he has advanced to finance all lathing jobs completed, and any of the proceeds from any completed lathing job shall remain, Coelho shall be paid from said proceeds remaining up to an amount equal to 7% of the gross contract price charged by Coelho for that job. The balance thereafter remaining shall be divided equally between Benton and Coelho.

'The parties hereby expressly confirm that on all jobs heretofore performed by Coelho, whether settlement has been heretofore effected or whether settlement remains to be made, the advances by Benton have been on the basis outlined in this memorandum of agreement *and on no other basis*.' (Emphasis added.)

Plaintiff advanced Coelho moneys on jobs started before the above mentioned contract was entered into as well as after. All of the jobs were under contracts between Hofmann and Coelho. Hofmann was a plastering contractor who sublet the lathing to Coelho. Over the period involved Benton advanced some $73,000 which was not paid back to him. On occasion funds advanced by Benton for a particular job were used by Coelho, unknown to Benton, to pay indebtedness on other jobs for which Benton was providing the financing.

Benton contends that the contract constituted a loan agreement requiring repayment of all moneys advanced. Coelho contends [2] and the court found, that the contract was a loan agreement, repayment to be made solely from the proceeds of the lathing contracts. We adopt the statement of the trial judge, Honorable Joseph A. Murphy, in holding that the intent of the agreement was that repayment of advances should come solely from the lathing contracts. 'The agreement provides that Benton shall advance certain funds to Coelho on contracts which are then assigned to Benton, and, in the event that there is a loss on the contracts, such loss may be recouped from any subsequent contracts. This phase of the agreement, in the opinion of the court, indicates that each advance was, in fact, a debt due from Coelho to Benton because of the fact that either party could cancel the agreement at any time, and, conforming to the intent of the agreement if it were cancelled, Coelho's obligation to Benton for any losses up to the time of cancellation would automatically terminate. ***66** This is also borne out by the fact that Benton set up a reserve account against individual contracts, indicating that it was his intent that such reserve would liquidate not only the contract from which the reserve was drawn, but also any future contracts. This is also supported to some extent by the admission of Benton that be [he] made considerable profits on prior contracts and that at the outset he told Coelho he would like to get into the business to 'make a fast buck.' All of the circumstances and dealings would indicate that it was purely speculative * * *.

'There was testimony that Coelho made certain misrepresentations to Benton prior ****272** to November 22, 1957, and on the basis thereof procured advances from Benton. The evidence, however, is susceptible to a further inference; namely, that, while the funds advanced were not used on the particular job noted in the assignment, they were used on other jobs which had previously been financed by Benton; hence, the question of fraud is speculative and not

proved by a preponderance of evidence. It is also to be noted that after discovery of the fraud, Benton continued to make advances to Coelho.'

The agreement provides for repayment of the loans out of the proceeds of present contracts, and if these are insufficient, out of future contracts. There is no provision expressly relating to repayment of the loans in the event that both of these sources should prove insufficient. On the face of the contract, it appears that the parties provided with particularity for the sources of repayment of the loans, thereby indicating that the parties intended those sources to be the sole method of repayment. As the contract is ambiguous, the court looked behind it to the evidence, and concluded from both the contract and the evidence what the intent of the parties was. Benton contends that the fact that the deed of trust executed by Coelho and wife was to secure to Benton 'payment to indebtedness in the sum of any deficiency arising through beneficiary having financed Alvin George Coelho in purchasing and installing lathing * * *' conclusively shows that the loans were to be fully repaid. The court apparently believed the testimony of both Coelho and his wife that they were persuaded by Benton to execute the deed of trust to protect their home from Coelho's creditors. Therefore the court's finding that Benton is not entitled to recover from Coelho the unpaid balance to the moneys advanced by Benton should be affirmed.

2. ASSIGNMENTS.

As stated hereinbefore, the Benton-Coelho agreement provided that all proceeds of lathing contracts for which Benton ***67** made advances were assigned to Benton. While the record is not clear as to whether all the Hofmann-Coelho contracts under which Coelho did the lathing jobs contained the same provision as to nonassignability of the moneys to become due thereon, or whether they all contained nonassignability clauses, the parties have assumed they all had the following clause or one similar to it: 'That no assignment of this Subcontract, nor of any money due or which may become due hereunder shall be made without the written consent of the Contractor [Hofmann].'

The court found that 'provisions of the Hofmann-Coelho agreements against assignment of money due or to become due by virtue of said agreements did not, under the law of this State, prevent the assignment by defendant Coelho of such moneys to plaintiff, and therefore plaintiff, as Coelho's assignee, is entitled to judgment for the following sums * * *.'

The court was in error in its statement, which, in effect, declared that the law of California considered nonassignability clauses of this kind ineffective. In Parkinson v. Caldwell (1954), 126 Cal.App.2d 548, 552, 272 P.2d 934, 937, the court stated: 'Where the language is clear an agreement not to assign a debt is effective.' The court, after referring to a New York decision, relies upon language in 4 Corbin on Contracts, section 872, page 486, where the author stated: 'In any case, it is quite possible for the parties to show by apt words that rights created by the contract shall not be assignable.'

The court also relies upon the holding in Fairbanks v. Crump Irr. etc. Co., Inc. (1930), 108 Cal.App. 197, 205, 291 P. 629, 292 P. 529. In Fairbanks the court held that a provision that money due under a contract might be assigned with the permission of the obligor, is the same as a provision that it may not be assigned without such permission and that such a provision should be given effect. Parkinson concurs in this conclusion. (See also 37 A.L.R.2d 1251, 1253.)

There is a distinction between an assignment of a contract and an assignment ****273** of the proceeds of the contract. See Trubowitch v. Riverbank Canning Co. (1947), 30 Cal.2d 335, 339, 182 P.2d 182, holding that a provision in a contract against assignment does not preclude the assignment of money due or to become due under the contract. However, here the prohibition was against assigning either the contract or the moneys to become due thereunder. Such a prohibition is proper. (See 4 Corbin on Contracts, pp. 482, 486, 494.) ***68** Trubowitch also implies that the parties may effectively so provide by the use of appropriate language.

Section 176 of the Restatement of Contracts provides: 'A prohibition in a contract of the assignment of rights thereunder is for the benefit of the obligor, and does not prevent the assignee from acquiring rights against the assignor by the assignment or the obligor from discharging his duty under the contract in any way permissible if there were no such prohibition.' That provision is in accord with the statement in 5 Cal.Jur.2d 292, which states: 'It appears that the courts will generally refuse to enforce nonassignability clauses, at least as between the assignor and assignee and those claiming under them, where the transfer works no substantial detriment to the rights of the other party to the contract. [Citing 35 Cal.L.Rev. 577.] Thus, it is ruled that clauses restricting assignability are for the benefit of the obligor, and do not prevent the assignee from acquiring rights

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

against the assignor by an assignment apparently prohibited by the terms of the contract.'

In the instant case it is the obligor who will apparently suffer if the assignment is held valid as against him. The validity of the assignment does not aid plaintiff in seeking recovery against Coelho, as his rights against Coelho exist independently of the assignment. The only question is one of set-off and priority as between Hofmann and plaintiff.

The area of limitations on assignments is, of course, one in which the courts strictly construe such restrictions just as they jealously guard the right to transfer property in general. However, explicit language will be followed in cases of this kind. The court in Thomas v. Thomas (1961), 192 Cal.App.2d 771, 779, 13 Cal.Rptr. 872, 877, after quoting from Fairbanks v. Crump, supra, 108 Cal.App. 197, 291 P. 629, 292 P. 529, and Parkinson v. Caldwell, supra, 126 Cal.App.2d 548, 272 P.2d 934, notes, 'The courts, of course, have placed certain limits on nonassignment clauses—there is strong policy in favor of the free transferability of all types of property (Farmland Irrigation Co. v. Dopplmaier, 48 Cal.2d 208, 222, 308 P.2d 732, 66 A.L.R.2d 590); accordingly, where the restriction against assignability is waived, rights may be transferred despite the prohibition (Trubowitch v. Riverbank Canning Co., 30 Cal.2d 335, 342, 182 P.2d 182), and the prohibition does not apply where all that remains to do under the contract is the payment of money. Butler v. San Francisco Gas & Electric Co., 168 Cal. 32, 41, 141 P. 818. Here, it is conceded, there has been no waiver by Edison as ***69** obligor; also, the Fairbanks case, quoted from Parkinson v, Caldwell, supra, would seem to support the view that *where the prohibition against assignment relates to money due under a contract, it will be enforced where the prohibition in question is explicit*.' (Emphasis added.)

Here there is no question of waiver by Hofmann. The prohibition in the lathing contracts extends not merely to the contracts themselves but to the money due or to become due thereunder as well. The nonassignment provisions are valid and should be enforced. Hofmann's right to the moneys under the Coelho-Hofmann lathing contracts is superior to that of Benton, as assignee. However, as Hofmann did not appeal from that portion of the judgment awarding Benton $4,415.80 against Hofmann, such award must stand.

Although the court's finding that Hofmann was entitled against Benton to the proceeds of the 'Capwell Store' Hofmann-Coelho lathing contract was based upon a different theory than the nonassignability of the moneys under that contract, and such ****274** theory may have been incorrect, the result was correct, as, because of the nonassignability clause, Hofmann had the superior right to those moneys.

For the same reason the question of the appropriateness of the court's allowing certain set-offs against Benton in favor of Hofmann of moneys it found due from Coelho to Hofmann, has become moot.

3. THE EDEN OFFICE BUILDING.

On what is known as the Eden Office Building, upon which Coelho did the lathing under a subcontract with Hofmann, there was a balance unpaid to Coelho of $6,617.89. This balance Hofmann refused to pay because the County of Alameda for whom the work was being done claimed that the plastering did not comply with the specifications, and refused to pay the general contractor, who in turn refused to pay Hofmann. There is a conflict in the evidence as to whether the fault was that of Coelho or of Hofmann, although there is strong evidence that the fault was Coelho's. It is not necessary to discuss this evidence for the reason that in a meeting at which Benton was present, with Coelho, Hofmann, and representatives of the county and of the general contractor, Hofmann and Coelho waived any right to receive additional payments in consideration of acceptance of the defective building by the county. At this meeting, when asked if he had any objections to the compromise, Benton made no reply. ***70** The court concluded that this compromise agreement 'was in effect a new contract between the parties, and that the so-called 'fruits' of the contract never became due to Hofmann or to Coelho, hence plaintiff, as assignee of Coelho, is entitled to recover nothing' from the Eden Office Building job.

The court's conclusion must be affirmed for two reasons: (1) As we have heretofore shown, the assignment of the proceeds of the contract by Coelho to Hofmann is superior to the assignment to Benton. Hence Hofmann had the right to make the compromise. An obligor who has accepted an assignment of the money due under a construction contract may settle a claim under the contract by accepting a lesser sum in settlement. The 'anticipatory debtor may * * * do whatever reasonably appears to be necessary to enable the assignor to perform the contract.' (Peden Iron & Steel Co. v. McKnight (1910), 60 Tex.Civ.App. 45, 128 S.W. 156.) (2) Even if the assignment by Coelho to Benton granted the latter any interest in the proceeds of the Eden contract, Benton's acquiescence, by silence, in the compromise bars him from now contending that he is not barred by it. Benton had a great interest in Coelho's continued solvency. Without

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

a compromise of this type, Coelho was faced with a lawsuit to prove that the defective work was not his fault, or with considerable expense to repair the work, neither of which Coelho could afford. Although Benton contends that he had no duty to reply when asked if he had any objections to the compromise, his conduct led Coelho and Hofmann into a trap, and they reasonably had the right to assume and did assume that Benton's silence constituted consent. Both Coelho and Hofmann acted to their detriment in reliance upon Benton's failure to object. Thereby, by his failure to object, Benton waived any objection that he might have had.

4. THE DEED OF TRUST.

On November 14, 1957, Coelho and his wife signed a deed of trust conveying to a title company, as trustee, certain real property in Alameda County as security for the advances made by Benton under the December 21, 1953, Benton-Coelho agreement. The court found 'that plaintiff represented and promised defendants Alvin G. Coelho and Anita K. Coelho that if the said deed of trust were executed and delivered to plaintiff, plaintiff would continue to finance Coelho on his lathing jobs; that it is also true that at the time of making said representation and promise, plaintiff did not intend to keep his promise and did not intend to continue ***71** financing Coelho and ****275** that shortly thereafter plaintiff refused to continue financing Coelho.' In its conclusions, the court stated 'that the execution and delivery of the deed of trust were vitiated by plaintiff's false promise and plaintiff is not entitled to foreclose said deed of trust.'

Benton contends that neither the pleadings nor the evidence support these findings. Both contentions are unfounded. In the Coelho cross-complaint Coelho alleged 'that there was no proper execution acknowledgement or delivery of said instrument and *further that said defendants were coerced into signing said instrument by said plaintiff*.' (Emphasis added.) The court, both in its pretrial order and in its findings of fact, found that there was due execution and delivery of the instrument. It is the consideration for its execution and delivery with which we are concerned. In addition to the allegation in the cross-complaint that the instrument was obtained by coercion, the pretrial order states, 'There is the further issue of the validity of the deed of trust.' During the trial, the court granted Coelho's motion to amend to conform to the proof 'in that there was either no consideration given by plaintiff Benton for the Deed of Trust, or if consideration was given there was a failure of consideration by Plaintiff Benton.' Thus it is clear that the pleadings support the findings.

Benton points out that while the court granted leave to amend, no formal amended pleadings were filed, and contends that therefore the amendment allowed may not be considered. His contention is hypertechnical and is not supported by the decisions. The Supreme Court stated in Campagna v. Market St. Ry. Co. (1944), 24 Cal.2d 304, 308, 149 P.2d 281, 283: 'As a general rule, an order granting leave to amend is not an amendment, and in the absence of a written statement of facts concerning the issue, it is not properly pleaded. Central Cal. Creditor's Ass'n v. Seeley, 91 Cal.App. 327, 267 P. 138. But when such a motion is granted during the trial, and the case is tried as if the amendment had been made, a party may not later complain that no formal amendment was filed. [Citations.]'

The court in Campagna commented on the wide discretion which a trial court has to allow amendments to conform to proof, and in view of the presence of the issue of the validity of the deed of trust in the pretrial order, this discretion was wisely exercised in the instant case, and the issue of failure of consideration (continued financing) was properly before the trial court.

***72** Turning to the evidence, while the testimony of Benton to the effect that the deed of trust was given him to secure the advances he had made, conflicts with that of the Coelhos, the court apparently believed the latter and resolved the conflict in their favor. We are bound by that determination, as there is substantial evidence to support it. According to Mrs. Coelho Benton threatened to terminate his financial backing of the lathing contracts if she did not sign the deed of trust. Benton told her he only wanted it to prevent creditors from reaching the Coelho home. He stated to her, 'if I didn't sign it, he wouldn't go on, *but, if I signed, then he would go on and continue to finance until the jobs were pulled out*.' (Emphasis added.) The other testimony in general relates to Benton's statements that he would *not* finance the lathing contracts if Mrs. Coelho refused to sign. The quoted statement alone is sufficient to support the findings. Mrs. Coelho testified that she would not have signed the deed of trust without such representations and promises. It is admitted that Benton ceased financing Coelho shortly thereafter.

While there is no direct evidence that Benton, at the time of his representations to the Coelhos, did not intend to carry out his promises, the court was entitled reasonably to infer from all the facts and circumstances that he had no intention of doing so. A promisor who does not mean what he says seldom reveals his true state of mind. That must be determined by the ****276** trier of fact from what the promisor does under all the circumstances of the case. (See Cox v. Klatte (1938), 29

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Cal.App.2d 150, 84 P.2d 290.) Benton received profits from the Coelho lathing contracts until January, 1958. At that time Benton ceased advancing moneys to Coelho, although several jobs were still in progress and required financing in order to be completed. There is evidence that both Benton's and Coelho's losses on the entire transaction were due to Benton's ceasing to advance further moneys, and Coelho's inability to otherwise finance himself. Coelho, in several instances, was forced to abandon his lathing contracts for this reason. Even partial failure of consideration is a defense to foreclosure of a mortgage or deed of trust. (Briggs v. Crawford (1912), 162 Cal. 124, 129, 121 P. 381.)

Benton interprets the findings and conclusion above mentioned as findings of fraud and claims that no fraud was alleged and hence these findings are improper. Technically, Benton may be correct in that the findings might be susceptible to such interpretation. However, the facts upon which ***73** they are based show, and the findings and conclusion may reasonably be interpreted as determining, that there was a failure of consideration for the execution of the deed of trust. As Judge Murphy said in his memorandum opinion, 'Benton represented to the Coelhos, and particularly Mrs. Coelho, that if the deed of trust were executed and delivered, he would continue to finance Coelho on his jobs. Within a short time thereafter he refused to continue financing Coelho and Coelho was compelled to abandon his business as a lathing contractor.'

5. FINDINGS.

Benton objects to finding II dealing with the ninth cause of action, the count in which Benton sought recovery from Coelho of $72,194.83 and foreclosure of the deed of trust. This finding is to the effect that under the terms of the agreement between Benton and Coelho, Benton agreed to finance Coelho in the performance of the lathing contracts. Actually, as Benton points out, there is no promise made by Benton to make advances, in the agreement, the agreement being unilateral in that respect. However, such finding is immaterial. The court nowhere bases its judgment upon any assumption that Benton was required *under the contract* to continue making advances. It did find that the deed of trust was obtained under representations by Benton that he would continue to finance Coelho. There is no conflict between the two findings and the fact that the first finding is unsupported is immaterial.

Finding XIII is to the effect that the Benton-Coelho agreement did not provide for a continuing obligation on the part of Coelho to repay all moneys advanced, and that 'it is not true that defendant Coelho acted with intent to defraud plaintiff with respect to the amounts of payroll furnished to various lathing jobs from moneys advanced by plaintiff.'

Benton's objection to the first part of this finding is that the court failed to find either that there was or was not an agreement, implied by law, that Coelho would repay all advances. Such a finding was unnecessary. Where, as here, the court found that there was an express agreement as to the method of payment, the law cannot imply a contract in the face of such express agreement.

As to the second part of the finding, it is true that at times Coelho used moneys advanced by Benton for a particular lathing contract to pay debts incurred on another contract, or other contracts. The trial judge's opinion gives the reason for ***74** finding that in so acting Coelho did not intend to defraud Benton. Under the agreement any losses Benton suffered were to be recouped from other jobs. The instances in which Coelho used moneys from one job to offset losses on another, caused no net loss to Benton on the total for all the jobs. Moreover, that Benton acquiesced in this type of action is shown, as stated by the court, by the fact that he continued for approximately two to three months after ****277** knowledge, to finance the jobs. The court made no finding as to the amounts of the payments in this category. In view of the court's determination of the subject, there is no necessity for such a finding, as the amount of such advances is immaterial.

The other findings or their subject matter objected to by Benton have been discussed elsewhere herein.

The judgment is affirmed.

SULLIVAN, J., and AGEE, J. Assigned, concur.

All Citations

207 Cal.App.2d 61, 24 Cal.Rptr. 268

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Footnotes

1 This cross-complaint was dismissed by Coelho.

2 Coelho orginally contended that the agreement was one of partnership between Benton and himself. This contention was abandoned at the trial.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-6

Black's Law Dictionary (11th ed. 2019), assignment

ASSIGNMENT

Bryan A. Garner, Editor in Chief

Preface | Guide | Legal Maxims | Bibliography

assignment (14c) **1.** The transfer of rights or property <assignment of stock options>.

> "An *assignment* is a transfer or setting over of property, or of some right or interest therein, from one person to another; the term denoting not only the *act* of transfer, but also the instrument by which it is effected. In these senses the word is variously applied in law." Alexander M. Burrill, *A Treatise on the Law and Practice of Voluntary Assignments for the Benefit of Creditors* § 1, at 1 (James Avery Webb ed., 6th ed. 1894).

> "Negotiability differs from assignment, with which it has obvious affinities, in at least two respects. In the first place no notice need be given of the transfer of a negotiable instrument, and in the second place the transfer of such an instrument is not subject to equities. Thus whereas an assignor only transfers his rights subject to any defences which could be pleaded against him, a transfer of a negotiable instrument to someone in good faith passes a good title, free from any such defences. For instance a person who receives a cheque in good faith obtains a good title, even though the cheque may have been stolen. It is not, of course, any document which has the attributes of negotiability. Only those documents recognized by the custom of trade to be transferable by delivery (or endorsement) are negotiable. Other documents can only be transferred by assignment." P.S. Atiyah, *An Introduction to the Law of Contract* 278–79 (3d ed. 1981).

- **absolute assignment.** (18c) An assignment that leaves the assignor no interest in the assigned property or right. Cf. *partial assignment*.
- **assignment by operation of law.** (18c) A transfer of a right or obligation as a necessary consequence of a change in legal status, regardless of the affected party's intent. • For example, a right and a corresponding obligation may disappear if they vest in the same person, as might happen in a merger or acquisition.
- **assignment for the benefit of creditors.** See ASSIGNMENT FOR THE BENEFIT OF CREDITORS.
- **assignment for value.** (18c) An assignment given in exchange for consideration.
- **assignment in gross.** (1890) A transfer of a company's trademark separately from the goodwill of the business. • Courts often hold that such an assignment passes nothing of value to the transferee. — Also termed *naked assignment.* See ANTI-ASSIGNMENT-IN-GROSS RULE.
- **assignment of account.** (1808) An assignment that gives the assignee the right to funds in an account, usu. to satisfy a debt.
- **assignment of application.** (1896) **1.** *Patents.* The U.S. Patent and Trademark Office's formal routing of a patent or trademark application to the examining group to which it appears to belong based on subject matter. **2.** The transfer of the right to prosecute a patent or register a trademark. • The assignee must show ownership in the property to be patented or registered and, if less than absolute, the extent of ownership. *See* 37 CFR § 3.73.
- **assignment of dower** (**dow**-ər) (17c) The act of setting apart a widow's share of her deceased husband's real property.
- **assignment of easement.** (1896) An assignment by which an easement-holder transfers the easement to a third party.
- **assignment of income.** See *assignment of wages*.
- **assignment of lease.** (17c) An assignment in which a lessee transfers the entire unexpired remainder of the lease term, as distinguished from a sublease transferring only a portion of the remaining term.
- **assignment of mortgage.** (18c) An assignment by which a mortgage-holder transfers the mortgage to a third party.
- **assignment of note.** (1818) An assignment by which the holder of a promissory note transfers the note to a third party.
- **assignment of note and mortgage.** (1902) An assignment transferring both a promissory note and the mortgage that secures it.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

- **assignment of realty.** (1846) A transfer of a real-property interest that is less than a freehold. • The term includes debt-security interests in land.
- **assignment of wages.** (1836) A transfer of the right to collect wages from the wage earner to a creditor. — Also termed *assignment of income.*
- **assignment pro tanto.** (18c) An assignment that results when an order is drawn on a third party and made payable from a particular fund that belongs to the drawer. • The drawee becomes an assignee with respect to the drawer's interest in that fund.
- **bail assignment.** See BAIL ASSIGNMENT.
- **collateral assignment.** (18c) An assignment of property as collateral security for a loan.
- **common-law assignment.** (1824) An assignment for the benefit of creditors made under the common law, rather than by statute.
- **conditional assignment.** (18c) An assignment of income (such as rent payments or accounts receivable) to a lender, made to secure a loan. • The lender receives the assigned income only if the assignor defaults on the underlying loan.
- **effective assignment.** (1838) An assignment that terminates the assignor's interest in the property and transfers it to the assignee.
- **equitable assignment.** (18c) **1.** An assignment that, although not legally valid, will be recognized and enforced in equity — for example, an assignment of a chose in action or of future acquisitions of the assignor. • To accomplish an "equitable assignment," there must be an absolute appropriation by the assignor of the debt or fund sought to be assigned. **2.** An assignment that is valid and enforceable under the principles of fairness and justice.
- **fly-power assignment.** A blank written assignment that, when attached to a stock certificate, renders the stock transferable.
- **foreign assignment.** (18c) An assignment made in a foreign country or in another jurisdiction.
- **general assignment.** (18c) Assignment of a debtor's property for the benefit of all the assignor's creditors, instead of only a few. — Also termed *voluntary assignment.* See ASSIGNMENT FOR THE BENEFIT OF CREDITORS.
- **gratuitous assignment.** (18c) An assignment not given for value; esp., an assignment given or taken as security for — or in total or partial satisfaction of — a preexisting obligation.
- **legal assignment.** (17c) An assignment that meets all the statutory requirements and is enforceable by law.
- **mesne assignment** (meen) (18c) A middle or intermediate assignment; any assignment before the last one.
- **naked assignment.** See *assignment in gross*.
- **partial assignment.** (18c) The immediate transfer of part but not all of the assignor's right. Cf. *absolute assignment*.
- **preferential assignment.** See PREFERENTIAL TRANSFER.
- **total assignment.** (18c) An assignment empowering the assignee to enforce the entire right for the benefit of the assignor or others. • Examples are assignment to secure an obligation and assignment to a trustee.
- **voluntary assignment.** See *general assignment*.
- **wage assignment.** (1911) An assignment by an employee of a portion of the employee's pay to another (such as a creditor).

2. The rights or property so transferred <the aunt assigned those funds to her niece, who promptly invested the assignment in mutual funds>. **3.** The instrument of transfer <the assignment was appended to the contract>. **4.** A welfare recipient's surrender of his or her rights to child support (both current and past due) in favor of the state as a condition of receiving governmental financial assistance <the assignment made economic sense to her because her child support amounted to $200 a month, while she received $400 a month in welfare>. **5.** A task, job, or appointment <the student's math assignment> <assignment as ambassador to a foreign country>.

- **intercircuit assignment.** (1956) The temporary appointment of a federal judge in one judicial circuit to serve in another circuit. • The Chief Justice of the United States has the statutory authority to assign judges temporarily to assist courts in other circuits that have excessive workloads. The Judicial Conference Committee on Intercircuit Assignments, consisting of three federal judges, maintains a roster of senior and active judges who have volunteered to accept assignments and advises the Chief Justice about which judges to appoint. Assignments are usu. brief, lasting from a few days to a few weeks.
- **intracircuit assignment.** (1961) The temporary appointment of a federal district judge to assist another district court within the same circuit. • The chief judge of the circuit authorizes temporary transfers among courts within the circuit.

6. The act of assigning a task, job, or appointment <the assignment of various duties>.

- **assignment of the floor.** *Parliamentary law.* The process by which the chair recognizes who is entitled to speak.

7. In litigation practice, a point that a litigant advances <the third assignment of error>.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

- **assignment of error.** See ASSIGNMENT OF ERROR.
- **new assignment.** *Hist*. A plaintiff's restatement of a claim because the first complaint did not contain sufficient details. • The purpose was to allow a plaintiff to reply to a defendant's responsive plea that did not address the plaintiff's specific claim because the complaint was too general. New assignment has been replaced by amended pleadings. — Also termed *novel assignment.*

> "A new assignment is a restatement in the replication of the plaintiff's cause of action. Where the declaration in an action is ambiguous and the defendant pleads facts which are literally an answer to it, but not to the real claim set up by the plaintiff, the plaintiff's course is to reply by way of new assignment; that is, to allege that he brought his action, not for the cause supposed by the defendant, but for some other cause, to which the plea has no application." Benjamin J. Shipman, *Handbook of Common-Law Pleading* § 214, at 370 (Henry Winthrop Ballantine ed., 3d ed. 1923).

Westlaw. © 2019 Thomson Reuters. No Claim to Orig. U.S. Govt. Works.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-7

223 Cal.App.4th 831
Court of Appeal, Fourth District, Division 1, California.

BREWER CORPORATION et. al., Plaintiffs and Respondents,
v.
POINT CENTER FINANCIAL, INC., Defendant and Appellant.

D061665
|
Filed January 31, 2014
|
As Modified on Denial of Rehearing February 27, 2014
|
Review Denied April 30, 2014

Synopsis

Background: Construction contractors brought action against construction lender for liability on bonded stop notices. The Superior Court, San Diego County, No. 37–2007–74230–CUBC–CTL, William R. Nevitt, Jr., J., entered judgment for contractors and awarded costs, prejudgment interest and attorneys' fees pursuant to statute. Lender appealed.

Holdings: The Court of Appeal, McIntyre, J., held that:

stop notice claims took precedence over lender's prepayment to itself of interest, a loan fee, and other fees from construction loan funds;

stop notice claims took precedence over disbursements of interest to third party investors; but

contractor was required to serve preliminary notice on lender as condition of stop notice claim; but

contractor's failure to serve notice of commencement of action did not preclude recovery under stop notice.

Affirmed in part, reversed in part, and remanded.

Procedural Posture(s): On Appeal; Judgment; Motion to Enter Judgment; Other; Motion for Reconsideration; Motion to Renew; Motion in Limine.

****558** APPEAL from a judgment of the Superior Court of San Diego County, William R. Nevitt, Jr., Judge. Affirmed in part, reversed in part and remanded. (Super.Ct. No. 37–2007–74230–CUBC–CTL)

Attorneys and Law Firms

Fox Johns Lazar Pekin & Wexler, Michael H. Wexler, R. Gordon Huckins and Dale A. Martin, for Defendant and Appellant Point Center Financial, Inc.

Marks, Finch, Thornton & Baird, Jason R. Thornton, Jon F. Gauthier and Christopher R. Sillari; Hoyt Law Firm and Kenneth C. Hoyt for Plaintiffs and Respondents Brewer Corporation and Division 8.

Lincoln, Gustafson & Cercos and Theodore R. Cercos for Plaintiff and Respondent Brady Company/San Diego, Inc.

Niddrie Fish & Addams and David A. Niddrie for Respondents.

Law Offices of Murray M. Helm, Jr., and Murray M. Helm, Jr., for Respondent Dynalectric Company.

Opinion

McINTYRE, J.

***837** In this case, we are required to interpret several stop notice statutes. (Civ. Code, former §§ 3082–3267; Civ.Code, §§ 8000–9566, effective July 1, 2012 (Stats.2010, ch. 697, § 16). Unless otherwise indicated, undesignated statutory references are to the former sections of the Civil Code, which were in effect at all times material to this appeal, and references to the current sections of the Civil Code are designated by the word "current.") First, we conclude the trial court correctly followed *Familian Corp. v. Imperial Bank* (1989) 213 Cal.App.3d 681, 262 Cal.Rptr. 101 (*Familian*) when it held that a construction lender must make available to stop notice claimants those amounts the lender has already disbursed to itself on the construction loan.

We next conclude that the trial court correctly found that one stop notice claimant's failure to serve a preliminary 20-day notice (preliminary notice) under section 3097 prevented it from recovering under its bonded stop notice. Nonetheless, the judgment in favor of the stop notice claimant is

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

provisionally reversed and the matter remanded for further proceedings on a potentially dispositive factual issue.

Finally, we conclude that the trial court correctly found one stop notice claimant's failure to give the lender a notice of the commencement of the stop notice action under section 3172 did not bar the stop notice claimant from recovering where the lender suffered no prejudice.

FACTUAL AND PROCEDURAL BACKGROUND

Appellant Point Center Financial, Inc. (Lender), is a licensed real estate broker that facilitated the raising of construction loan funds for a condominium project (the project) located in San Diego, California, ****559** adjacent to Balboa Park. In 2006, the owner of the project borrowed $13,625,000 (the loan amount) from Lender to fund the remaining construction of the project (the construction loan). Lender agreed that it acted as a "[c]onstruction [l]ender" for purposes of the stop notice statutory scheme as this term is defined in section 3087. Under the terms of the construction loan, Lender was obligated to obtain about $2.8 million to close the transaction and agreed to use its best efforts to raise the balance of the loan amount in stages. Lender obtained the initial funds and disbursed them to the owner.

As Lender raised funds for subsequent stages of construction, it assigned portions of its beneficial interest in the construction loan trust deed to third-party investors. Lender entered into private loan servicing agreements with its third-party investors, by which it served as each investor's agent with regard to the construction loan. Lender paid the third-party investors interest on their ***838** fractional loan interest at a rate of 10 percent and charged a servicing fee of 1.5 percent. Significant to this action, under the private loan placement and fee agreements on each of these loans Lender prepaid itself interest, loan fee/points, loan underwriting and other fees—totaling $1,555,771.37. (As used in this decision, the term "prepaid" means that the Lender was paid before the stop notice claimants were paid in full on their claims.) The loan servicing agreements between Lender and the third-party investors were not recorded as a public record.

Lender contributed some of its own money to fund the construction loan, which resulted in it obtaining a 2.99 percent beneficial interest in the construction loan trust deed and promissory note. In connection with the construction loan, Lender raised and disbursed a total of $12,018,612.50. Lender never funded the remaining balance of the loan amount.

Respondents Brady Company/San Diego, Inc. (Brady), Dynalectric Company (Dynalectric), Division 8, Inc. (Division 8), and Brewer Corporation (Brewer, collectively Respondents) are contractors that provided labor, services, equipment and materials to the project. In June 2007, Brewer served on Lender its bonded stop notice. At that time, Lender was holding sufficient unexpended construction loan funds to cover the claim. Lender, however, did not withhold funds pursuant to Brewer's bonded stop notice claim. The parties agreed that Lender had stop notice liability stemming from its failure to withhold funds under Brewer's bonded stop notice claim.

By October 2007, Lender had fully disbursed all monies in the construction loan fund. Thus, when Lender received additional bonded stop notices from Brady, Dynalectric and Division 8 in March and April 2008, all construction loan funds held by it had already been disbursed.

Respondents filed individual actions against Lender, the owner and others; the trial court later consolidated these actions. All claims against the owner were stayed upon its bankruptcy filing. The bankruptcy court decided the priority of Respondents' mechanic's lien claims. The sole issue before the trial court was Lender's liability with respect to Respondents' bonded stop notice claims. Specifically, Respondents cited section 3166, which prohibited assignments, before or after receipt of a stop notice, and *Familian, supra,* 213 Cal.App.3d 681, 262 Cal.Rptr. 101 which holds that "[l]enders cannot avoid a section 3166 priority by private agreement." (*Id.* at p. 686, 262 Cal.Rptr. 101.)

Relying on *Familian,* the trial court determined that Respondents' stop notice claims took precedence over Lender's alleged contractual right to pay itself all interest, loan fees and other preallocated expenses. The trial court awarded Respondents a total of $1,555,771.37, which ****560** was then apportioned among them under section 3167. It further awarded Respondents costs, prejudgment interest and attorneys' fees pursuant to statute. The trial court ***839** also denied motions by Lender for entry of judgment against Dynalectric and Division 8 based on the alleged failure of these claimants to comply, respectively, with sections 3097 and 3172.

DISCUSSION

I. *General Legal Background*

A mechanic's lien is a claim against real property, which may be filed if a claimant has provided labor or furnished materials for the property and has not been paid. (*Kim v. JF Enterprises* (1996) 42 Cal.App.4th 849, 854, 50 Cal.Rptr.2d 141.) The mechanic's lien derives from the California Constitution and “courts have uniformly classified the mechanics' lien laws as remedial legislation, to be liberally construed for the protection of laborers and materialmen.” (*Connolly Development, Inc. v. Superior Court* (1976) 17 Cal.3d 803, 826–827, 132 Cal.Rptr. 477, 553 P.2d 637 (*Connolly*).) The mechanic's lien, however, lost its effectiveness when lenders began recording construction loan trust deeds before commencement of construction. (*Id.* at p. 827, 132 Cal.Rptr. 477, 553 P.2d 637.) The recorded construction loan trust deed is superior to any later recorded mechanic's lien; thus, if the lender forecloses on the property, the mechanic's lien has no value. (10 Miller & Starr, Cal. Real Estate (3d ed. 2012) § 28:68, p. 28-234 (rel. 12/2012).) “Even if the prior lien is not foreclosed, if the value of the property does not exceed the debt secured by the prior lien, there will be no equity in the property to secure the mechanic[']s liens.” (*Ibid.*)

The Legislature created the stop notice, now referred to as the stop payment notice, as an additional and cumulative remedy to protect laborers and materialmen. (*Connolly, supra,* 17 Cal.3d at p. 809, 132 Cal.Rptr. 477, 553 P.2d 637; current § 8044, subd. (c).) As our high court explained, “ ‘[l]abor and material contractors [in the construction industry] are in a particularly vulnerable position. Their credit risks are not as diffused as those of other creditors. They extend a bigger block of credit, they have more riding on one transaction, and they have more people vitally dependent upon eventual payment. They have much more to lose in the event of default. There must be some procedure for the interim protection of contractors in this situation.’ ” (*Connolly,* at p. 827, 132 Cal.Rptr. 477, 553 P.2d 637.)

After giving a 20-day preliminary notice (§ 3160), a laborer or materialman may serve a stop notice upon the owner or the construction lender. (§§ 3158, 3159.) A timely served stop notice obligates the owner or lender to withhold funds for the benefit of the stop notice claimant. (10 Miller & Starr, Cal. Real Estate, *supra,* § 28:74, pp. 28-248–28-249 (rel. 12/2012).) Once a stop notice is timely served on an owner or lender, an action to enforce the stop notice must be commenced within 90 days of the ***840** deadline to serve the stop notice, regardless of whether the stop notice was served early. (§ 3172.) The party who received the timely stop notice is required to withhold funds in the amount of the stop notice until the expiration of the claimant's deadline to file an action to enforce the stop notice, plus five additional days for receipt of a notice of commencement of the action under section 3172. (§ 3172.) If several stop notices have been filed and not enough money exists to pay them all, stop notice claimants share pro rata in the available funds. (§ 3167.) If a lender fails to withhold funds required by the bonded stop notice, it is personally liable to the claimant for the full amount of the claim. (*Connolly, supra,* 17 Cal.3d at p. 809, 132 Cal.Rptr. 477, 553 P.2d 637.)

****561** II. Familian *Issue*

A. Background

A stop notice claimant obtains priority over any “assignment” of the construction loan funds, whether the assignment is made before or after a stop notice is served. (§ 3166.) In *A–1 Door & Materials Co. v. Fresno Guarantee Sav. & Loan Ass'n* (1964) 61 Cal.2d 728, 40 Cal.Rptr. 85, 394 P.2d 829 (*A–1 Door*), our high court interpreted subdivision (h) of Code of Civil Procedure former section 1190.1, the statutory predecessor to section 3166. (*A–1 Door,* at pp. 731–732, 40 Cal.Rptr. 85, 394 P.2d 829; *Familian, supra,* 213 Cal.App.3d at p. 684, 262 Cal.Rptr. 101.) In *A–1 Door,* the contract between the lender and property owners required that the property owners assign the construction loan funds to the lender as security for their obligation to repay the loans and for any of their other obligations to the lender. (*A–1 Door,* at p. 735, 40 Cal.Rptr. 85, 394 P.2d 829.) When construction stopped, the lender retained the unexpended loan proceeds per its agreement with the property owners. (*Id.* at p. 731, 40 Cal.Rptr. 85, 394 P.2d 829.) Unpaid materialmen issued a stop notice and then sued the lender for enforcement. (*Ibid.*) The lender argued that there were no undisbursed funds to garnish because its contract with the property owners allowed it to retain possession of the funds. (*Id.* at pp. 733, 735, 40 Cal.Rptr. 85, 394 P.2d 829.) Our high court disagreed, concluding that the antiassignment provision in subdivision (h) of Code of Civil Procedure former section 1190.1 “require[d] that funds earmarked for construction purposes be used to pay suppliers of labor and materials who file claims under the subsection and therefore supersede[d]

the private arrangements of borrower and lender.” (*A–1 Door,* at p. 734, 40 Cal.Rptr. 85, 394 P.2d 829.)

In *Familian,* the court answered a question of first impression, whether a secured construction lender could defeat a bonded stop notice claimant's statutory priority to construction loan proceeds by segregating the fund into preallocated accounts and thereafter deducting charges and interest as accrued. (*Familian, supra,* 213 Cal.App.3d at p. 683, 262 Cal.Rptr. 101.) During construction, the ***841** lender paid itself for preallocated loan expenses including interest, loan fees, document preparation fees, and general and administrative expenses. (*Ibid.*) The lender then received stop notice claims greatly exceeding the remaining loan funds. (*Ibid.*) The lender foreclosed on the property and interpleaded the remaining loan funds, arguing that the laborers and materialmen were entitled to a pro rata share of this fund only. (*Ibid.*)

Interpreting section 3166, the *Familian* court rejected the lender's argument. It held that the preallocation of funds to pay points, interest and other nonconstruction costs constituted an assignment within the meaning of section 3166 that was subordinate to the perfected claims of laborers and materialmen. (****562** *Familian, supra,* 213 Cal.App.3d at pp. 686–687, 262 Cal.Rptr. 101.) It explained that “[s]ection 3166 does not prohibit [the lender's] practices; it simply assures priority to those who contribute the labor and materials to improve the property and increase the value of the lender's security.” (*Id.* at p. 687, 262 Cal.Rptr. 101.)

The *Familian* court then addressed the lender's argument that “a stop notice claimant's priority applie[d] only to ‘unexpended’ or ‘undisbursed’ loan funds” and that stop notice claimants were not entitled to priority for fees, points and interest incurred and paid to a lender before the borrower commenced work on the project as these funds had already been spent. (*Familian, supra,* 213 Cal.App.3d at p. 687, 262 Cal.Rptr. 101.) The court quickly rejected this contention stating: “[T]his argument seeks to engraft a loophole into section 3166. A construction lender would need only to deduct its profits at the inception of the loan to assure a double recovery at the expense of those who enhance the value of the property by supplying labor and materials.” (*Ibid.*) Accordingly, it held “that a preallocation of construction loan funds and periodic disbursements to the lender are assignments within the meaning of section 3166. Therefore, ‘whether made before or after a stop notice or bonded stop notice is given to a construction lender,’ the assignment does not take priority over the stop notice. (§ 3166.) Laborers and materialmen are entitled to retain the protection historically afforded under section 3166 just as lenders retain the right to foreclose on their security interest in the property, including its enhanced value as a result of the construction.” (*Familian,* at p. 688, 262 Cal.Rptr. 101.)

B. Analysis

Lender contends that *Familian* was wrongly decided and should be rejected. Alternatively, it asserts we should not follow *Familian* as the facts are distinguishable. Finally, it claims that the trial court went beyond the *Familian* facts and holdings. We address each contention, in turn.

***842** 1. *Familian* Is Not Legally Flawed

Section 3166 stated: “ ‘No assignment by the owner or contractor of construction loan funds, whether made before or after a stop notice or bonded stop notice is given to a construction lender, shall be held to take priority over the stop notice or bonded stop notice, and such assignment shall have no effect insofar as the rights of claimants who give the stop notice or bonded stop notice are concerned.’ ” The *Familian* court held “that a preallocation of construction loan funds and periodic disbursements to the lender” constituted assignments within the meaning of section 3166. (*Familian, supra,* 213 Cal.App.3d at p.688, 262 Cal.Rptr. 101.) The trial court followed the *Familian* court's interpretation of the word “assignment” in rendering judgment for the stop notice claimants. Thus, we too are called upon to interpret the meaning of an assignment as used in section 3166.

This presents a question of law subject to de novo review. (*Bialo v. Western Mutual Ins. Co.* (2002) 95 Cal.App.4th 68, 76–77, 115 Cal.Rptr.2d 3.) The objective of statutory interpretation is to ascertain and effectuate legislative intent. (*Burden v. Snowden* (1992) 2 Cal.4th 556, 562, 7 Cal.Rptr.2d 531, 828 P.2d 672.) We examine the words of the statute, giving them a plain and commonsense meaning, the entire substance of the statute, and consider the statutory framework as a whole. (*People v. Murphy* (2001) 25 Cal.4th 136, 142–143, 105 Cal.Rptr.2d 387, 19 P.3d 1129.) Where the statutory language in dispute is clear and unambiguous, there is no need for construction and we should not indulge in it. (*California Fed. Savings & Loan Assn. v. City of Los Angeles* (1995) 11 Cal.4th 342, 349, 45 Cal.Rptr.2d 279, 902 P.2d 297.) “Only when the language of a statute is susceptible to more than one reasonable construction is it appropriate to turn to extrinsic aids, including the legislative history of the measure, to ascertain its meaning.” (*Diamond Multimedia Systems,*

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Inc. v. Superior Court (1999) 19 Cal.4th 1036, 1055, 80 Cal.Rptr.2d 828, 968 P.2d 539.) The separation of powers doctrine requires that we "limit ourselves to interpreting the law as written and leave for the ... Legislature the task of revising it as [it might] deem wise." (****563** *People v. Garcia* (1999) 21 Cal.4th 1, 14–15, 87 Cal.Rptr.2d 114, 980 P.2d 829; Cal. Const., art. III, § 3.)

An assignment is defined as a "transfer of rights or property." (Black's Law Dict. (9th ed. 2009) p. 136.) Here, the full amount of the loan was for the purpose of "fund[ing] the subject construction project." The parties, however, agreed that Lender could prepay itself interest, a loan fee and other fees. This agreement amounts to a transfer of rights over the construction loan funds from the borrower to Lender and constituted an assignment.

***843** Lender does not acknowledge this inescapable conclusion; rather, it contends that disbursements to itself are not assignments because the disbursements were simply the means by which the borrower performed its contractual obligation to pay interest and other items of bargained-for consideration to Lender. This argument confuses the assignment (i.e., the agreement between the parties) with the act of carrying out the assignment (i.e., disbursing the construction loan funds). Taking Lender's argument to its logical conclusion, Lender appears to assert that contractual language allowing it to disburse some of the construction loan funds to itself can never constitute an assignment. This result is contrary to the entire purpose of section 3166, which was to supersede the private arrangements of the borrower and lender to ensure that construction loan funds "earmarked for construction purposes be used to pay [suppliers of labor and materials that file claims under section 3166]." (*A–1 Door, supra,* 61 Cal.2d at p. 734, 40 Cal.Rptr. 85, 394 P.2d 829.) Moreover, Lender's argument makes the existence of an assignment dependent upon *when* it removed money from the construction loan funds. As Respondents note, construction loan agreements preallocating some of the construction loan funds back to a lender are drafted before construction loan funds are disbursed; thus, a lender can control when funds are expended or earned. ****564**

Lender presents lengthy arguments explaining why money it has already removed from the construction loan funds pursuant to its agreement with the borrower are unavailable to stop notice claimants. It notes that sections 3159 and 3162 required that a construction lender withhold sufficient funds when a bonded stop notice was filed. Section 3167 provided that if the money withheld was insufficient to pay any valid claims in full, that the funds would be distributed on a pro rata basis. Lender asserts that when section 3166 is construed in the context of the entire statutory scheme, particularly the withholding provisions of sections 3159, 3162 and 3167, that section 3166 disallowed an assignment only if the assignment reduced the *unexpended* funds available to satisfy a stop notice claim. In other words, it could not "withhold" funds that had already been disbursed based on an assignment.

While Lender's argument has superficial appeal, its proposed construction defeats the purpose of the stop notice procedure. The Legislature created the stop notice law to give laborers and materialmen priority over lenders to payment from the construction loan fund. (*Connolly, supra,* 17 Cal.3d at p. 827, 132 Cal.Rptr. 477, 553 P.2d 637.) A lender could simply draft the construction loan agreement to provide that all interest, fees, points or other costs were due before work started on a project. As our high court sagely noted when it interpreted the predecessor statute to section 3166 (Code Civ. Proc., former § 1190.1, subd. (h)), if the terms of the construction loan agreement determined the rights of stop notice claimants "the parties to the contract could effectively eliminate those rights." (*A–1 Door, supra,* 61 Cal.2d at p.734, 40 Cal.Rptr. 85, 394 P.2d 829.) The *Familian* ***844** court recognized this, stating such an interpretation would allow lenders and borrowers to "engraft a loophole into section 3166." (*Familian, supra,* 213 Cal.App.3d at p. 687, 262 Cal.Rptr. 101.) "A construction lender would need only to deduct its profits at the inception of the loan to assure a double recovery at the expense of those who enhance the value of the property by supplying labor and materials." (*Ibid.*)

Lender is correct that cases decided before *Familian* involved claims against unexpended funds. (*Calhoun v. Huntington Park First Savings & Loan Assoc.* (1960) 186 Cal.App.2d 451, 455, 9 Cal.Rptr. 479; *Rossman Mill & Lumber Co. v. Fullerton Savings & Loan Assoc.* (1963) 221 Cal.App.2d 705, 708, 34 Cal.Rptr. 644; *A–1 Door, supra,* 61 Cal.2d at pp. 731–732, 40 Cal.Rptr. 85, 394 P.2d 829; *Miller v. Mountain View Savings & Loan Assoc.* (1965) 238 Cal.App.2d 644, 649–650, 651, 652, fn. 5, 48 Cal.Rptr. 278.) That the *Familian* court decided an issue of first impression does not render its result suspect. As one commentator noted, "[b]ecause the stop notice remedy is so highly effective for stop notice claimants, construction lenders have made several attempts over the years to structure a construction loan that effectively circumvents it." (Campbell, Stop Notice Risks for Construction Lenders (Jan. 2010) L.A. Law., at p. 18.)

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Lender argues that part of the money preallocated and disbursed to it under the terms of the construction loan agreement was "earned," meaning the money constituted reimbursements for out-of-pocket costs and expenses associated with locating lenders, raising funds, paying salaries, etc. It also argues that "the funds paid to [it] and the private party lenders were used to satisfy legitimate costs of construction." Lender's contention is supported by one commentator who advocates for a more "tailored approach" that "unearned prepayments, if proved as a matter of fact, do not qualify as sums earned and paid before receipt of the bonded stop notice, and do not reduce the fund available to the stop notice claimant." (Soffer, *Policy Considerations Trump Statutory Construction, Giving Stop Notice Claimants a Big Advantage Over Construction Lenders* (Nov. 2009)20 Miller & Starr: Real Estate Newsalert 85, 92–93, italics omitted.) On the other hand, Respondents suggest that all distributions to Lender out of the construction loan fund were "unearned," meaning they constituted profits. The parties concede, however, that the issue whether the distributions Lender received were earned or unearned was never argued below. As the case was not tried on this theory, it is impossible for us to address it.

In any event, we conclude that labeling the disbursements Lender received as earned versus unearned is of little consequence. Our high court made it clear in *Connolly,* over 36 years ago, that monies in a construction loan fund are intended to pay construction costs. (*Connolly, supra,* 17 Cal.3d at pp. 807, 820, 825, 132 Cal.Rptr. 477, 553 P.2d 637.) It held that a construction loan fund is "not available ***845** for ordinary expenses." (*Id.* at p. 820, 132 Cal.Rptr. 477, 553 P.2d 637.) Additionally, when served upon the construction lender a stop notice "attaches only to funds previously committed to finance construction of the improvement (§ 3162)." (*Id.* at p. 826, 132 Cal.Rptr. 477, 553 P.2d 637.) Here, the parties agreed in the joint trial readiness conference report that the full amount of the loan was for the purpose of "fund[ing] the subject construction project." Although Lender argued in its reply brief that "the funds paid to [it] and the private party lenders were used to satisfy legitimate costs of construction," it cited absolutely no evidence to support this statement.

****565** Finally, it is worth noting that the *Familian* court did not invalidate the preallocation of construction loan funds by lenders. Lenders remain free to draft construction loan agreements to give themselves a contractual right to priority. It is only in situations, such as the one presented here that lenders' contractual priority cedes to a stop notice claimants' statutory priority, allowing a court to reach back to funds a lender has disbursed to itself as a source to pay stop notice claimants.

2. *Familian* Is Not Distinguishable

Assuming we will follow the *Familian* analysis, Lender alternatively argues that the judgment in favor of Respondents should be reversed based on the distinguishable facts of this case.

Lender first points out that in *Familian,* the lending bank foreclosed on its trust deed (*Familian, supra,* 213 Cal.App.3d at p. 683, 262 Cal.Rptr. 101); thus, it obtained a double recovery by obtaining the real property and that value added to the property by the stop notice claimants' improvements. In contrast here, the property was encumbered by a "super-priority" first trust deed that was foreclosed thereby wiping out the Lender's first trust deed. Accordingly, Lender asserts that it recovered nothing and was not unjustly enriched by the stop notice claimants' contributions to the project.

Stated differently, Lender asserts that the stop notice claimants should not be entitled to statutory priority under section 3166 because it suffered a loss, rather than a gain. We disagree as Lender's argument makes application of section 3166 priority dependent upon equitable principles. The Legislature eliminated the judicially developed equitable lien remedy and confined recovery to statutory mechanic's lien and stop notice procedures when it enacted section 3264. (*Sofias v. Bank of America* (1985) 172 Cal.App.3d 583, 586, 218 Cal.Rptr. 388.) The *Familian* court acknowledged the existence of section 3264 (*Familian, supra,* 213 Cal.App.3d at pp. 685–686, 262 Cal.Rptr. 101) and unequivocally held that "[l]enders cannot avoid a section 3166 priority by private agreement." (*Id.* at p. 686, 262 Cal.Rptr. 101.) Contrary to Lender's assertion, the theme ***846** in *Familian* was not the avoidance of unjust enrichment. Simply put, whether a lender forecloses on its trust deed or ultimately realizes a gain or loss is not relevant to application of section 3166.

Lender next claims that *Familian* is distinguishable because the lending bank segregated the funds to pay itself from the remainder of the loan funds by setting up preallocated accounts. While the *Familian* court articulated the issue presented as whether "a secured construction lender [can] defeat a bonded stop notice claimant's statutory priority to construction loan proceeds by segregating the fund into

preallocated accounts and thereafter deducting charges and interest as accrued," the segregation of the funds into different accounts did not factor into its analysis. (*Familian, supra,* 213 Cal.App.3d at p.683, 262 Cal.Rptr. 101.) Instead, the *Familian* court broadly held that "a preallocation of construction loan funds and periodic disbursements to the lender are assignments within the meaning of section 3166." (*Id.* at p. 688, 262 Cal.Rptr. 101.) Similarly here, the parties agreed that Lender could preallocate construction loan funds to pay interest and loan fees and disburse to itself the construction loan funds to pay accrued interest on the loan. Thus, the lack of segregated accounts does not distinguish the instant case from *Familian.*

Finally, Lender makes a number of arguments directed at specific portions of the trial court's award, contending that ****566** the trial court went beyond the facts and holding of *Familian.* Lender claims the trial court erred when it awarded Respondents the total amount of interest paid on the loan because it received a small interest payment and the third-party investors received the rest. Lender asserts we should reverse that portion of the judgment reflecting interest paid to the third-party investors, approximately $1,012,200. Lender's argument misses the point.

The purpose of section 3166 is to afford stop notice claimants priority over a construction lender's assignment of construction funds. (See *Familian, supra,* 213 Cal.App.3d at p. 687, 262 Cal.Rptr. 101.) The loan servicing agreements that Lender entered into with each of the third-party investors constituted another type of assignment. Under the loan servicing agreements Lender paid itself interest out of the construction loan funds and later disbursed the majority of the interest payments to the third-party investors. The fact Lender did not retain the interest payments is irrelevant to the *Familian* analysis. Additionally, we note that the loan servicing agreements contain an indemnity clause whereby each third-party investor agreed to indemnify Lender to the extent of the fractional interest of each third-party investor for any claims incurred by Lender not covered by insurance so long as Lender acted in good faith and without gross negligence or willful misconduct.

Lender also complains the trial court improperly awarded Respondents a loan servicing fee paid to Lender by the third-party investors in the amount of ***847** about $136,380. Lender claims that the third-party investors paid the fee. We reject this argument as it ignores that Lender was paid its loan servicing fee via monthly deductions from payments received from the owner. Next, Lender asserts the trial court improperly awarded Respondents $1,540 representing tax service and credit report charges because these amounts were reimbursements from the owner and not profits. The trial court made a finding that these charges should be part of the *Familian* award because they came out of the construction loan funds. It is irrelevant that Lender did not profit.

Lastly, Lender claims the trial court erred in awarding Respondents $19,500, representing the amount of fees paid to Lender by the owner in connection with a $390,000 supplemental loan to owner for the purpose of paying city permit fees, noting that the owner paid off the loan before the service of the first stop notice. We disagree. Trial testimony established that the owner paid Lender a loan fee of $476,875 at closing and that Lender later loaned $390,000 of the fee back to the owner to pay for permits required to allow the start of construction. The supplemental loan was secured by a trust deed on the same property enhanced by Respondents' labor, equipment and material. This evidence establishes that the loan was for the purpose of financing the construction of improvements on the property. Thus, the trial court properly included the loan fee from this supplemental loan as part of its *Familian* award.

III. *Dynalectric Issue*

Service of a preliminary 20-day notice is required to enforce a mechanic's lien or stop notice claim. (§ 3097, subds. (a)-(b) [a preliminary notice is "a necessary prerequisite to the validity of any claim of lien"].) A preliminary notice must be served within 20 days after the claimant has begun providing labor, services, equipment, or material for which a mechanic's lien or stop notice claim will be made. (§ 3097, subd. (d).) The Legislature imposed the notice requirement ****567** to alert property owners and lenders "to the fact that the property or funds involved might be subject to claims arising from contracts to which they were not parties and would otherwise have no knowledge." (*Romak Iron Works v. Prudential Ins. Co.* (1980) 104 Cal.App.3d 767, 778, 163 Cal.Rptr. 869.) The Legislature intended "to exact strict compliance with the preliminary notice requirement." (*Ibid.*; see *IGA Aluminum Products, Inc. v. Manufacturers Bank* (1982) 130 Cal.App.3d 699, 703–704, 181 Cal.Rptr. 859 [same].)

***848** Lender contends the trial court erred as a matter of law when it concluded that Dynalectric, a direct contractor, was not required to serve Lender with a preliminary notice

under subdivision (b) of section 3097 (section 3097(b)) as a condition to maintaining its stop notice claim because service of a preliminary notice by a stop notice claimant under a direct contract with the owner is required unless the claimant is the general contractor. Dynalectric asserts the plain language of subdivision (a) of section 3097 (§ 3097(a)) exempted it from serving a preliminary notice on Lender.

Dynalectric also contends we need not interpret section 3097 because, even if it was not exempt from the preliminary notice requirement under section 3097, it was not required to serve a preliminary notice on Lender because the undisputed facts establish it commenced work before Lender recorded its construction loan trust deed. In other words, Dynalectric contends it had a factual excuse for not serving a preliminary notice on Lender. (*Kodiak Industries, Inc. v. Ellis* (1986) 185 Cal.App.3d 75, 83–85, 229 Cal.Rptr. 418 [a private work lender stop notice claimant who commences work on a project before the construction loan trust deed is recorded is not required to serve the construction lender with a preliminary notice under § 3097] (*Kodiak*).) Assuming we agree with Dynalectric that the undisputed facts establish it commenced work before Lender recorded its construction loan trust deed, then Dynalectric claims the judgment in its favor can be affirmed on this alternative ground.

As we shall explain, we conclude the trial court erred as a matter of law when it concluded that Dynalectric was not required to serve Lender with a preliminary notice. We also conclude that the judgment in favor of Dynalectric should be provisionally reversed and the matter remanded to the trial court for an evidentiary hearing on the potentially dispositive factual excuse issue regarding when Dynalectric started work on the project. We first address the legal issue presented by the parties and then turn to the factual excuse issue.

A. Legal Issue

It is undisputed that Dynalectric was a contractor with a direct contract with the owner of the project and that it did not serve Lender with a preliminary notice. In a nutshell, Lender claims Dynalectric was required to serve a preliminary notice under section 3097(b) because it was a direct contractor and not an exempt general contractor. Dynalectric asserts the plain language of section 3097(a) exempted it from serving a preliminary notice on Lender and, when properly interpreted, it was also exempt under section 3097(b).

***849** In interpreting section 3097 we apply the general rules of statutory interpretation. (*Ante,* pt. II.B.1.) We start with the plain language of the statute. In relevant part, section 3097 provides that a preliminary notice must be given before filing a stop notice under the following circumstances:

> ****568** "(a) Except one under direct contract with the owner ... every person who furnishes labor, service, equipment, or material [to a work of improvement] shall, as a necessary prerequisite to the validity of any ... notice to withhold, cause to be given to the owner or reputed owner, to *the original contractor,* or reputed contractor, and to the construction lender, if any, or to the reputed construction lender, if any, a written preliminary notice as prescribed by this section.
>
> "(b) Except *the contractor*... all persons who have a direct contract with the owner and who furnish labor, service, equipment, or material [to a work of improvement] shall, as a necessary prerequisite to the validity ... of a notice to withhold, cause to be given to the construction lender, if any, or to the reputed construction lender, if any, a written preliminary notice as prescribed by this section." (Italics added.)

The term " '[o]riginal contractor' " used in section 3097(a) is defined as "any contractor who has a direct contractual relationship with the owner." (§ 3095.) The term "the contractor" used in section 3097(b) is not defined. Accordingly, "the contractor" must mean something different than an original contractor with a direct contractual relationship with the owner.

Taking the liberty to rearrange the wording of these subdivisions and substitute "any contractor who has a direct contractual relationship with the owner" for the term "original contractor," section 3097(a) states: every person who furnishes labor, etc. to a work of improvement, except one under direct contract with the owner, must give notice to a lender or any contractor who has a direct contractual relationship with the owner. In turn, section 3097(b) states: all persons having a direct contract with the owner that furnishes labor, etc., to a work of improvement, except the contractor, must give the notice to the lender. The subdivisions are plainly different. Section 3097(a) requires notice to a lender or any other contractors who have a direct contractual relationship with the owner, while section 3097(b) requires notice only to a lender.

We now take the rearranged subdivisions to determine whether Dynalectric, a person that furnished labor etc. through a direct contract with the owner, was required to

serve a preliminary notice on Lender under either section 3097(a) or (b). Plainly, and as conceded by Lender, section 3097(a) did not require such notice because Dynalectric had a direct contractual relationship with the owner. Thus, we turn to section 3097(b).

***850** Again, our rearranged section 3097(b) states: all persons having a direct contract with the owner that furnishes labor, etc. to a work of improvement, except the contractor, must give the notice to the lender. Dynalectric qualifies as a person having a direct contract with the owner; thus, it was required to give notice to the lender under section 3097(b) unless it qualified as "the contractor."

Interpreting the predecessor to section 3097, the court in *Korherr v. Bumb* (9th Cir., 1958) 262 F.2d 157, interpreted the term "the contractor" to refer to "the general or prime contractor." (*Id.* at p. 161.) Other courts have adopted this interpretation. (*Kodiak, supra,* 185 Cal.App.3d at p. 82, fn. 3, 229 Cal.Rptr. 418 [the contractor "has sensibly been construed to mean the general or prime contractor for the entire project"]; *Westfour Corp. v. California First Bank* (1992) 3 Cal.App.4th 1554, 1561, 5 Cal.Rptr.2d 394 [same]; *Shady Tree Farms v. Omni Financial* (2012) 206 Cal.App.4th 131, 138, 141 Cal.Rptr.3d 412 [same] (*Shady Tree*).) As ****569** noted by the *Shady Tree* court, section 3097(b) "refers to *the* contractor rather than *a* contractor. The use of 'the' indicates a single person, i.e., the prime or general contractor for the project, not multiple contractors, i.e., the subcontractors or others with direct contracts with the owner." (*Shady Tree, supra,* at p.138, 141 Cal.Rptr.3d 412.) Accordingly, as a person having a direct contract with the owner, Dynalectric was required to give notice to Lender under section 3097(b) because it was not the general or prime contractor on the project.

Recent amendments to the mechanic's lien laws support this interpretation. The Legislature indicated that the 2010 amendments were intended to, among other things, "recodify, reorganize, and clarify the mechanics lien statute; modernize terminology and eliminate inconsistencies in language; make provisions more readable and easier to use; enact separate provisions for private and public works; [and] modernize and streamline existing notice requirements." (Sen. Com. on Judiciary, Analysis of Sen. Bill No. 189 (2009–2010 Reg. Sess.), as amended Dec. 15, 2009 (Senare Committee on Judiciary Analysis); available at <http://www.leginfo.ca.gov/pub/09–10/bill/sen/sb_0151–0200/sb_189_cfa_20100111_183140_sen_comm.html> [as of Jan. 31, 2014].) The California Law Revision Commission "placed its highest priority on drafting a 'nonsubstantive reorganization of the existing mechanics lien statute that would modernize and clarify existing law.' " (*Id.* at p. 2.) The Legislature noted that section 3097(b) "contain[ed] an ambiguity relating to whether a general contractor must give preliminary notice to a construction lender on a private work." (Sen. Com. on Judiciary Analysis, at p. 4.) The bill clarified "that a general contractor must give preliminary notice to a construction lender on a private work." (*Ibid.*)

***851** Thus, the Legislature amended section 3097 to state that a claimant "shall give preliminary notice to the following persons: [¶] (1) The owner or reputed owner. [¶] (2) The direct contractor or reputed direct contractor to which the claimant provides work, either directly or through one or more subcontractors. [¶] (3) The construction lender or reputed construction lender, if any." (Current § 8200, subd. (a).) "Notwithstanding the foregoing subdivisions: [¶] (1) A laborer is not required to give preliminary notice. [¶] (2) *A claimant with a direct contractual relationship with an owner or reputed owner is required to give preliminary notice only to the construction lender or reputed construction lender, if any.*" (Current § 8200, subd. (e), italics added.)

Once again, our rearranged section 3097(b) states: all persons having a direct contract with the owner who furnish labor, etc., to a work of improvement, except the contractor, must give the notice to the lender. The ambiguity referred to in the Senate Judiciary Committee analysis is the reference to "the contractor" in section 3097(b) as this term was eliminated from the amended statute. (See current § 8200.) The current statute now provides that "[a] claimant with a direct contractual relationship with an owner or reputed owner is required to give preliminary notice only to the construction lender or reputed construction lender, if any." (Current § 8200, subd. (e)(2).) Just as the Legislature intended, the amended statute resolves the ambiguity in section 3097(b) by providing that any "direct contractor," including a general contractor, must serve a preliminary notice on the lender. (Sen. Com. on Judiciary Analysis, *supra,* at p. 4.) As further support for this conclusion, current section 8018 defines "[" '[d]irect contractor' " as "a contractor that has a direct contractual relationship with an owner. A reference in another statute to ****570** a 'prime contractor' in connection with the provisions in this part means a 'direct contractor.' "

In summary, the trial court erred when it concluded that Dynalectric was not required to serve a preliminary notice on Lender.

B. Factual Excuse Issue

1. Facts

Before trial, Lender moved for nonsuit or a partial judgment under Code of Civil Procedure section 631.8 to determine the validity of Dynalectric's stop notice claim on undisputed facts. Lender argued that, as a matter of law, Dynalectric was required to serve Lender a preliminary notice, and Dynalectric did not do so and was barred from pursuing a stop notice claim against ***852** Lender. In opposition to the motion, Dynalectric argued it was not required to serve Lender a preliminary notice because the plain language of section 3097(a) and 3097(b) exempted it from serving a preliminary notice on Lender. Dynalectric also asserted a factual defense that it was not required to serve a preliminary notice because there was no lender when it began work on the project.

At the hearing on the motion, Lender presented an oral reply to Dynalectric's opposition that addressed the legal issue, but not the factual issue of when Dynalectric began work on the project. Lender later admitted it "was nowhere on the scene" in 2004 when Dynalectric executed a letter of intent with the owner, but that the initial work Dynalectric did was of "no consequence" because it pertained to a "separate work of improvement." Lender claimed that another judge found that the "current work of improvement" started a few weeks before it recorded its trust deed in June 2006, that Dynalectric first started work under the contract in September 2006, and that Dynalectric prepared its preliminary notice 20 days after it started work, but never served Lender. Lender asserted that even if the court had "question of fact" regarding whether Dynalectric was excused from the preliminary notice requirement, it could still rule on the legal issue.

Thereafter, the trial court denied Lender's motion to find Dynalectric's stop notice claim invalid. The court later clarified that it ruled on the legal issue of whether Dynalectric was required to file a preliminary notice on Lender, not the factual issue. Lender filed a "Motion for Reconsideration of Prior Motion Re Dynalectric's Statutory Duty to Serve a Preliminary Notice on Point Center; for Renewal of Prior Motion as to Said Duty Issue; For Relief Based on Mistake, Inadvertence, Surprise or Excusable Neglect; For a Determination, as a Motion in Limine, that Dynalectric's Contention that it was Excused for Factual Reasons from Serving a Preliminary Notice on Point Center Raises a Triable Issue of Fact; and for Related Relief" (the reconsideration motion). Among other things, Lender explained during argument that its in limine motion requested that the trial court reserve for trial any determination on the factual issue regarding whether Dynalectric was excused from serving a preliminary notice on Lender. The trial court denied the reconsideration motion.

2. Analysis

In its opening brief, Lender focused exclusively on the trial court's ruling on the legal issue. Seizing on the fact Lender failed to argue the factual excuse issue as a basis for reversing the trial court's ruling, Dynalectric ***853** contends Lender presented no evidence showing the existence of a factual dispute regarding when Dynalectric started work on the project, that Lender had a full and fair opportunity to ****571** present such evidence and the trial court's ruling in Dynalectric's favor should be affirmed on the alternative ground that the undisputed facts show Dynalectric commenced work on the project before Lender recorded its construction loan trust deed. Alternatively, should we conclude that triable issues of fact remain unresolved, Dynalectric requests that we remand the matter for further proceedings.

The parties impliedly agree that a ruling on the factual excuse issue potentially moots the legal issue that we addressed above. (*Ante,* pt. III.A.) Our review of the record reveals, however, that Lender did not have the opportunity to present evidence on the factual excuse issue. Dynalectric raised the factual excuse issue in its opposition to Lender's motion and presented a declaration to support its argument. Lender provided an oral reply at the hearing on the motion. It asserted the court could rule on the legal issue even if factual questions existed regarding whether Dynalectric was excused from the preliminary notice requirement. After the trial court ruled in Dynalectric's favor on the legal issue, Lender filed its multifaceted reconsideration motion which argued that Dynalectric's factual excuse issue should be tried. Lender stated during oral argument on the reconsideration motion that it had a number of exhibits and witnesses to address the factual excuse issue. Although Dynalectric chides Lender for not presenting this evidence as part of its reconsideration motion, Lender was not required to do so because the court made no factual determination that was subject to reconsideration. Lender argued below that the factual excuse issue needed to be tried. Dynalectric agrees as it alternatively

argued on appeal that we could remand the matter for further proceedings.

Because the record reveals that the parties did not have a full and fair opportunity to litigate the potentially dispositive factual excuse issue, we decline to rule on whether Dynalectric had a factual excuse for not complying with the preliminary notice requirement. In the interest of justice, we provisionally reverse the judgment in favor of Dynalectric and remand the matter to the trial court with directions to hold an evidentiary hearing on when Dynalectric started work on the project. For purposes of this appeal, the provisional reversal means that on remand, Dynalectric and the lender are placed in the same positions and have the same rights as before rendition of the judgment. (*Hall v. Superior Court* (1955) 45 Cal.2d 377, 381, 289 P.2d 431.) If the trial court finds in favor of Dynalectric on the existence of a factual excuse for not serving a preliminary notice on Lender the judgment in favor of Dynalectric should be affirmed. Alternatively, if the trial court finds against Dynalectric on the existence of a factual excuse, the judgment in favor of Dynalectric should be reversed.

***854** IV. *Motion Regarding Division 8*

A. Facts

On April 10, 2008, Division 8 served Lender with its bonded stop notice and filed a complaint to foreclose its mechanic's lien on the project. In May 2008, Division 8 filed a first amended complaint which added a stop notice claim against Lender. In July 2008, Division 8 served its first amended complaint on Lender. Division 8, however, never served Lender with a notice of the commencement of its stop notice action within five days after filing its complaint as required by section 3172.

During trial, Lender orally moved under Code of Civil Procedure section 631.8 for entry of judgment against Division 8 for Division 8's failure to serve a notice of commencement of action under section 3172. The trial court considered a supplemental trial brief filed by Lender and heard oral argument. Upon conclusion of the argument, the trial court orally denied Lender's motion, finding that Division 8 substantially complied with the notice of ****572** commencement requirements and, even if it had not, that Lender was not prejudiced by Division 8's failure to serve the notice.

B. Analysis

An action to enforce a stop notice must be commenced between 10 and 90 days after filing of the stop notice. (§ 3172; current § 8550, subd. (a)-(c).) Commencement of the action within the 90-day period is a necessary step in perfecting a stop notice claimant's right to the funds held by the lender. If the action is filed late, the notice is no longer effective and the lender must release the funds previously held pursuant to the stop notice. (§ 3172; current § 8550, subd. (d).) Within five days after filing an action to enforce the stop notice, the claimant "shall" give notice of the commencement of the action to the same persons who have received the stop notice. (§ 3172; current § 8550, subd. (e).)

Lender contends the trial court erred when it refused to enter judgment in its favor based on Division 8's failure to ever serve a notice of the commencement of its stop notice action because the use of the word "shall" in the statute requires mandatory compliance. We disagree.

Again, we are faced with a question of statutory interpretation subject to de novo review. (*Bialo v. Western Mutual Ins. Co., supra,* 95 Cal.App.4th at pp. 76–77, 115 Cal.Rptr.2d 3.) "[T]here is no simple, mechanical test for ***855** determining whether a [statutory] provision should be given 'directory' or 'mandatory' effect." (*Morris v. County of Marin* (1977) 18 Cal.3d 901, 909, 136 Cal.Rptr. 251, 559 P.2d 606.) Generally, "requirements relating to the time within which an act must be done are directory rather than mandatory or jurisdictional, unless a contrary [legislative] intent is clearly expressed." (*Edwards v. Steele* (1979) 25 Cal.3d 406, 410, 158 Cal.Rptr. 662, 599 P.2d 1365.) "In ascertaining probable intent, California courts have expressed a variety of tests. In some cases, focus has been directed at the likely consequences of holding a particular time limitation mandatory, in an attempt to ascertain whether those consequences would defeat or promote the purpose of the enactment. [Citations.] Other cases have suggested that a time limitation is deemed merely directory 'unless a consequence or penalty is provided for failure to do the act within the time commanded.' " (*Ibid.*)

Looking at the language of section 3172, the notice of commencement of action is not required until *after* the lender has already been served with a stop notice action. Thus, the purpose of the notice of commencement of action does not serve to "notify" the lender of the pending stop notice. Instead, the notice of commencement of action is more likely designed as a safeguard to alert persons withholding funds pursuant to a stop notice that the funds are claimed (per the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

commenced stop notice action) and prevent premature release of the funds.

We are not the first court to come to this conclusion. Almost 50 years ago, the court in *Sunlight Electric Supply Company v. McKee* (1964) 226 Cal.App.2d 47, 37 Cal.Rptr. 782 (*Sunlight*) similarly interpreted Code of Civil Procedure former section 1197.1, subdivision (b), the predecessor provision to the language at issue in section 3172. (See Stats. 1967, ch. 542, § 1, pp. 1890, 1891.) The *Sunlight* court concluded that the notice of commencement of action requirement is not jurisdictional, but merely directory unless some detriment can be shown to have resulted from failure to file the notice within the five days. (*Sunlight, supra,* at p. 51, 37 Cal.Rptr. 782.) It explained that "[t]he various steps and time requirements as to ****573** filings and services of notice are for the purpose of providing protective measures and a necessary warning to those to whom notice is to be given or upon whom service is to be made. If the time provisions are not complied with and as a consequence injury results to the entity or a legal claimant under the entity upon which service is required then it would stand to reason that a strict compliance with the requirement could properly be insisted upon by the servicee. But if no right of the servicee or any person or entity who could legally claim under the ***856** servicee is adversely affected by failure to comply with the time for service requirement, then the requirement unless made so by specific mandate, is not a jurisdictional factor requiring the collapse of any remedy of which such notice or service forms a part." (*Sunlight, supra,* at p. 50, 37 Cal.Rptr. 782.)

While Lender is correct that *Sunlight* is distinguishable because there a notice of commencement of action was filed 14 days late which led the trial court to find substantial compliance with the statute. (*Sunlight, supra,* 226 Cal.App.2d at p. 49, 37 Cal.Rptr. 782.) In contrast, here, a notice was never filed. We believe this to be a distinction without a difference because the critical aspect of the *Sunlight* decision, with which we agree, is that the notice of commencement of action requirement is directory in the absence of prejudice. (*Id.* at p. 50, 37 Cal.Rptr. 782.) Here, Lender does not allege it suffered any prejudice as a result of Division 8's failure to give it a notice of the commencement of the action. The evidence shows that Lender suffered no prejudice because it had no undisbursed construction funds left in its control when Division 8 served Lender its bonded stop notice. Thus, Division 8's failure to give Lender the notice of commencement of action after it served Lender its stop notice action resulted in no prejudice as it had no funds to release.

Finally, we reject Lender's assertion that *Sunlight* has been superseded by more recent strict compliance cases. The cases Lender relies on are inapposite because they address the section 3097 preliminary notice that is required prior to a contractor's performance of work on a project site. (*Harold L. James v. Five Points Ranch, Inc.* (1984) 158 Cal.App.3d 1, 3–7, 204 Cal.Rptr. 494; *Shady Tree, supra,* 206 Cal.App.4th at pp. 135–139, 141 Cal.Rptr.3d 412.) As discussed above, the unambiguous language of section 3097 indicates that the preliminary notice is a necessary prerequisite to the validity of the lien. (*Ante,* pt. III.A.)

DISPOSITION

The judgments in favor of respondents Brady, Division 8 and Brewer are affirmed. These respondents are to recover their costs on appeal.

The judgment in favor of Dynalectric is provisionally reversed and the matter is remanded to the trial court for further proceedings, on an expedited basis, consistent with the views expressed in this opinion. If the trial court finds in favor of Dynalectric on the existence of a factual excuse for not serving a preliminary notice on Lender, the judgment in favor of Dynalectric ***857** is affirmed and Dynalectric is to recover its costs on appeal. Alternatively, if the trial court finds against Dynalectric on the existence of a factual excuse, the judgment in favor of Dynalectric is reversed and Lender is to recover its costs on appeal.

WE CONCUR:

BENKE, Acting P.J.

IRION, J.

All Citations

223 Cal.App.4th 831, 167 Cal.Rptr.3d 555, 14 Cal. Daily Op. Serv. 1225, 2014 Daily Journal D.A.R. 1377

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-8

West's Annotated California Codes
Civil Code (Refs & Annos)
Division 3. Obligations (Refs & Annos)
Part 1. Obligations in General
Title 2. Interpretation of Obligations (Refs & Annos)
Chapter 3. Conditional Obligations (Refs & Annos)

West's Ann.Cal.Civ.Code § 1442

§ 1442. Forfeiture; strict construction

Currentness

CONDITIONS INVOLVING FORFEITURE, HOW CONSTRUED. A condition involving a forfeiture must be strictly interpreted against the party for whose benefit it is created.

Credits
(Enacted in 1872.)

Notes of Decisions (119)

West's Ann. Cal. Civ. Code § 1442, CA CIVIL § 1442
Current with urgency legislation through Ch. 4 of 2020 Reg.Sess

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-9

203 Cal.App.4th 1328
Court of Appeal, Second District, Division 2, California.

CALIFORNIA INSURANCE GUARANTEE ASSOCIATION, Petitioner,
v.
WORKERS' COMPENSATION APPEALS BOARD and Next Enterprises, Respondents;
Oracle Imaging et al., Real Parties in Interest.

No. B231491.
|
Feb. 6, 2012.

Synopsis
Background: California Insurance Guarantee Association (CIGA) filed a petition for a writ of review of a decision of the Workers' Compensation Appeals Board (WCAB), Nos. ADJ4357722, ADJ5714365, determining that medical lienholders' claims for medical services provided to claimant, being asserted on their behalf by collection service, qualified as "covered claims," and rejecting CIGA's contention that the claims had been effectively assigned to collection service and thus were barred by statute.

The Court of Appeal, Ashmann-Gerst, J., held that there was no assignment of the claims, and thus they were "covered claims."

Affirmed and remanded.

Doi Todd, Acting P.J., filed concurring opinion.

Attorneys and Law Firms

****26** Guilford Steiner Sarvas & Carbonara, Anaheim, and Richard E. Guilford, for Petitioner.

Jeffrey M. Trombacco, for Real Parties in Interest.

Charles Edward Clark, Pasadena, as Amici Curiae on behalf of Express Pharmacy and Express Care Management.

No appearance for Respondents Workers' Compensation Appeals Board and Next Enterprises.

Opinion

ASHMANN–GERST, J.

***1333** Petitioner California Insurance Guarantee Association (CIGA) seeks review of a ruling by the Workers' Compensation Appeals Board (WCAB) that recognized claims asserted by real parties in interest Oracle Imaging, N-Care and Nations Surgery Center (collectively medical providers) as "covered" claims under Insurance Code section 1063.1.[1] The claims were asserted by real party in interest Pinnacle Lien Services (Pinnacle) on behalf of the medical providers. CIGA contends that it has no obligation to pay because Pinnacle was an assignee of the claims and assigned claims are excluded under section 1063.1, subdivision (c)(9).

We granted CIGA's petition for writ of review. We affirm the ruling that Pinnacle is not excluded from pursuing the claims against CIGA for two reasons. First, the facts do not establish that the medical providers assigned their claims to Pinnacle. Second, section 1063.1, subdivision (c)(9) does not exclude the claims from being "covered" because the medical providers are original claimants and Pinnacle is their administrator or personal representative.

****27 BACKGROUND**

Anastasia Jenkins filed a workers' compensation claim against her employer, whose workers' compensation insurance carriers became insolvent during the pendency of the proceedings. Medical services were rendered to Jenkins by real parties in interest the medical providers.

***1334** Each of the medical providers had separately entered into a "Collection Agreement" with Pinnacle, pursuant to which Pinnacle was to provide "exclusive collection services" for accounts "assigned" to Pinnacle by the "client" medical provider. The three agreements were essentially identical, and provided that Pinnacle was an independent contractor and would receive a certain percentage of the amount collected as compensation for its services. Under the agreements, Pinnacle had the discretion to negotiate the amount and terms of payment, subject to approval of the medical provider if the negotiated amount fell below specified percentages. It was not disputed that any insurance payments were to be made by checks payable directly to the medical provider, under its tax identification number.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

When the workers' compensation insurers became insolvent, CIGA was obliged to assume their obligations. "CIGA was created by legislation in 1969 ([Ins.Code,] § 1063 et seq.) to establish a fund from which insureds could obtain financial and legal assistance in the event their insurers become insolvent, i.e. 'to provide insurance against "loss arising from the failure of an insolvent insurer to discharge its obligations under its insurance policies." (Ins.Code, § 119.5.)' " (*Isaacson v. California Ins. Guarantee Assn.* (1988) 44 Cal.3d 775, 784, 244 Cal.Rptr. 655, 750 P.2d 297.)

CIGA took the position that the claims of the medical providers submitted by Pinnacle were specifically excluded from coverage by section 1063.1, subdivision (c)(9), which provides that covered claims do not include "(B) a claim by a person other than the original claimant under the insurance policy in his or her own name ... and does not include a claim asserted by an assignee or one claiming by right of subrogation, ..."

CIGA and real parties in interest submitted the question of whether the claims were barred to the workers' compensation administrative law judge (WCJ), who concluded that they were not barred. CIGA sought reconsideration, again contending that a claim asserted by an assignee is not a covered claim. The WCJ recommended denial of the petition for reconsideration, noting that Pinnacle only represented the medical providers and transmitted the amounts collected to them, while retaining a percentage of the collected sums as payment for its services.

The WCAB agreed and denied reconsideration. The WCAB opined that CIGA had failed to prove that legal title to the medical providers' claims had been transferred to Pinnacle, and therefore there was no assignment but only a delegation of the task of collection to Pinnacle. CIGA has sought review of this determination.

***1335 DISCUSSION**

I. No Assignment of Claims

" '[I]t is a fundamental principle of law that one of the chief incidents of ownership in property is the right to transfer it.' [Citation.]" (*Essex Ins. Co. v. Five Star Dye House, Inc.* (2006) 38 Cal.4th 1252, 1259, 45 Cal.Rptr.3d 362, 137 P.3d 192.) "This 'chief incident of ownership' applies equally to tangible and intangible forms of property, including causes of action. Originally codified in 1872, [Civil Code] section 954 states: 'A thing in action, arising out of the violation of a right of property, or out of an obligation, ****28** may be transferred by the owner.' An assignment is a commonly used method of transferring a cause of action." (*Id.* at p. 1259, 45 Cal.Rptr.3d 362, 137 P.3d 192.) " 'To "assign" ordinarily means to transfer title or ownership of property....' " (*Recorded Picture Company Productions Ltd. v. Nelson Entertainment, Inc.* (1997) 53 Cal.App.4th 350, 368, 61 Cal.Rptr.2d 742.)

An assignment may be complete or partial. "An unqualified assignment of a contract or chose in action, however, with no indication of the intent of the parties, vests in the assignee the assigned contract or chose and all rights and remedies incidental thereto." (*National R. Co. v. Metropolitan T. Co.* (1941) 17 Cal.2d 827, 832–833, 112 P.2d 598.) A complete assignment passes legal title to the assignee who is the real party in interest and may sue in his or her real name. (1 Witkin, Summary of Cal. Law (10th ed. 2005) Contracts, § 732, p. 816.) "A partial assignment of a claim is unenforceable without the debtor's consent, and the assignee ordinarily has no legal standing to sue." (1 Witkin, Summary of Cal. Law (10th ed. 2005) Contracts, § 733, p. 817.)

"An assignment for collection vests legal title in the assignee which is sufficient to enable him to maintain an action in his own name, but the assignor retains the equitable interest in the thing assigned." (*Harrison v. Adams* (1942) 20 Cal.2d 646, 650, 128 P.2d 9.) "Such an assignee has been referred to as the trustee or agent of the assignor ..., and a fiduciary relationship exists between them." (*Ibid.*, citations omitted.) CIGA does not contend that Pinnacle was granted an unqualified assignment by which it obtained all rights and remedies, but rather a partial assignment with legal title to pursue the medical providers' lien claims.

In determining whether an assignment has been made, "the intention of the parties as manifested in the instrument is controlling." (*National R. Co. v. Metropolitan T. Co., supra,* 17 Cal.2d at p. 832, 112 P.2d 598.) " '[A]n assignment, to be effective, must include manifestation to another person by the owner of his intention to transfer the right, without further action, to such other person or to a third person....' " (*Recorded Picture Company Productions Ltd. v.* ***1336** *Nelson Entertainment, Inc., supra,* 53 Cal.App.4th at p. 368, 61 Cal.Rptr.2d 742.) "The language of a contract governs its interpretation, if the language is clear. (Civ.Code, § 1638.) 'A contract must be so interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting,

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

so far as the same is ascertainable and lawful.' (*Id.,* § 1636; see 1 Witkin, Summary of Cal. Law (9th ed. 1987) Contracts, § 684, p. 617.)" (*County of San Joaquin v. Workers' Comp. Appeals Bd.* (2004) 117 Cal.App.4th 1180, 1184, 12 Cal.Rptr.3d 406.) The entire contract must be considered, not just isolated parts, and the words of the contract are to be given their usual and customary meaning. (Civ.Code, §§ 1641, 1644; *Sass v. Hank* (1951) 108 Cal.App.2d 207, 215, 238 P.2d 652.)

Established rules of contract interpretation apply in workers' compensation proceedings. Here, the agreements provided that each medical provider "is *the sole owner* of accounts receivable for which CLIENT desires PINNACLE to provide collection services." (Italics added.) The agreements also provided that after being in effect for six months, either party could terminate the agreement upon 30 days' notice. Two of the agreements provided that upon termination, the medical provider had the option of taking back previously assigned accounts for a fee, and the other agreement gave the client the right to demand "the reassignment" of specific individual accounts even without terminating ****29** the agreement. The agreements described Pinnacle's duties as "exclusive collection services for accounts assigned by CLIENT to PINNACLE." While Pinnacle was given "full discretion to negotiate the amount and terms of payment of CLIENT's accounts," it had to obtain approval from the medical providers to settle accounts for less than specified percentages of the original statement amount. Finally, the medical providers were to remain the custodians of all original records.

CIGA relies on the words "assign" and "reassign" in the agreements to support its position that Pinnacle became the assignee with legal title to the medical providers' claims. But use of the word "assign" is not conclusive. (9 Corbin on Contracts (rev. ed. 2007) § 47.4, p. 139.) CIGA's interpretation of the agreements does not take into account the full context of the agreements. Reading each agreement in its entirety makes clear that the medical providers retained full ownership of their accounts receivable, retained the right to terminate their relationships with Pinnacle and pursue collection efforts themselves, and maintained the right to approve certain settlement amounts. Indeed, the agreements refer to "CLIENT's accounts," not "Pinnacle's accounts." In other words, under the agreements the medical providers retained control of the accounts receivable and the authority to collect. The agreements establish that the medical providers only transferred to Pinnacle the *task* of collecting their accounts receivable, for a fee. Pinnacle was hired to provide collection *services,* nothing more.

***1337** CIGA argued that the medical providers only retained "financial control" of the accounts receivable. But this argument ignores the contractual language that the medical providers remained the "sole owners" of their accounts, with the ability to fire Pinnacle and collect on their own. CIGA relies on *Merchants Serv. Co. v. Small Claims Court* (1950) 35 Cal.2d 109, 111, 112, 216 P.2d 846, which found that an assignment resulted where the contractual language included the terms " 'relinquish, disclaim, and quitclaim any right, title or interest in and to the merchandise....' " No such language is used here. Taken as a whole, the language in the agreements does not establish an assignment.

Nor does the conduct of the parties support the finding of an assignment. " 'It is the substance and not the form of a transaction which determines whether an assignment was intended.... If from the entire transaction and the conduct of the parties it clearly appears that the intent of the parties was to pass title to the [property], then an assignment will be held to have taken place.' " (*Recorded Picture Company Productions Ltd. v. Nelson Entertainment, Inc., supra,* 53 Cal.App.4th at p. 368, 61 Cal.Rptr.2d 742, quoting *McCown v. Spencer* (1970) 8 Cal.App.3d 216, 225, 87 Cal.Rptr. 213.) There was no evidence presented that it was the intent of the medical providers to pass legal title to Pinnacle, or that Pinnacle proceeded as if it had such title. For example, in the three notices and requests for allowance of lien filed with the WCAB, Pinnacle identified the medical providers as the lien claimants and itself as their "representative," a clear indication that it was pursuing recovery of the claims on behalf of the medical providers. Additionally, the evidence showed that any money owed to the medical providers would be paid by check directly to them using their tax identification numbers, and not to Pinnacle. "An assignment of a right is a manifestation of the assignor's intention to transfer it by virtue of which the assignor's right to performance by the obligor is extinguished in whole or in part and the assignee acquires ****30** a right to such performance." (Rest.2d Contracts, § 317, subd. (1).) The medical providers did nothing to extinguish their rights to receive payments directly from CIGA. The record supports the finding that the medical providers did not assign their claims to Pinnacle.

II. The Claims Are Covered.

Section 1063.1, subdivision (c)(9) excludes claims from being "covered" unless they are asserted by an original

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

claimant or, inter alia, its administrator or personal representative. We are called upon to interpret the statute to determine whether the claims at issue are "covered."

***1338** A. *The rules of statutory interpretation.*

When interpreting a statute a court should ascertain the intent of the Legislature so as to effectuate the law's purpose. (*People v. Lewis* (1993) 21 Cal.App.4th 243, 247, 25 Cal.Rptr.2d 827.) In ascertaining that intent, a court must " 'first turn[ ] to the words used. [Citation.] [¶] When statutory language is clear and unambiguous, there is no need for construction and courts should not indulge in it. [Citations.]' [Citation.]" (*Ibid.*) Nonetheless, "the 'plain meaning' rule does not prohibit a court from determining whether the literal meaning of a statute comports with its purpose or whether such a construction of one provision is consistent with other provisions of the statute. The meaning of a statute may not be determined from a single word or sentence; the words must be construed in context, and provisions relating to the same subject matter must be harmonized to the extent possible. [Citation.]" (*Lungren v. Deukmejian* (1988) 45 Cal.3d 727, 735, 248 Cal.Rptr. 115, 755 P.2d 299.) If a statute is susceptible to more than one reasonable interpretation, the court may consider the statute's purpose, the evils to be remedied, the legislative history, public policy, and contemporaneous administrative construction. (*Nolan v. City of Anaheim* (2004) 33 Cal.4th 335, 340, 14 Cal.Rptr.3d 857, 92 P.3d 350.) In addition, the court may consider the consequences that will flow from a particular interpretation. (*Dyna–Med, Inc. v. Fair Employment & Housing Com.* (1987) 43 Cal.3d 1379, 1387, 241 Cal.Rptr. 67, 743 P.2d 1323.)

B. "*Original claimant.*"

"Original claimant" is not defined by the Insurance Code. However, the word "claimant" is defined as "an insured making a first party claim or a person instituting a liability claim." (§ 1063.1, subd. (g).) Thus, "original claimant" means (1) original "insured making a first party claim" or (2) original "person instituting a liability claim." In the context of first party insurance, "original claimant" has been construed to mean the original insured. (*Baxter Healthcare Corp. v. California Ins. Guarantee Assn.* (2000) 85 Cal.App.4th 306, 313, 102 Cal.Rptr.2d 87 (*Baxter*).)[2] In the ****31** context of third party insurance, "original claimant" has been construed to mean a ***1339** person who institutes a claim against an insured for liability. (*Black Diamond Asphalt, Inc. v. Superior Court* (2003) 114 Cal.App.4th 109, 119–120, 7 Cal.Rptr.3d 466 ["Under the unambiguous language of the statutory scheme, an original claimant can be any person (other than an insurer) instituting a liability claim within the coverage of the policy, provided that he or she does so in his or her own name and not through assignment or by right of subrogation."]; *Catholic Healthcare West v. California Ins. Guarantee Assn.* (2009) 178 Cal.App.4th 15, 31, 100 Cal.Rptr.3d 125 (*Catholic Healthcare*) ["the phrase 'original claimant under the insurance policy in his or her own name' was included in the statute to limit CIGA's liability to those individuals or entities that were named in the policy as well as members of the public injured by a named insured"].) An original claimant does not have to be the insured.[3]

Under the second definition of "claimant" in section 1063.1, subdivision (g), the person must institute a liability claim. Though "liability claim" is not defined by the CIGA statutes, "covered claim" is defined as an obligation ***1340** of an insolvent insurer. (§ 1063.1, subds. (c)(1).) Because a liability claim must be a covered claim to trigger CIGA's protection, a liability claim ****32** implicates a liability of an insured that is also the obligation of an insolvent insurer.

In our view, a medical lien under Labor Code section 4903, subdivision (b) is a liability claim. This is because the insured employer has a liability to a medical provider and the insolvent insurer has an obligation to pay. But instead of demanding payment from an insured employer, a medical provider has the option of expediting recovery by asserting a medical lien against the compensation award. If a third party claim is a covered claim, there is no logical reason to exclude a lien claim. Moreover, section 1063.1, subdivision (c)(1)(F) provides that covered claims include the obligations of insolvent insurers "to provide workers' compensation benefits under the workers' compensation law of this state." If a lien was not a liability claim, then the CIGA statutory scheme would not satisfy the definition of a covered claim with respect to the payment of medical expenses.

The medical providers qualify as original claimants. They instituted liability claims by asserting medical liens in the first instance. That they were aided by Pinnacle does not change the analysis. Pinnacle was an agent, and everything it did was solely on behalf of the medical providers.

C. "*Under the insurance policy.*"

To be a covered claim, a liability claim must be instituted "under the insurance policy." That phrase could refer to

a contractual claim for policy benefits by an insured employer or employee. But that interpretation only implicates first party claims, and it would render superfluous the language regarding a "person instituting a liability claim." Moreover, case law establishes that third party claims can be covered claims. Thus, "under the insurance policy" broadly encompasses a liability claim that triggers the obligation of an insolvent insurer. And because the law contemplates that a medical provider's lien will be satisfied out of insurance proceeds, we conclude that a medical lien arises "under the insurance policy."

D. "*In his or her own name.*"

The original claimant must seek recovery in his or her own name. We conclude that the medical providers met this requirement by instituting lien claims in their own names through Labor Code section 4903, subdivision (b).

E. "*Administrator"; "personal representative.*"

It is notable that a covered claim does not include "a claim by a person other than the original claimant under the insurance policy in his or ***1341** her own name, his or her assignee as the person entitled thereto under a premium finance agreement as defined in Section 673 and entered into prior to insolvency, his or her executor, administrator, guardian, or other personal representative or trustee in bankruptcy." (§ 1063.1, subd. (c)(9)(B).) Stated in the affirmative, a covered claim can be asserted by any person who is on that list. Only "a claim asserted by an assignee or one claiming by right of subrogation" is specifically barred. (*Ibid.*) Pinnacle is neither an assignee nor one claiming by right of subrogation. Nor is Pinnacle even making any claims. Rather, Pinnacle is making claims on behalf of the medical providers.

We conclude that Pinnacle fits the definition of "administrator" and "personal representative." While "administrator" is not defined by statute, one of various dictionary definitions is "a person who administers the affairs of an organization." (Dictionary.com, administrator < http://dictionary.reference.com/browse/administrator> [as of Feb. 6, 2012].) Pinnacle was hired by the medical providers to administer their Labor Code liens. ****33** Similarly, Pinnacle was hired to represent the medical provider and is therefore a personal representative. Without this interpretation, a lien holder could not use the services of collection agencies.

F. *Conclusion.*

Because the medical providers are original claimants and Pinnacle is their administrator or personal representative, the claims are not barred by section 1063.1, subdivision (c)(9).

DISPOSITION

The ruling of the WCAB is affirmed. The case is remanded for further proceedings consistent with this opinion.

I concur: CHAVEZ, J.

DOI TODD, Acting P.J., Concurring

I concur with the outcome. I write separately because I disagree with the majority's conclusion that the medical providers qualify as "original claimants" making "covered" liability claims. In my opinion, Insurance Code section 1063.1, subdivision (c)(9) addresses only claims made by an insured and has no application to a third party claim asserted by a lien claimant under Labor Code section 4903. In other words, lien claims are different than liability claims asserted under an insurance policy.

***1342** I. The Statutory Lien Scheme

The Insurance Code recognizes there is an entire body of law governing workers' compensation. The threshold provisions of Insurance Code section 1063.1, subdivision (c)(1) defining "covered claims" includes in subdivision (F) "In the case of a policy of workers' compensation insurance, to provide workers' compensation benefits under the workers' compensation law of this state." (Ins.Code, § 1063.1, subd. (c)(1)(F).)

It is undisputed by the California Insurance Guarantee Association (CIGA) that the medical providers have statutory medical lien claims arising from medical services provided to the injured worker. Medical liens in the workers' compensation system are governed by the Labor Code. (See *Hand Rehabilitation Center v. Workers' Comp. Appeals Bd.* (1995) 34 Cal.App.4th 1204, 1210, 40 Cal.Rptr.2d 734.) Labor Code section 4901 provides, "No claim for compensation nor compensation awarded, adjudged, or paid, is subject to be taken for the debts of the party entitled to such compensation except as hereinafter provided." In other words, "there can be no lien against a workers' compensation award for any kind of debt except as the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Labor Code specifically provides." (*Rangel v. Interinsurance Exchange* (1992) 4 Cal.4th 1, 15, 14 Cal.Rptr.2d 783, 842 P.2d 82.) Labor Code section 4903 provides that the Workers' Compensation Appeals Board (WCAB) "may determine, and allow as liens against any sum to be paid as compensation" reasonable medical expenses. [1] (Lab.Code, § 4903, subd. (b); *Hand Rehabilitation Center, supra,* at p. 1210, 40 Cal.Rptr.2d 734.)

"[Labor Code] [s]ection 4903 itemizes the 'debts' which may be allowed as liens against a compensation award by the appeals board. These two sections [4901 and 4903] indicate a clear legislative intent to ****34** remove such awards from the operation of the usual remedies available to creditors, to limit and regulate the kinds of debts which may be allowed, and to insure that the award is made available to the injured employee for his recovery and rehabilitation in accordance with the purposes of the act." (*Ogdon v. Workmen's Comp. Appeals Bd.* (1974) 11 Cal.3d 192, 196–197, 113 Cal.Rptr. 206, 520 P.2d 1022, fn. omitted.) The allowance of liens specifically identified in Labor Code section 4903 is the only exception to the requirement that compensation be paid directly to the injured worker.

***1343** Article XIV, section 4 of the California Constitution mandates expeditious, inexpensive and unencumbered payment of compensation to injured workers. [2] Because injured workers and their employers are often ready to resolve the worker's claim for indemnity before resolution of claims by lien claimants, the law grants a lien claimant an independent right to prove its claims in a separate proceeding. (Lab.Code, § 4903.4.) A lien claimant can also initiate the action even if the injured worker never pursues his or her claim. (Lab.Code, § 5501; *Permanente Medical Group v. Workers' Comp. Appeals Bd.* (1985) 171 Cal.App.3d 1171, 1178, 217 Cal.Rptr. 873.) The WCAB "may order the amount of any lien claim, as determined and allowed by it, to be paid directly to the person entitled, either in a lump sum or in installments." (Lab.Code, § 4904, subd. (c).) The WCAB is vested with discretion to determine the reasonableness of the claimed amount (Lab.Code, § 4906), and the priorities among lien claimants (Lab.Code, § 4903).

II. Statutory Construction and Legislative History

The majority has set forth the fundamental rules of statutory construction, and I will not repeat them. But applying these rules here makes clear that the exclusions set forth in Insurance Code section 1063.1, subdivision (c)(9) do not include situations involving *qualified or partial assignment; collection agreement by a collection agency or attorney; a company administering lien claims for another company.* The commonsense interpretation is that section 1063.1, subdivision (c)(9) has no application to a third party claim asserted by a lien claimant under Labor Code section 4903.

The legislative history supports this conclusion. "To determine the most reasonable interpretation of a statute, we look to its legislative history and background." (*Goodman v. Lozano* (2010) 47 Cal.4th 1327, 1332, 104 Cal.Rptr.3d 219, 223 P.3d 77, citing *Doe v. City of Los Angeles* (2007) 42 Cal.4th 531, 543, 67 Cal.Rptr.3d 330, 169 P.3d 559.) CIGA was created in ***1344** 1969 on an "urgency" basis at the request of the Department of Insurance "for the immediate preservation of the public peace, health or safety" following the insolvency of insurers that had provided workers' compensation insurance policies "to ****35** persons of modest means." (Assem. Bill No. 1310 (1969 Reg. Sess.) as amended Aug. 1, 1969, § 5.) The 1969 legislative history of section 1063.1 does not include any discussion of the term "assignee," but the statement of intent describes the need to deal with the "extreme hardship" upon "insureds, claimants, public agencies and the public at large." (Assem. Bill No. 1310, (1969 Reg. Sess.) as amended Aug. 1, 1969 § 5.) While the meaning of the word "claimants" is not defined in this statement of intent, the term is used as a category separate from "insureds." Because the lien claim process under the Labor Code was already in effect at the time section 1063.1 was enacted, we may reasonably presume that the Legislature was aware of the process by which medical lien claimants utilized third parties to assert their claims. There is nothing in the legislative history to show that the Legislature specifically intended to exclude claims by workers' compensation lien claimants who utilize collection agencies for processing their CIGA claims, or that the Legislature considered such arrangements to be assignments that were not covered claims under CIGA.

The legislative history is notably silent with respect to any potential impact on the role that collection agencies play in the processing of workers' compensation claims, or with respect to the manner in which injured worker's claims for medical services should be processed under CIGA. The bill's sponsor, the Department of Insurance, did not describe any problems relating to this process. If the Legislature had intended to prohibit the use of collection agencies in processing CIGA claims, such prohibition would have most likely generated

significant opposition or at least concern and discussion. The legislative history does not document any such opposition or concern.

Section 1063.1 has been amended several times since 1969, most recently in 2010. We have not been made aware of any problems arising from having collection agencies pursue medical lien claims, and assume that had there been problems, the Legislature would have addressed them. As the court stated in *California Ins. Guarantee Assn. v. Workers' Comp. Appeals Bd.* (2005) 128 Cal.App.4th 307, 316, 26 Cal.Rptr.3d 845, "if the Legislature had wanted to make an exception for workers' compensation claims from [section 1063.1], it could and would have said so." (See also *California Ins. Guarantee Assn. v. Argonaut Ins. Co.* (1991) 227 Cal.App.3d 624, 634, 278 Cal.Rptr. 23 ["In our view, if the Legislature views workers' compensation as significantly different from other insurance so as to necessitate different treatment in recovering claims from CIGA, the Legislature can say so. ***1345** Insurance Code section 1063.1 shows that the Legislature knew how to make an exception for workers' compensation benefits when it so intended," (fn. omitted)].)

III. Section 1063.1, Subdivision (c)(9) Does Not Apply to Lien Claims

Based on the above, I believe that third party lien claims are different from third party liability claims asserted against an insurance policy. The fundamental differences between lien claims and liability claims are: (1) The lien claimant has performed a service for which it is entitled to be paid, while a claimant under an insurance policy has sustained an injury for which it may or may not be compensated under the insurance policy; (2) A workers' compensation lien is asserted against compensation to be paid (Lab.Code, § 4903), while a claim against an insurance policy is made against the policy; and (3) A lien obligation is not based on a contractual relationship; rather, it is an obligation imposed by law, while obligations arising from an insurance policy are contractual in nature. In light of these distinctions, I ****36** believe that lien claims are entirely different from insurance policy claims, and as such should be treated differently from claims made against an insurance policy.

None of the cases upon which the majority relies involved lien claims. *Black Diamond Asphalt, Inc. v. Superior Court* (2003) 114 Cal.App.4th 109, 7 Cal.Rptr.3d 466 involved an indemnity claim asserted between defendant tortfeasors; *Catholic Healthcare West v. California Ins. Guarantee Assn.* (2009) 178 Cal.App.4th 15, 100 Cal.Rptr.3d 125 dealt with the problem of successor corporations and whether successors were "original claimants"; and *Nowlon v. Koram Ins. Center, Inc.* (1991) 1 Cal.App.4th 1437, 2 Cal.Rptr.2d 683 involved a negligence action by an injured employee against a liability broker. Although the majority quotes at length from *Nowlon,* that case simply noted in dicta that section 1063.1, subdivision (g) would allow an injured employee to bring a third party claim against CIGA. Moreover, in *Baxter Healthcare Corp. v. California Ins. Guarantee Assn.* (2000) 85 Cal.App.4th 306, 313, 102 Cal.Rptr.2d 87, the court stated: "CIGA's contention that 'original claimant' means 'original insured' is the only rational way to read the phrase 'original claimant under the insurance policy in his or her own name.' Any other reading of the statute would do violence to the phrase." (*Id.* at p. 313, 102 Cal.Rptr.2d 87.) I agree with this conclusion, and therefore disagree with the majority that the medical providers are original claimants ***1346** asserting liability claims. Because a lien claim is fundamentally different from a liability claim, Insurance Code section 1063.1, subdivision (c)(9) simply does not apply to the medical lien claims asserted here.

All Citations

203 Cal.App.4th 1328, 138 Cal.Rptr.3d 24, 77 Cal. Comp. Cases 143, 12 Cal. Daily Op. Serv. 2457, 2012 Daily Journal D.A.R. 2712

Footnotes

1 All further statutory references are to the Insurance Code unless otherwise indicated.

2 "[T]he distinction between first and third party claims can be summarized as follows: If the insured is seeking coverage against *loss or damage sustained by the insured,* the claim is first party in nature. If the insured is seeking coverage against *liability of the insured to another,* the claim is third party in nature." (*Garvey v. State*

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Farm Fire & Casualty Co. (1989) 48 Cal.3d 395, 399, fn. 2, 257 Cal.Rptr. 292, 770 P.2d 704.) *Baxter* did not adhere to this distinction. It involved general liability insurance, which ostensibly implicates a third party claim. But according to *Baxter,* the appellant was seeking indemnity as the owner of various policies and therefore it was making a first party claim. (*Baxter, supra,* 85 Cal.App.4th at p. 312, 102 Cal.Rptr.2d 87.) The court denied CIGA coverage because the appellant received a transfer of the policies after it acquired the assets of the original insured in a merger. It was noted that the policies were not in the appellant's name and the named insured no longer existed. (*Ibid.*) The holding in *Baxter* is therefore limited to a first party claim by an insured.

3 *Nowlon v. Koram Ins. Center, Inc.* (1991) 1 Cal.App.4th 1437, 2 Cal.Rptr.2d 683 (*Nowlon*) bolsters our conclusion. An injured employee sued his employer for damages and discovered that the employer's insurer was insolvent and not a member of CIGA. The employer filed for bankruptcy. Seeking a remedy, the employee sued the employer's insurance broker. One issue was whether the employee could have made a third party claim against CIGA if the insurer had been a CIGA member.

The *Nowlon* court concluded that third party claims against CIGA are permitted. It noted that at "the time the CIGA statutes were introduced, the digests accompanying the proposed legislation, Assembly Bill No. 1310, stated that 'Covered claims eligible for payment by the guarantee association are defined as those arising out of policies issued to residents of this state or payable to residents of this state ...' [Citation.] A letter from the bill's author conveying the legislation to then-Governor Ronald Reagan for his signature on August 11, 1969, stated that the effect of CIGA was to guarantee that 'all members of the public in California can be assured that their claims will be paid despite the fact that a company may become insolvent.' The letter goes on to note that 'the bill immediately gives relief to claimants and policyholders' of a small insurance company which had declared bankruptcy." (*Nowlon, supra,* 1 Cal.App.4th at p. 1443, 2 Cal.Rptr.2d 683.) Nonetheless, "section 1063.1 as enacted was ambiguous as to third party claimants. Accordingly, an attempt to clarify the statute was made in 1983 with Senate Bill No. 350, whose stated purpose was to 'make[ ] clear that "claimant" as used in the statute includes both first and third party claimants.' [Citation.] This task was supposedly accomplished by changing [existing language] ... to read that ' "Covered claims" shall not include (i) any claim to the extent it is covered by any other insurance of a class covered by the provisions of this article available to the claimant *or insured* ...', the underlined addition intended to draw a distinction between insureds who made claims and third parties who made claims." (*Nowlon, supra,* at pp. 1443–1444, 2 Cal.Rptr.2d 683.) According to *Nowlon,* this "attempt at clarification was apparently not clear enough, prompting yet another amendment to section 1063.1 in 1987. The 1987 amendment added subdivision (g) to [section 1063.1]." (*Nowlon, supra,* at p. 1444, fn. 5, 2 Cal.Rptr.2d 683.) The court explained that "both the original legislation and its subsequent amendment attempted to define the scope of CIGA as encompassing both insureds and third party claimants. The intent to allow third party claims was present, even if the language used in the statute was not equal to the task of clearly expressing this intent." (*Id.* at p. 1444, 2 Cal.Rptr.2d 683.)

1 Labor Code section 4903 allows the following liens: (a) reasonable attorney fees; (b) reasonable medical expenses; (c) reasonable value of the living expenses of an injured employee or of his or her dependents; (d) reasonable burial expenses; (e) reasonable living expenses of the spouse; (f) unemployment compensation disability benefits; (g) unemployment compensation benefits and extended duration benefits; (h) family temporary disability insurance benefits; (i) indemnification granted by the California Victims of Crime Program; and (j) amounts paid by the Asbestos Workers' Account.

2 California Constitution, article XIV, section 4 provides that "[t]he Legislature is hereby expressly vested with plenary power, unlimited by any provision of this Constitution, to create, and enforce a complete system of workers' compensation, by appropriate legislation, and in that behalf to create and enforce a liability on the part of any or all persons to compensate any or all of their workers for injury or disability, and their dependents for death incurred or sustained by the said workers in the course of their employment, irrespective of the fault of any party. ... [T]he the administration of such legislation shall accomplish substantial justice in all cases expeditiously, inexpensively, and without incumbrance of any character; all of which matters are expressly declared to be the social public policy of this State, binding upon all departments of the State government."

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-10

538 F.Supp. 1306
United States District Court,
N.D. Ohio, Eastern Division.

CITY OF CLEVELAND, Plaintiff,
v.
The CLEVELAND ELECTRIC ILLUMINATING COMPANY, Defendant.

Civ. A. No. C75-560.
|
Oct. 20, 1980.
|
Supplemental Opinion Oct. 31, 1980.

Synopsis

Antitrust action was brought by city against electric utility. On utility's motions for dismissal, the District Court, Krupansky, J., held that: (1) evidence adduced at trial failed to support existence of either power exchange or wholesale market, and (2) sole relevant product market was therefore sale of retail firm electric power.

Motions granted in part and denied in part.

Attorneys and Law Firms

***1308** William B. Norris, Hahn, Loeser, Freedheim, Dean & Wellman, James E. Young, Thomas E. Wagner, Director of Law, City of Cleveland, Cleveland, Ohio, for plaintiff.

John Lansdale, James P. Murphy, Squire, Sanders & Dempsey, Cleveland, Ohio, for defendant.

MEMORANDUM AND ORDER

KRUPANSKY, District Judge.

This matter is presently before the Court on a series of motions advanced by the defendant The Cleveland Electric Illuminating Company (CEI) pursuant to Rule 50(a), Fed.R.Civ.P., whereby CEI seeks a determination that dismissal of the plaintiff's cause, in whole or in material part, is warranted on the grounds of insufficient proof. The Court, in the course of proceedings conducted on October 16, 1980, permitted extensive oral argument on the defendant's various assertions. See Transcript at pp. 4730-4909.

In passing on the defendant's motions, the Court is fully cognizant of the standards governing the application of Rule 50, Fed.R.Civ.P. As succinctly stated by the Sixth Circuit Court of Appeals in Morelock v. NCR Corp., 586 F.2d 1096, 1104-1105 (6th Cir. 1978), cert. denied, 441 U.S. 906, 99 S.Ct. 1995, 60 L.Ed.2d 375 (1979):

> The issue raised by a motion for a judgment n.o.v. is whether there is sufficient evidence to raise a question of fact for the jury. O'Neill v. Kiledjian, 511 F.2d 511, 513 (6th Cir. 1975). This determination is one of law to be made by the trial court in the first instance. Id. In determining whether the evidence is sufficient, the trial court may neither weigh the ***1309** evidence, pass on the credibility of witnesses nor substitute its judgment for that of the jury. Rather, the evidence must be viewed in the light most favorable to the party against whom the motion is made, drawing from that evidence all reasonable inferences in his favor. See Gillham v. Admiral Corp., 523 F.2d 102, 109 (6th Cir. 1975), cert. denied, 424 U.S. 913, 96 S.Ct. 1113, 47 L.Ed.2d 318 (1976). If, after thus viewing the evidence, the trial court is of the opinion that it points so strongly in favor of the movant that reasonable minds could not come to a different conclusion, then the motion should be granted. Id. at 109; Reeves v. Power Tools, Inc., 474 F.2d 375, 380 (6th Cir. 1973); 9 Wright & Miller, Federal Practice and Procedure s 2524 (1971). [1]

Accord: Milstead v. International Brotherhood of Teamsters, 580 F.2d 232, 235 (6th Cir. 1978). See Pergola v. Pennsylvania R. R. Co., 311 F.2d 837, 838-839 (6th Cir. 1963); Patrick v. South Central Bell Telephone Co., 641 F.2d 1192, at p. 1197 (6th Cir. 1980).

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Mindful of the foregoing principles, the Court undertakes to assess the defendant's various contentions, considering in the first instance the relevant product market. As is apparent from the City's Trial Brief of September 2, 1980, the plaintiff has asserted that there exists for purposes of this controversy three separate and distinct relevant product markets, namely, a regional power exchange market, a wholesale firm power market and a retail firm power market. The Court, for the reasons outlined more fully below, is persuaded by its review of the record and the governing authorities that the evidence adduced at trial fails to support the existence of either a power exchange or a wholesale market herein, and thus compels the conclusion that the sole relevant product market is the sale of retail firm electric power.

It is beyond peradventure that the plaintiff in an antitrust action bears the burden of defining and proving the relevant product market charged to have been monopolized in violation of s 2 of the Sherman Act. United States v. E. I. DuPont DeNemours & Co., 351 U.S. 377, 76 S.Ct. 994, 100 L.Ed. 1264 (1956); Fount-Wip, Inc. v. Reddi-Wip, Inc., 568 F.2d 1296, 1301 (9th Cir. 1978); Cf. United States v. Marine Bancorporation, 418 U.S. 602, 94 S.Ct. 2856, 41 L.Ed.2d 978 (1974). And, meeting this burden is “a necessary predicate” for establishing a claim under the antitrust laws. See e.g., United States v. E. I. DuPont DeNemours & Co., 353 U.S. 586, 77 S.Ct. 872, 1 L.Ed.2d 1057 (1957); Fount-Wip, Inc. v. Reddi-Wip, Inc., supra.

In assessing the sufficiency of plaintiff's proof in support of its relevant market contentions, the Court's attention is directed initially to the pronouncements of the United States Supreme Court in United States v. E. I. DuPont DeNemours & Co., 351 U.S. 377, 76 S.Ct. 994, 100 L.Ed. 1264 (1956), wherein that Tribunal thoroughly explored the scope of antitrust product markets, stating:

> In considering what is the relevant market for determining the control of price and competition, no more definite rule can be declared than that commodities reasonably interchangeable by consumers for the same purposes make up that “part of the trade or commerce,” monopolization of which may be illegal.
>
> The “market” which one must study to determine when a producer has monopoly power will vary with the part of commerce under consideration. The tests are constant. That market is composed of ***1310** products that have reasonable interchangeability for the purposes for which they are produced-price, use and qualities considered.

Id. 76 S.Ct. 1007-1012. Similarly, in Brown Shoe Company v. United States, 370 U.S. 294, 82 S.Ct. 1502, 8 L.Ed.2d 510 (1962), the Court again observed:

> The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it.

Id. 82 S.Ct. at 1523-1524. See also United States v. Grinnell Corp., 384 U.S. 563, 86 S.Ct. 1698, 16 L.Ed.2d 778 (1966); United States v. Greater Buffalo Press, 402 U.S. 549, 91 S.Ct. 1692, 29 L.Ed.2d 170 (1971).

Of course, considerations of commodity interchangeability per se are not implicated by the present controversy. Nonetheless, implicit in the above-referenced criteria and apparent from the case authorities addressed below, are even more fundamental aspects of market existence or definition upon which plaintiff's proof falters.

“The basic tests developed by the Supreme Court in defining product and geographic markets only have meaning in the context of transactions between buyer and seller.” American Medicorp, Inc. v. Humana, Inc., 445 F.Supp. 589, 597 (E.D.Pa.1977). As explained by the Seventh Circuit Court of Appeals in Sargent-Welch Scientific Co. v. Ventron Corp., 567 F.2d 701 (7th Cir. 1977), cert. denied, 439 U.S. 822, 99 S.Ct. 87, 58 L.Ed.2d 113 (1978):

> In determining what constitutes a relevant market for antitrust purposes, the goal is to “delineate markets which conform to areas of effective competition and to the realities of competitive practice.”

Id. at 710, quoting in part from L. G. Balfour Co. v. FTC, 442 F.2d 1, 11 (7th Cir. 1971); see also FTC v. Rhinechem Corp., 459 F.Supp. 785, 788 (N.D.Ill.1978); Fontana Aviation, Inc. v. Cessna Aircraft Co., 460 F.Supp. 1151, 1158 (N.D.Ill.1978). Thus, central to a determination of relevant market is proof of the existence or prospect of meaningful competitive conditions, see e.g., United States v. E. I. DuPont DeNemours & Co., supra 76 S.Ct. at 1005-1010, and the authorities have uniformly stressed the importance of demonstrating “the flow of commercial interaction”, Columbia Metal Culvert Company, Inc. v. Kaiser Aluminum & Chemical Corp., 579

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

F.2d 20, 26 (3rd Cir. 1978), cert. denied, 439 U.S. 876, 99 S.Ct. 214, 58 L.Ed.2d 190 (1979), and the "pattern of competition", id. as well as the necessity of "identifying consumer behavior patterns." Fontana Aviation, Inc. v. Cessna Aircraft Company, supra at 1158. No relevant product market can be defined "unless focus is made on particular services and actual commercial transactions between buyers and sellers." T.V. Signal Co. v. American Tel. & Tel. Co., 465 F.Supp. 1084, 1089 (D.S.D.1979), vacated on other grounds, 617 F.2d 1302 (8th Cir. 1980).

Apparent from the foregoing authorities is the fundamental principle that the Sherman Act concept of relevant product market is properly defined with reference to actual or prospective competition, that is, the existence of two or more firms competing or attempting to compete for the opportunity to serve or supply an existing or prospective group of identifiable consumers.

Applying this criteria, and appraising the evidence in light of the "commercial realities of the (electrical energy) industry", Brown Shoe Company v. United States, supra, 370 U.S. at 336, 82 S.Ct. at 1530; see United States v. Grinnell Corp., supra, it is readily apparent that plaintiff's claimed "regional power exchange market" does not, as a matter of law, constitute a separate and distinct "market" within the purview of the Sherman Antitrust Act.

Regional power transactions involve the exchange of electric power between utilities for the purpose of maintaining member firm power supply at the lowest reasonable cost. The "services" of a regional exchange are essentially the use of the most efficient supply available at a given time as among all sources within the exchange. For example, ***1311** an increase in demand for electricity, or "load", within the service area of a given utility which that utility alone could meet only by activating its most expensive peaking units would be satisfied by using power from another system's "baseload" at less cost. Exchange might also occur when a member-owned generating unit is shut down for maintenance purposes, or in an emergency situation. Members of a power exchange coordinate the development of the system to facilitate the most efficient operation of the individual utilities involved. Obviously, the element of cooperative reciprocity (rather than competitive give- and-take) is central to the successful operation of the power exchange.

Plaintiff contends nonetheless that such an arrangement is a "market" composed of buyers and sellers of the "cluster of services" which might be transferred as among member utilities.

In West-Texas Utilities Co. v. Texas Electric Service Co., 470 F.Supp. 798, 821-822 (N.D.Tex.1979), however, the Court rejected a similar contention that a power exchange arrangement among various utilities constituted a relevant product market within the purview of the Sherman Act, emphasizing that the exchange was not "a market where competition occurred, but rather an area of cooperation". Id. at 821.

As alluded to hereinabove, the element of competition between potential sellers for the opportunity to serve or supply identifiable buyers is fundamental to and inherent in the criteria for determining the existence of a relevant product market. The plaintiff has produced no evidence to show that as between members of the power exchange in question herein there is competition for the opportunity to "sell" a service to another member when needed. Nor is there any evidence that any member thereof has ever sought to increase the amount of power "sold" within the exchange. Moreover, the record is utterly devoid of proof that any member-utility has sought to curtail its firm power retail sales so as to "compete" more effectively for the right to supply some other retailer with its cheapest power, provided without charge as to capital expense.

Furthermore, there is no evidence that the demand for power in a power exchange is distinct from consumer demand for firm power. A member of a power exchange would desire "peakload" power only when its firm retail demand required it. "Baseload" power would be desired only when it was more efficient or economical. There obviously can be no "market" at any price for power provided through a power exchange if the participants in the exchange are not in the business of selling firm power to consumers. The "competition" to be used as between generating units in a power exchange, all owned by utilities for the express purpose of providing firm power for sale, does not rise to the level of separate product markets for efficient and inefficient methods of supplying power at a given time.

In summary, the evidence of record in its entirety has failed to demonstrate that the regional power exchange arrangements identified in the Second Amended Complaint were anything other than areas of mutual cooperation or joint ventures among exchange members. The record is certainly devoid of proof even suggesting that exchange members competed with

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

each other, or for that matter with other utilities, to provide the "cluster of services" available to each member utility. [2]

The plaintiff having failed to demonstrate the existence of either actual or potential competition within the arena of regional power exchange transactions, the Court concludes, as a matter of law, that ***1312** the City's claimed "regional power exchange market" does not constitute a product market within the meaning of 15 U.S.C. s 2.

Although the record fails to support a separate and distinct power exchange market as such, sufficient evidence has been presented by plaintiff to permit a jury assessment of the City's charge that CEI's unilateral conduct effectively denied the City access to the benefits of coordinated regional power exchange transactions, thereby adversely affecting MELP's ability to compete in the retail power market. But see infra at pp. 1316-1318

For slightly different but equally compelling reasons, the Court concludes that plaintiff has failed to adduce evidence sufficient to support the existence of a separate and distinct wholesale power market. As alluded to hereinabove, essential to the existence of an actual or potential product market is the availability of an identifiable group or class of consumers of the commodity offered for sale. In Brown Shoe Company v. United States, supra, Chief Justice Warren, in discussing those factors which must be examined in ascertaining the existence of a product submarket, observed that emphasis must be given to "practical indicia" such as "distinct customers" available to purchase the product in question. 82 S.Ct. at 1530. And, in L. G. Balfour Company v. FTC, 442 F.2d 1 (7th Cir. 1971), the Seventh Circuit Court of Appeals commented "that any test (of market definition) 'which ignores the buyers and focuses on what the sellers do, or theoretically can do, is not meaningful.' " Id. at 11 quoting in part from United States v. Bethlehem Steel Corp., 168 F.Supp. 576 (S.D.N.Y.1958); see also Sargent-Welch Scientific Co. v. Ventron Corp., supra.

The Court has examined the record in this proceeding, and finds that, with respect to the City's claimed "wholesale power market", the evidence has failed to even suggest the existence of a class of prospective consumers of wholesale power within the relevant geographical area. See discussion of geographical market, infra at pp. 1313-1314. In other words, even if plaintiff had been able to generate or obtain bulk power to market on a wholesale basis, the evidence has utterly failed to identify or establish any existing or prospective utilities that might have conceivably purchased that power from the City. Absent a distinct and identifiable body of consumers of a product, there obviously can be no competition in terms of selling the commodity, and hence no "market" within the purview of the Sherman Act.

Moreover, plaintiff's argument advancing the so-called "captive sales" principle is without merit. In this regard the Court finds instructive the reasoning of Judge Young in Neugebauer v. A. S. Abell Company, 474 F.Supp. 1053 (D.Md.1979) wherein the Court rejected such an argument under circumstances strikingly similar to those presented by the case at bar. In that case, plaintiff-Neugebauer was a distributor of defendant-Abell's newspapers as well as a retail sales competitor of the defendant. Plaintiff charged Abell with having attempted to " 'squeeze' plaintiff out of the home delivery business by increasing the wholesale price charged for their newspapers." 474 F.Supp. at 1057. Although competition occurred only at the retail distribution level, "plaintiff attempted to prove that the relevant product market was the wholesale newspaper market." Id. at 1061. The Court posited:

> The essential fallacy in plaintiff's argument, however, lies in his attempting to define the relevant product market not on the basis of commercial realities such as use and quality of the item but rather on the basis of the distribution system utilized by Abell. If accepted, the logic of plaintiff's argument would mean that the definition of the product market would turn on how defendant Abell distributed its product rather than on the nature of what was being distributed. Additionally, plaintiff's theory would premise liability on the presence of two types of alleged monopoly, with monopoly again being defined in terms of the product distribution system. The first monopoly ***1313** is that which defendant has over its own product when sold at wholesale. The second monopoly, one which plaintiff has failed to prove, is that acquired in competing with other products in the relevant market. Obviously, by

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> definition, no one competes with Abell at wholesale: plaintiff can purchase Sunpapers for resale only from Abell because no one else makes them.

Id. at 1062. In a footnote, the Court disapproved plaintiff's attempts to artificially create a wholesale market comprised in part of defendant's sales of newspapers to itself:

> The real issue raised here is whether plaintiff and Abell actually compete in the newspaper wholesale market. Plaintiff claims that they do and argues that defendant Abell, when selling at retail itself, establishes a stipulated "shadow" wholesale price for its own newspapers. In other words, plaintiff claims that Abell the wholesaler sells Abell papers to Abell the retailer. See note 2 supra. Plaintiff must invent such a fictional wholesale price in order to overcome the natural monopoly argument.

Id. at 1063 n. 7.

Similarly, the City attempts to define the relevant market for purposes of this case with reference to its characterization of the electrical distribution system employed by CEI. There is no evidence in the record however that defendant "sold" wholesale power to itself for resale nor is there even a scintilla of proof that the parties competed or might have competed in wholesale sales of electrical energy. The City's attempt to create a wholesale market within the parameters of this suit is nothing more than a fictional abstraction without support in either the record or the "commercial realities" of the industry here in issue. See also United States v. Phillipsburg National Bank, 399 U.S. 350, 90 S.Ct. 2035, 26 L.Ed.2d 658 (1970).

For the foregoing reasons, the Court finds that plaintiff has failed to adduce evidence which even suggests the existence of a separate and cognizable wholesale power market, and concludes, as a matter of law, that such a market does not exist.

Of course, at this juncture of the proceedings there is sufficient proof from which a jury might reasonably infer damage to plaintiff by reason of its inability to purchase PASNY (wholesale) power. However, such a lack of access to alternative sources of wholesale power would only have impacted upon plaintiff's ability to compete in the retail power market, and, for the obvious reasons stated above, could not have affected any attempt on the part of the City to market power on a wholesale basis. The fact that access to wholesale power might be an important element of competition in the retail power market, however, does not compel the conclusion that wholesale power sales comprise a separate and distinct product market within the parameters of the instant controversy.

Defendant further urges that it is entitled to a determination that the relevant geographic market is the thirty-square-mile-area within which plaintiff and defendant actually compete. Plaintiff maintains that the evidence is sufficient to present a jury question as to whether the entire CEI service area, or at least some portion thereof, is one of at least potential competition and thus properly considered in determining the scope of and the injury resulting from the alleged s 2 violations.

In ascertaining the scope of the relevant geographic market for Sherman Act purposes, it is incumbent upon the trier of fact to determine "where, within the area of competitive overlap, the effect of the (antitrust violation) on competition will be direct and immediate." United States v. Philadelphia National Bank, 374 U.S. 321, 83 S.Ct. 1715, 1738, 10 L.Ed.2d 915 (1963); United States v. Grinnell Corp., supra. The boundaries of the geographic area, however, must be drawn so as to take into account not only existing but potential competition as well. Otter Tail Power Co. v. United States, 410 U.S. 366, 93 S.Ct. 1022, 35 L.Ed.2d 359 (1973).

In this regard, the authorities are unanimous in recognizing that an antitrust plaintiff ***1314** need not actually be engaged in a going business in a specific geographic location in order to have Sherman Act standing; "it is sufficient if he has manifested an intention to enter the business (or market) and has demonstrated his preparedness to do so." Hecht v. Pro-Football, Inc., 570 F.2d 982, 987 (D.C.Cir.1977), cert. denied 436 U.S. 956, 98 S.Ct. 3069, 57 L.Ed.2d 1121 (1978); Hayes v. Solomon, 597 F.2d 958, 973 (5th Cir. 1979), cert. denied, 444 U.S. 1078, 100 S.Ct. 1028, 62 L.Ed.2d 761 (1980); Solinger v. A. & M. Records, Inc., 586 F.2d 1304, 1309-10 (9th Cir. 1978), cert. denied, 441

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

U.S. 908, 99 S.Ct. 1999, 60 L.Ed.2d 377 (1979); Martin v. Phillips Petroleum Company, 365 F.2d 629, 632-33 (5th Cir. 1966), cert. denied, 385 U.S. 991, 87 S.Ct. 600, 17 L.Ed.2d 451 (1966); Volasco Products Co. v. Lloyd A. Fry Roofing Co., 308 F.2d 383, 395-96 (6th Cir. 1962), cert. denied, 372 U.S. 907, 83 S.Ct. 721, 9 L.Ed.2d 717 (1963); Peller v. International Boxing Club, 227 F.2d 593 (7th Cir. 1955); Laurie Visual Etudes v. Chesebrough-Pond's, Inc., 473 F.Supp. 951, 995 (S.D.N.Y.1979); Huron Valley Hospital v. City of Pontiac, 466 F.Supp. 1301, 1311 (E.D.Mich.1979); Magnus Petroleum Co., Inc. v. Skelly Oil Co., 446 F.Supp. 874, 880-881 (E.D.Wis.1978), reversed on other grounds, 599 F.2d 196 (7th Cir. 1979), cert. denied, 444 U.S. 916, 100 S.Ct. 231, 62 L.Ed.2d 171 (1979); N.W. Controls, Inc. v. Outboard Marine Corp., 333 F.Supp. 493, 507 (D.Del.1971). Moreover, in Heatransfer Corp. v. Volkswagenwerk, A.G., 553 F.2d 964, 988 n.20 (5th Cir. 1977), cert. denied, 434 U.S. 1087, 98 S.Ct. 1282, 55 L.Ed.2d 792 (1978), the Fifth Circuit Court of Appeals quite appropriately commented:

> (T)he Court does not believe that a going concern, which is the victim of an anticompetitive practice, must forego damages for sales it would have made as the result of the natural expansion of its business simply because it was victimized early in its existence before its attempts to expand could ripen into evidence of preparedness and intent to increase its output. Thus, the question for the Court's determination is whether, under the facts of the present case, the manufacture of units for each type of Volkswagen vehicle in the relevant market can be considered the expansion of a present business into a new market for purposes of standing, or simply one facet of growth in an ongoing business for purposes of damages. The line to be drawn between expansion into new areas and growth in established ones is not easily defined and one that must be determined from the facts of each case.

Quoted in TV Signal Company of Aberdeen v. American Telephone & Telegraph Co., 617 F.2d 1302, 1308 (8th Cir. 1980).

The record reflects at least some evidence of plaintiff's efforts to extend its existing retail sales market beyond the aforementioned thirty-square-mile-area, see e.g., Transcript 2805-2810, and the Court is therefore unable to find, at this juncture, that an "intent and preparedness" to extend MELP's geographical service area has, as a matter of law, not been demonstrated or that a "natural expansion" of MELP's existing retail business was not wrongfully frustrated.

Accordingly, defendant's motion is hereby denied insofar as it seeks a directed verdict on the issue of relevant geographic market.

CEI also seeks to avoid the imposition of any liability whatsoever by invoking the established principle that a "monopolist which achieves that status because of 'a superior product, business acumen, or historic accident,' cannot be faulted". Byars v. Bluff City News Co., Inc., 609 F.2d 843, 853 (6th Cir. 1979), quoting United States v. Grinnell Corp., supra. That is to say, CEI currently urges the Court to hold, as a matter of law, that the distribution of electric power at retail within the geographic market here in issue constitutes a natural monopoly and that, accordingly, conduct undertaken by the defendant in furtherance of any attempt to monopolize such market is not actionable under Section 2 of the Sherman Act. CEI argues more specifically in this regard that, in view of the existence of the alleged natural monopoly market, the defendant was under no affirmative obligation to deal with its direct competitor, the ***1315** City, and could therefore resist, with impunity, any and all of the plaintiff's efforts to secure from CEI a permanent interconnection and the wheeling of PASNY power.

Defendant predicates its natural monopoly contention upon two principal sources, those being (i) the testimony of the plaintiff's experts, see Transcript at pp. 3904-3907, 3938, 4322-4325; and (ii) the general recognition, reflected in both the case authorities and the pertinent scholarly literature, that the distribution of electric power at retail constitutes a natural monopoly.[3] In contesting defendant's claim, however, the City argues with considerable force that while the foregoing sources lend support to the assertion that the retail distribution of electricity generally represents a natural monopoly market, these particular sources fail, for the most part, to address

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the actual conditions prevailing in the specific geographic market here in question. The City notes in this regard that neither of the plaintiff's expert witnesses expressly opined, or were asked to so opine, that the retail distribution of electric power in the Cleveland area itself constitutes a natural monopoly market. The City argues further that defendant's natural monopoly contention is not entirely consistent with historic fact, as the evidence discloses, without contradiction, that each of the instant utility systems has in fact managed to survive the rigours of competition for a duration which now exceeds sixty (60) years.

The Court, having reviewed the record, cannot agree that the evidence adduced to date, even if buttressed by the aforementioned general recognition which defendant suggests should be judicially noticed, “points so strongly in favor” of CEI's natural monopoly claim that “reasonable minds could not come to a different conclusion”. Morelock, supra. While the Court acknowledges that a contrary result might arguably obtain in the event it was incumbent upon the plaintiff to disprove the existence of a natural monopoly, it would appear that the City bears no such burden. The District of Columbia Circuit Court of Appeals' decision in Hecht v. Pro-Football, Inc. supra, is instructive:

> The trial judge further instructed the jury, however, that (plaintiff-) Hecht bore the burden of proving that the (defendant-) Redskins did not have a natural monopoly...
>
> This part of the instruction, we think, was incorrect. It is the clear thrust of Alcoa (United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945)) that, once plaintiff has proven the defendant's maintenance of its monopoly power through conscious business practices, a rebuttable presumption is established that defendant has the requisite intent to monopolize. The defendant can defeat this presumption by showing that it had monopoly, as some have greatness, “thrust upon it”-that its power derives from “superior skill, foresight and industry” or (as is particularly relevant here) from the advantages of natural monopoly conditions. Both the Supreme Court, and the lower courts, have echoed this position. We are not called upon in this case to elaborate the various circumstances under which the burden of proof in s 2 cases might shift to defendant; we hold merely that when, as here, a defendant seeks to avoid a charge of monopolization by asserting that it has a natural monopoly owing to the market's inability to support two competitors, the defendant, and not the plaintiff, bears the burden of proof on that score.

Hecht, supra at 991 (footnotes omitted).

In view of the fact that comparatively little evidence has been adduced which demonstrates the actual market conditions prevailing in the particular geographic market here in issue, and in light of the fact that the evidence, viewed most favorably to the plaintiff, permits the inference that the instant market is reasonably capable of supporting more than one competitor, the Court is constrained to conclude that reasonable minds could indeed differ ***1316** on the question of whether the defendant has sustained its burden of establishing that the retail distribution of electric power in the Cleveland area constitutes a natural monopoly market. Having made this determination, the Court cannot currently accede to the defendant's request that the Court hold, as a matter of law, that CEI was under no obligation to deal with the plaintiff and was therefore justified in resisting interconnection and the wheeling of PASNY power. The Court observes in this respect that while it is well-settled that “as a general rule, there exists no duty to deal, so long as the determination is made unilaterally”, Byars, supra at 854, it is equally well-established that where a business enterprise “possesses monopoly power, added obligations are imposed on the defendant which would not attach in the ordinary refusal to deal context”. Id. at 855. Accordingly, a business possessing monopoly power ordinarily cannot wilfully refuse to deal with a competitor if the refusal is designed and calculated to foreclose competition or to remove or exclude a competitor by unfair, unreasonable or predatory practices or conduct. See Eastman Kodak Co. v. Southern Photo Materials Co., 273 U.S. 359, 47 S.Ct. 400, 71 L.Ed. 684 (1927); Lorain Journal v. United States, 342 U.S. 143, 72 S.Ct. 181, 96 L.Ed. 162 (1951); Otter Tail Power Co. v. United States, supra. In ascertaining whether a unilateral refusal to deal is sufficiently anticompetitive in nature to comprise unfair or predatory conduct, it would appear that the “overall impact of the monopolist's practices” must be assessed and a “thorough analysis” of the prevailing “fact situation” undertaken. Byars, supra at 860.

The Court would discern from the foregoing principles that, at this juncture of the proceedings, the issue of whether the defendant was justified in resisting the plaintiff's efforts to secure an interconnection and the wheeling of PASNY power is essentially a question for the jury's resolution, requiring the panel to take into account numerous factors, including, as a threshold matter, the question of whether CEI does in fact possess monopoly power in the relevant geographic market. The Court accordingly declines as improvident the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

defendant's invitation to hold and instruct the jury that CEI was under absolutely no compulsion to deal with the plaintiff in connection with the aforesaid endeavors.

The Court does find meritorious, however, the defendant's Rule 50(a) motion insofar as it seeks a determination that the City has failed to adduce sufficient proof in support of its contention that it has been unlawfully excluded from membership in the Central Area Power Coordinating Group, (CAPCO). The Court would observe initially that the plaintiff has utterly failed to sustain its burden of demonstrating that the exclusion from CAPCO was occasioned by the instant defendant's unilateral conduct, as required under the terms of this Court's Memorandum and Order of October 1, 1980, 538 F.Supp. 1287. The Court notes in this regard that while the evidence has disclosed that CEI did in fact oppose plaintiff's proposed membership in CAPCO as of August, 1973, and that this opposition persisted thereafter, the evidence further establishes, in uncontroverted fashion, that several other CAPCO members, including the Ohio Edison Company, its operating subsidiary Pennsylvania Power Company, and the Duquesne Light Company, similarly opposed the City's request for CAPCO membership. PTX 32, 764. The December 10, 1973 correspondence of John Arthur, Chairman of the Board and Chief Executive Officer of Duquesne Light, is particularly revealing:

> You have asked to join the Capco Power Pool and requested a response to your request. We assume that you will understand that Duquesne Light Company can answer only for itself and not for any other Capco company.
>
> We do not see an advantage from your entrance into the Capco group and we see serious disadvantages. Capco is a voluntary association in which each member reaches independent decision, and in which any member can frustrate joint action. We believe that Capco would not be operable as a practical matter with the addition of an electric operating entity of ***1317** your small size. We feel that your electric generating, transmission and distribution characteristics are so dissimilar from ours and the other Capco companies that you would not be a workable addition to Capco.
>
> In your letter you propose to become an owner of a small percentage share of certain power stations which are in various stages of planning and construction. In addition to the question whether it is legally proper for you to become such an owner, we think it would be very difficult if not impossible to replan and renegotiate all the complicated understandings and arrangements for individual power station construction which presently exist.

PTX 764.

There has been no evidence adduced which demonstrates, or which permits the reasonable inference that, the opposition of either Ohio Edison or Duquesne Light was in any way coerced, induced, or otherwise prompted by the instant defendant's conduct. The evidence thus demonstrates, without contradiction, that the plaintiff's exclusion from membership in CAPCO ultimately ensued as a consequence of opposition thereto which was shared by several CAPCO participants, and which was not simply the product of CEI's unilateral conduct. Under the instant circumstances, the Court is of the opinion that insufficient proof of CEI's unilateral conduct has been presented to warrant jury consideration of this particular contention.

The City has similarly failed, in connection with its CAPCO claim, to adduce sufficient proof of either its legal or financial ability to participate in the organization. It is clear from the record and the applicable authorities that while CAPCO contemplated at the time of the City's membership proposals joint ownership of various generating facilities, see DTX 1, Transcript at pp. 3398, 3408-3408, the City was prohibited from participating in such a manner by Section 6, Article XVIII of the Ohio Constitution, which, as authoritatively construed by the Ohio Supreme Court, proscribes arrangements whereby a municipality owns "part of property which is owned in part by another, so that the parts owned by both, when taken together, constitute but one property." State ex rel. Wilson v. Hance, 169 Ohio St. 457, 159 N.E.2d 741, Syllabus 3 at 742 (1959), approving Alter v. City of Cincinnati, 56 Ohio St. 47, 46 N.E. 69. Moreover, and without belaboring the point, the City has made no showing that it possessed the financial wherewithal to advance the substantial sums of capital necessary to fund entry into the CAPCO organization.

While the Court has, for the foregoing reasons, concluded that the defendant cannot be held liable for the plaintiff's failure to attain CAPCO membership, the Court, viewing the evidence most favorably to the plaintiff, is of the opinion that sufficient proof has been adduced to warrant jury consideration of the plaintiff's broader assertion that CEI has, apart from the denial of actual CAPCO membership, unlawfully and unilaterally denied the City access to the benefits of coordinated operations and development generally. Defendant's motion, insofar as it seeks a directed

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

verdict on this broader contention, as distinct from the question of CAPCO membership per se, is without merit and therefore denied.

The Court would observe lastly that, having reviewed the evidence heretofore adduced in light of the specific allegations of misconduct advanced in the plaintiff's Second Amended Complaint, it concurs with the defendant's assessment that the following allegations fail for lack of proof and are therefore no longer germane to this case:

1) the City's assertion that CEI has unlawfully refused to wheel or allow the transmission of electric power "from the plaintiff to any other electric utility system", Second Amended Complaint P 35(a);

2) the City's contentions that defendant has prevented the plaintiff from:

(a) "competing for industrial loads," id. P 36(3);

(b) "issuing bonds to finance improvements and extentions of its system", id. P 36(f); and

***1318** (c) "constructing transmission lines to interconnect its system with the electric systems of the Cities of Painesville and Orrville" id. P 36(i).

In accordance with the foregoing, the motion of the defendant for a directed verdict pursuant to Rule 50(a) is hereby granted in part, and denied in part, as appears more fully above.

IT IS SO ORDERED.

SUPPLEMENTAL OPINION

This matter is presently before the Court on a series of motions advanced by both parties pursuant to Rule 50(a), Fed.R.Civ.P., at the close of plaintiff's rebuttal evidence. During the course of proceedings conducted on October 28, 1980, the Court entertained oral arguments thereon. See Transcript at pp. 6216-6235.

Defendant, Cleveland Electric Illuminating Company (CEI), has inter alia renewed its request for a determination that the relevant geographic market is the thirty-square-mile-area within which plaintiff and defendant actually compete. Plaintiff, City of Cleveland (City) again maintains that the evidence is sufficient to present a jury question as to whether the 1,700-square-mile area comprising CEI's entire service territory constitutes the relevant geographic market for purposes of this case.

The plaintiff does not predicate its relevant market contention on the claim that MELP actually competed or could have competed in the latter area, see Transcript at pp. 6224-6226, and indeed the record is utterly devoid of evidence even suggesting the existence of or potential for retail service competition between the parties throughout the entire 1,700-square-mile territory. Rather, plaintiff maintains that the entire CEI service area constitutes the relevant geographic market because (1) MELP's actual competition with defendant within the aforesaid thirty-square-mile-area affects defendant's retail pricing throughout CEI's entire service territory, and (2) defendant "draws upon" its resources developed within that broader area to support and enhance its competitive efforts within the area of actual competition.

For reasons developed more fully below, however, the Court finds plaintiff's arguments legally insufficient to support its claim that the relevant geographic market comprises the entire aforesaid 1,700-square-mile area. As noted in this Court's Memorandum and Order of October 20, 1980:

> In ascertaining the scope of the relevant geographic market for Sherman Act purposes, it is incumbent upon the trier of fact to determine "where, within the area of competitive overlap, the effect of the (antitrust violation) on competition will be direct and immediate." United States v. Philadelphia National Bank, 374 U.S. 321, 83 S.Ct. 1715, 1738 (10 L.Ed.2d 915) (1963); United States v. Grinnell Corp., supra.

See City of Cleveland v. The Cleveland Electric Illuminating Co., 538 F.Supp. 1306, at 1313 (N.D.Ohio 1980). In other words, the relevant geographic market, for antitrust purposes, comprises that area within which the sellers of a commodity effectively compete, and in which prospective purchasers are effectively offered a choice as among alternative sources of supply. See e.g. United States v. Grinnell Corp., 384 U.S. 563, 86 S.Ct. 1698, 16 L.Ed.2d 778 (1966); Tampa Electric Company v. Nashville Coal Company, 365 U.S. 320, 81 S.Ct. 623, 5 L.Ed.2d 580 (1961). Plaintiff's arguments, however, ignore these established criteria of market definition.

The City's "price-influence" contention focuses not upon the "direct and immediate" effects of defendant's purported anticompetitive conduct, but rather upon indirect and secondary effects on defendant's retail service rates

(throughout its service area) resulting from plaintiff's conduct in competing with the defendant in the thirty-square mile area. Plaintiff has failed to demonstrate that the 1,700-square-mile territory was an "area of effective competition" between MELP and CEI, and the fact that actual competition between the parties within the aforesaid thirty-square-mile area might have affected defendant's ***1319** retail pricing throughout its entire service territory does not compel the conclusion that the latter area constitutes the relevant geographic market for purposes of this suit. Such an attempt to artificially expand the Sherman Act's scope of relevant geographic market was considered and rejected in West-Texas Utilities Co. v. Texas Electric Service Co., 470 F.Supp. 798 (N.D.Tex.1979) wherein Judge Porter disapproved a similar "price influence" contention:

> Some of plaintiffs' witnesses said that two utilities are in competition when one utility takes some action that will affect, in some way, the price charged by the other utility for its electric power. Thus, the defendants alleged refusal to operate electrically interstate has an effect on plaintiffs' prices, as evidenced allegedly from plaintiffs' economic testimony, and therefore plaintiffs are in competition with the defendants ...
>
> I should point out that if plaintiffs' view of competition is correct, then every Sherman Act case is really a price fixing case. If we accept plaintiffs' view of competition, then every purchaser has an ultimate choice of whether to buy a particular product, and every manufacturer in some way (significant or insignificant) affects the price of every commodity, thus there are no geographic limitations (and probably few product limitations) to the competitive market in an antitrust case.
>
> The case law also does not support such a broad reading of the term market in a Section 1 case, or for that matter, in a Section 2 case either.
>
> If I were to accept these definitions, I would, it seems to me, be virtually eliminating the concepts of geographic and product market from consideration in an antitrust case. Id. at 820-821.

Accordingly, the Court finds plaintiff's "price influence" argument legally insufficient to establish the 1,700-square-mile area as the relevant geographic market within the parameters of this suit.

Plaintiff's contention that the relevant geographic market constitutes that area of resources which defendant presumably "draws upon" to support its competition with MELP in the City of Cleveland is equally unsupportable. Such an argument also ignores the time-honored principles noted above that relevant geographic market is determined by reference to the "area of effective competition" or the area in which prospective purchasers are effectively offered a choice among alternative sources of supply, and focuses instead upon the mere size of the defendant's firm, or the territorial limits of its business activities. The Court is aware of no authority, and the plaintiff has cited none, which sanctions a definition of relevant geographic market dependent solely upon the boundaries of the defendant's business territory without reference to "areas of competitive overlap." While this Court has recognized that business activities carried on in one "market" or phase of an industry may affect competition in another, see City of Cleveland v. The Cleveland Electric Illuminating Co., supra at 1310 and 1313; see also Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263 (2d Cir. 1979), cert. denied, 444 U.S. 1093, 100 S.Ct. 1061, 62 L.Ed.2d 783 (1980), such does not compel the conclusion that the relevant geographic market encompasses the entire area wherein a defendant conducts its business. The relevant geographic market within the purview of the Sherman Act remains the area of "competitive overlap" within which the "direct and immediate" effects of the antitrust violations are manifested.

The logical extension of plaintiff's argument would not only lead to absurd results but would serve to "virtually eliminat(e) the concept of geographic ... market from consideration in an antitrust case." West-Texas Utilities Co., supra 470 F.Supp. at 821.

For the foregoing reasons, the Court concludes, as a matter of law, that the relevant ***1320** geographic market does not constitute the 1,700-square-mile area comprising CEI's entire retail service territory. The Court, however, is fully cognizant that "(t)he boundaries of the geographic area ... must be drawn so as to take into account not only existing but potential competition as well," City of Cleveland v. The Cleveland Electric Illuminating Co., supra at 1313, and that "(t)he record reflects at least some evidence of plaintiff's efforts to extend its existing retail sales market beyond the aforementioned thirty-square-mile area," Id. at 1314, see Transcript at pp. 1134-1146, 2805-2810, and even beyond the boundaries of the City of Cleveland. See Transcript at pp. 1139-1141, 2808-2810. Viewing this evidence of potential competition in

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

a light most favorable to the City, the Court concludes that reasonable minds might differ as to the precise parameters of the "area of effective competition" and, accordingly, the issue, as limited hereinabove, will be submitted to the jury for its determination upon proper instructions.

Upon review of the record in its entirety as well as the authorities cited in this Court's Memorandum Opinion of October 20, 1980, the Court concludes that all remaining Rule 50(a) motions advanced or renewed by either party at the close of plaintiff's rebuttal evidence, with the exceptions noted below, [1] are properly denied.

IT IS SO ORDERED.

All Citations

538 F.Supp. 1306

Footnotes

1 The fact that the motions at bar are in the nature of motions for a directed verdict, as opposed to the motion for a judgment n.o.v. specifically considered in Morelock, supra, is of no consequence here, as the case authorities have recognized that the applicable standards are the same for both procedural devices. Dulin v. Circle F Industries, Inc., 558 F.2d 456, 465 (8th Cir. 1977); Yazzie v. Sullivent, 561 F.2d 183, 188 (10th Cir. 1977); Boeing Co. v. Shipman, 411 F.2d 365, 374 (5th Cir. 1969); Neville Chemical Co. v. Union Carbide, 422 F.2d 1205, 1210 (3d Cir. 1970); 9 Wright and Miller, Federal Practice and Procedure s 2524 at 541-542 (1971).

2 While plaintiff accepts the characterization of regional power exchanges as "areas of cooperation," see Plaintiff's Reply Brief (filed herein July 14, 1980), rather than competition, it asserts that the inference "that if there is cooperation there is no market is mistaken: all markets are areas of cooperation." Reply Brief at 10 n.5. To accept the notion that competition and cooperation are not relevant distinctions in defining a market because, presumably, buyers and sellers must "cooperate" to consummate a transaction, is to shred the fabric of anti-trust law and to ignore the economic realities of competitive market structure.

3 Defendant submits that this recognition is of such a nature that judicial notice thereof may properly be taken pursuant to Rule 201, Fed.R.Ev.

1 The issues concerning (1) the applicability of the pass-on defense, and (2) limitation of damages resulting from CEI's refusal to wheel PASNY power are the subject of a separate Memorandum Opinion.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-11

KeyCite Yellow Flag - Negative Treatment
Distinguished by Restoration 1 of Port St. Lucie v. Ark Royal Insurance Company, Fla.App. 4 Dist., September 5, 2018

974 So.2d 368
Supreme Court of Florida.

CONTINENTAL CASUALTY COMPANY, etc., Petitioner,
v.
RYAN INCORPORATED EASTERN, etc., et al., Respondents. [1]
Lumbermens Mutual Casualty Company, Petitioner,
v.
Ryan Incorporated Eastern, etc., et al., Respondents.

Nos. SC05–1935, SC05–1816.
|
Jan. 24, 2008.

Synopsis

Background: Contractor and surety brought declaratory judgment action against insurers that issued primary and excess commercial general liability (CGL) policies to contractor for failing to defend and indemnify contractor and surety for the damages paid in underlying lawsuit brought by owner of golf course constructed by contractor. The Circuit Court, Collier County, Ted H. Brousseau, J., awarded summary judgment to insurers. Contractor and surety appealed, and filed motion for attorney fees. The District Court of Appeal, 910 So.2d 298,reversed and remanded, granted motion for attorney fees, and certified a conflict. Insurers filed application for review.

Holdings: The Supreme Court, Pariente, J., held that:

absent written assignment from contractor, surety was not entitled to recover its attorney fees;

general indemnity agreement between surety and contractor did not constitute an assignment of the rights of contractor to sue its insurers; and

surety was not entitled to award of attorney fees based on an implied assignment from contractor.

Decision of District Court of Appeal quashed.

Wells, J., concurred in result only and filed opinion.

Anstead, J., concurred in part, dissented in part, and filed opinion.

Procedural Posture(s): On Appeal; Motion for Summary Judgment.

Attorneys and Law Firms

***371** Jonathan L. Gaines of Karen L. Stetson, P.A., Miami, FL, and William M. Martin of Peterson Bernard, Fort Lauderdale, FL, for Continental Casualty Company, Petitioner.

Patrick E. Maloney of Tressler, Soderstrom, Maloney, and Priess, LLP, Chicago, IL, and Robert L. Donald of the Law Office of Sherman and Donald, Fort ***372** Myers, FL, for Lumbermens Mutual Casualty Company, Petitioner.

Steven G. Schember and Duane A. Daiker of Shumaker, Loop, and Kendrick, LLP, Tampa, FL, for Respondents.

Opinion

PARIENTE, J.

This Court has for review *Ryan Inc. Eastern v. Continental Casualty Co.,* 910 So.2d 298 (Fla. 2d DCA 2005), in which the Second District Court of Appeal certified conflict with *Western World Insurance Co., Inc. v. Travelers Indemnity Co.,* 358 So.2d 602 (Fla. 1st DCA 1978). The conflict issue is whether a surety that pays money on behalf of its principal and is subrogated to any rights the principal has against its own insurer under principles of equitable subrogation is entitled to recover its attorney's fees under section 627.428, Florida Statutes (2006), for prevailing in a coverage dispute against the principal's insurer. We have jurisdiction. *See* art. V, § 3(b)(4), Fla. Const. We conclude that a surety that has no written assignment from the insured and is not a named or omnibus insured or named beneficiary under the policy is not entitled to attorney's fees under section 627.428. Accordingly, we quash the Second District's decision in *Continental,* which granted a motion for fees by the surety, and approve the First District's decision in *Western World,* which denied a similar request for fees.

FACTS AND PROCEDURAL HISTORY

In November 2000, Ryan Incorporated Eastern (Ryan), as contractor, entered into a contract with 951 Land Holdings, Ltd. (951 Land Holdings), as owner of the property, to construct a golf course in Collier County. This contract required Ryan to obtain commercial general liability ("CGL") insurance. Ryan obtained two separate CGL policies. The primary insurance policy was issued by Continental Casualty Company (Continental) and the excess policy was issued by Lumbermens Mutual Casualty Company (Lumbermens). In December 2000, Ryan, as the principal, and Hartford Fire Insurance Company (Hartford), as the surety, executed performance and payment bonds to 951 Land Holdings, which were subject to an August 1994 General Indemnity Agreement (GIA) between Ryan and Hartford.

After completion of the golf course, 951 Land Holdings sued Ryan and Hartford for damages resulting from contaminated grass supplied by Ryan's subcontractor. The case proceeded to mediation, after which Hartford paid approximately $4.7 million in claims, fees and expenses to settle the dispute. [2] Subsequently, Ryan and Hartford instituted a declaratory judgment action against Continental and Lumbermens for failing to defend and indemnify Ryan and Hartford for the damages paid in the lawsuit brought by 951 Land Holdings. Ryan and Hartford filed a joint motion for summary judgment. Continental and Lumbermens each filed cross-motions for summary judgment. The trial court granted summary judgment in favor of Continental and Lumbermens, concluding that there was no insurance coverage under the CGL policies based on the faulty workmanship of the subcontractor. Ryan and Hartford appealed the decision on coverage and filed a motion for appellate attorney's fees under section 627.428.

On appeal, the Second District Court of Appeal reversed the final summary judgment in favor of Continental and Lumbermens ***373** on the underlying coverage issue and "[remanded] this case to the circuit court for further proceedings on the authority of *J.S.U.B., Inc. v. United States Fire Insurance Co.,* 906 So.2d 303 (Fla. 2d DCA 2005)." *Continental,* 910 So.2d at 299. [3] As to appellate attorney's fees, the court granted Ryan and Hartford's motion "conditioned upon the ultimate entry of judgment in favor of the Contractor and the Surety on remand." *Id.* at 301. The Second District determined that when a surety such as Hartford makes payment for its principal, "the surety becomes subrogated to the rights and remedies of its principal." *Id.* at 300. Because of its payment, the Second District reasoned that the surety "stands in the shoes of the Contractor as a first party claimant under the CGL policies" and is equally entitled to an award of fees under section 627.428. *Id.* at 301.

The Second District further elaborated on public policy considerations. Specifically, the court explained that because the GIA between Ryan and Hartford required Ryan to reimburse Hartford for any fees associated with the enforcement of the bond, a denial of fees to Hartford would make Ryan liable for those fees with no possibility of reimbursement from the insurers. *See id.* Because this result would contradict the purpose of section 627.428—to discourage the contesting of valid claims by insurance companies—and would "exalt[ ] form over substance," as the principal could have carried the ball in the litigation and been entitled to the same fees, the court conditionally granted Hartford's motion. *See id.*

In reaching this decision, the Second District certified conflict with *Western World.* In *Western World,* the surety and its principal sued the liability insurer for its failure to defend the principal and sought reimbursement for the money the surety paid on the bond. *See* 358 So.2d at 603. Similar to the Second District in *Continental,* the First District held that when a surety pays a judgment for the principal, the surety may be indemnified from the principal and is subrogated to any rights the principal has against its insurance carrier. *See id.* at 604. However, on nearly identical facts, the First District concluded that the surety was not entitled to its appellate fees because it was neither a named insured nor named beneficiary under the liability policy. *See id.* We accepted jurisdiction to resolve this conflict.

ANALYSIS

A. Overview of Section 627.428

This case requires us to review section 627.428, Florida Statutes (2006). [4] Because this issue involves the interpretation of a statute, our review is de novo. *Brass & Singer, P.A. v. United Auto. Ins. Co.,* 944 So.2d 252, 253 (Fla.2006). Section 627.428, a provision of the Florida Insurance Code, was originally enacted in 1959, *see* ch. 59–205, § 477, Laws of Fla., and has been the subject of extensive interpretation ***374** by both Florida and federal courts. *See,*

e.g., Fireman's Fund Ins. Co. v. Tropical Shipping & Constr. Co., 254 F.3d 987 (11th Cir.2001); *Dadeland Depot, Inc. v. St. Paul Fire & Marine Ins. Co.,* 945 So.2d 1216 (Fla.2006); *Brass & Singer,* 944 So.2d at 253–54; *David Boland, Inc. v. Trans Coastal Roofing Co.,* 851 So.2d 724 (Fla.2003); *Roberts v. Carter,* 350 So.2d 78 (Fla.1977). Although the section authorizes an award of attorney's fees, it does so only in a discrete set of circumstances. The statute provides in pertinent part that

> [u]pon the rendition of a judgment or decree by any of the courts of this state against an insurer and in favor of any named or omnibus insured or the named beneficiary under a policy or contract executed by the insurer, the trial court or, in the event of an appeal in which the insured or beneficiary prevails, the appellate court shall adjudge or decree against the insurer and in favor of the insured or beneficiary a reasonable sum as fees or compensation for the insured's or beneficiary's attorney prosecuting the suit in which the recovery is had.
> § 627.428(1), Fla. Stat.

As with any case of statutory construction, we begin with the "actual language used in the statute." *Borden v. East–European Ins. Co.,* 921 So.2d 587, 595 (Fla.2006). This is because legislative intent is determined primarily from the text. *See Maggio v. Fla. Dept. of Labor & Employment Sec.,* 899 So.2d 1074, 1076–77 (Fla.2005). The plain language of section 627.428 provides for an award of attorney's fees to a "*named* or *omnibus insured* or the *named beneficiary* " who obtains a judgment or decree against an insurer. § 627.428, Fla. Stat. (emphasis supplied).

A "named insured" is one who is "designated as an insured" under the liability policy. *Romero v. Progressive Southeastern Ins. Co.,* 629 So.2d 286, 288 (Fla. 3d DCA 1993). An "omnibus insured" is one who is covered by a provision in the policy but not specifically named or designated. *See Industrial Fire & Cas. Ins. Co. v. Prygrocki,* 422 So.2d 314, 315 (Fla.1982) (holding that a pedestrian was an omnibus insured under a liability policy providing coverage for medical and other expenses incurred as a result of bodily injuries sustained by "a pedestrian, through being struck by the insured motor vehicle"); *State Farm Fire & Cas. Co. v. Kambara,* 667 So.2d 831, 831–32 (Fla. 4th DCA 1996) (holding that a resident was an omnibus insured under a landlord's liability policy that provided coverage for "bodily injury caused by an accident on your premises you own or rent"). Additionally, the rights of an "omnibus insured" flow "directly from his or her status under a clause of the insurance policy without regard to the issue of liability." *Kambara,* 667 So.2d at 833. A "named beneficiary" is one who is specifically designated as such in the policy. *See Roberts,* 350 So.2d at 79.

Hartford does not contend that it falls within the narrow statutory class of entities outlined in section 627.428. Rather, it argues that it is entitled to an award of fees by standing in the shoes of Ryan, the "named insured" under the CGL policies, as both an assignee and equitable subrogee. Thus, the issue we must resolve is whether a surety that itself does not fall within any statutory classification may nevertheless recover attorney's fees by virtue of its relationship to an insured. [5]

*375 B. Assignment versus Subrogation

A surety may obtain standing to sue its principal's liability insurer either through an assignment, under principles of subrogation, or both. Despite the express limitations in section 627.428 as to the class of designated entities entitled to recover attorney's fees, this Court has previously approved an award of attorney's fees in situations where policy coverage was obtained through an assignment from an insured. The assignment exception is derived from language in our decision in *Roberts,* where we rejected an award of attorney's fees in favor of a third-party beneficiary of an insurance contract. 350 So.2d at 79.

In *Roberts,* an insurer and its insured appealed a district court decision authorizing an award of attorney's fees to an injured party under section 627.428. *Id.* at 78. The injured party was neither an "insured [n]or the named beneficiary" under the policy, but was entitled to sue the insurer because of its status as a third-party beneficiary. *See id.* at 79. [6] Because the injured third party did not fall within the narrow class of entities authorized to recover fees under the statute, we reversed the district court's award. *See Roberts,* 350 So.2d at 79. In reaching this decision, we held that

> an award of attorney's fees under Section 627.428(1) is available only to the contracting insured, the insured's estate, specifically named policy beneficiaries, and third parties who claim policy coverage by assignment from the insured.
> *Id.* (footnotes omitted).

By using the phrase "contracting insured," we unintentionally created confusion as to whether an "insured" other than the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

"contracting insured" could recover its fees under the statute. *See Prygrocki,* 422 So.2d at 315–16. However, we clarified that the term "contracting insured" was not intended to revise the language of the provision, but rather to distinguish between those persons insured under an insurance contract and the third party claimant at issue in *Roberts. See id.* at 316. We reiterated that the unambiguous terms of the statute clearly applied to all insureds under an insurance policy. *See id.* Furthermore, the Legislature amended the statute in 1982 to include "any named or omnibus insured or the named beneficiary." Ch. 82–243, § 376, Laws of Fla.

Unfortunately, in another decision regarding the assignment exception we recognized in *Roberts,* this Court may have created confusion by using the words "assignee" and "subrogee" interchangeably. *See Fid. & Deposit Co. v. First State Ins. Co.,* 677 So.2d 266, 267, 269 (Fla.1996). In *First State,* an entity received an assignment from the insured for the right to recover under the insured's insurance policy. However, we held that the assignee, as the insured's "subrogee, will be entitled to attorney's fees should it ultimately prevail in this litigation." *Id.* at 269. As cogently stated in 16 Lee R. Russ & ***376** Thomas F. Segalla, *Couch on Insurance* 3d (2005),

> [t]he distinction between rights arising by virtue of an assignment and by way of subrogation is frequently obscured by defining one in terms of the other, in a manner which makes it difficult to tell whether the usage was an intentional recognition that the two theories are considered as equivalent or an unintentional usage in a context where the difference was unimportant.

Id. § 222:54 (footnotes omitted).

Although we agree that the terms can be interrelated and are often confused, assignment and subrogation remain distinct legal concepts. Thus, the question we must resolve is whether, for purposes of the attorney's fees statute, obtaining the right to sue the insurer via equitable subrogation is functionally equivalent to obtaining that right through an assignment. Because the rights acquired under an assignment differ from the rights acquired by virtue of subrogation, we decline to equate these two distinct principles.

An assignment has been defined as "a transfer or setting over of property, or of some right or interest therein, from one person to another." *Black's Law Dictionary* 128 (8th ed.2004) (quoting Alexander M. Burrill, *A Treatise on the Law and Practice of Voluntary Assignments for the Benefit of Creditors* § 1, at 1 (James Avery Webb ed., 6th ed. 1894)). Essentially, it is the "voluntary act of *transferring* an interest." *DeCespedes v. Prudence Mut. Cas. Co.,* 193 So.2d 224, 227 (Fla. 3d DCA 1966); *accord Fla. Power & Light Co. v. Road Rock, Inc.,* 920 So.2d 201, 204 (Fla. 4th DCA 2006); 3A Fla. Jur.2d *Assignments* § 1 (2007); 6 Am.Jur.2d *Assignments* § 1 (2007). Importantly, once transferred, the assignor no longer has a right to enforce the interest because the assignee has obtained all "rights to the thing assigned." *Price v. RLI Ins. Co.,* 914 So.2d 1010, 1013–14 (Fla. 5th DCA 2005) (quoting *Lauren Kyle Holdings, Inc. v. Heath–Peterson Constr. Corp.,* 864 So.2d 55, 58 (Fla. 5th DCA 2003)).

On the other hand, subrogation is a broader concept, involving "an act of law growing out of the relation of the parties to the original contract of insurance," 16 Russ & Segalla, *supra,* § 222:53, where one entity pays the debt or discharges the obligations of another. *See* 22 Eric Mills Holmes, *Holmes' Appleman on Insurance* 2d § 141.1[B] (2003). Two types of subrogation have been recognized-conventional and equitable. Conventional subrogation is created by an agreement between the parties whereby one party having no interest in the matter discharges the debt of another and is thus entitled to the "rights and remedies of the original creditor." *Dade County Sch. Bd. v. Radio Station WQBA,* 731 So.2d 638, 646 (Fla.1999). Essentially, it is an agreement "that the party paying the debt will be subrogated to the rights of the original creditor." *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. KPMG Peat Marwick,* 742 So.2d 328, 332 (Fla. 3d DCA 1999), *approved,* 765 So.2d 36 (Fla.2000). Indeed, an assignment could be part of a conventional subrogation agreement.

Unlike conventional subrogation, which is created by an express agreement, equitable (sometimes referred to as legal) subrogation arises by operation of law. *See DeCespedes,* 193 So.2d at 227; 31A Fla. Jur.2d *Insurance* § 3295 (2002). Equitable subrogation has been defined as "the substitution of one party for another whose debt the party pays, entitling the paying party to rights, remedies, or securities that would otherwise belong to the debtor." *Black's Law Dictionary* 1467. ***377** Basically, it is an equitable remedy created "by the legal consequences of the acts and relationships

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

of the parties." *Radio Station WQBA,* 731 So.2d at 646. Accordingly, equitable subrogation, "the object of which is to prevent injustice," is governed by the principles of equity. Holmes, *supra,* § 141.1 [C] [1].

The Second District premised its award of attorney's fees on equitable subrogation, which is a remedy commonly associated with surety relationships. As we explained in *Transamerica Insurance Co. v. Barnett Bank of Marion County,* 540 So.2d 113, 116 (Fla.1989) (quoting *Pearlman v. Reliance Ins. Co.,* 371 U.S. 132, 137, 83 S.Ct. 232, 9 L.Ed.2d 190 (1962)), a surety "who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed." In the context of a surety relationship, the key to equitable subrogation lies in the surety's right to indemnification. Because a surety who pays a judgment on behalf of its principal is entitled to indemnification by its principal, it has the right to be subrogated to any rights the principal has against its liability insurer if that judgment is covered by the principal's liability policy. *See Western World,* 358 So.2d at 604.

Although the surety may stand in the shoes of the principal, the principal does not lose its status as an insured under the policy. In fact, as is evident from Ryan's involvement in the underlying litigation in this case and the principal's involvement in the underlying coverage dispute in *Western World,* the insured principal retains its right to sue for insurance coverage. Because the principal retains its rights under the policy, which includes the statutory right to claim attorney's fees, the surety does not acquire the principal's status as one of the designated entities entitled to attorney's fees under the statute. This prevents the insurer from being subject to a claim for attorney's fees from both the principal (insured) and the surety (subrogee) when, as in this case, both litigate the same coverage issue. On the other hand, an assignment transfers all of the insured's rights to a claim under the policy, including its status as an insured under the policy. Thus, an assignee is entitled to an award of fees under section 627.428. *See Roberts,* 350 So.2d at 79.

We reaffirm our holding in *Roberts* that only the named or omnibus insured, the insured's estate, specifically named beneficiaries under the policy, and other third parties who claim policy coverage through an assignment are entitled to an award of fees under section 627.428. *See id.* at 78–79. Hartford does not fall within the narrow class of entities identified in the statute. Thus, the only way Hartford can recover its fees in this declaratory judgment action is through a valid assignment from Ryan, the named insured under the CGL policies.

C. Alternative Grounds

Although not raised in the Second District, Hartford argues that it obtained a valid assignment of Ryan's rights under the CGL policies through the General Indemnity Agreement (GIA) entered into between Hartford and Ryan in 1994.[7] We have authority to consider alternative ***378** grounds for affirming the decision below that were not raised by the parties. *See Radio Station WQBA,* 731 So.2d at 644. However, after examining the language of the 1994 GIA, we conclude that it does not constitute an assignment of the rights of the principal to sue its insurer for insurance coverage after the dispute arose.

Hartford also asserts that it is entitled to an award of fees under the statute based on an implied assignment, similar to the one we recognized under the unique circumstances in *All Ways Reliable Building Maintenance, Inc. v. Moore,* 261 So.2d 131 (Fla.1972). In that case, a house repair company brought suit against both the owner and the insurance company that covered the owner's house for fire damage. *Id.* at 131. The owner filed a cross-claim arguing that the insurer was responsible because the insurer's agent had *preapproved* All Ways' estimate for the repairs. *Id.* The trial court awarded judgments in favor of All Ways and the owner and approved an award of attorney's fees to both parties. *Southern Am. Fire Ins. Co. v. All Ways Reliable Bldg. Maint., Inc.,* 251 So.2d 11, 13 (Fla. 4th DCA 1971).

In approving the trial court's award, this Court determined that a contract between All Ways and the insurance company arose by implication. *All Ways,* 261 So.2d at 132. This implied contract "logically included an assignment" of the owner's claim against the insurer. *Id.* We stated that

> [u]nder such circumstances it is highly technical and unrealistic to take the view that [the statute] does not authorize an attorney's fee for All Ways Reliable. All Ways Reliable was found by implication of the related circumstances to be the assignee of the insured Elsie Moore's loss claim against the insurance company; and,

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> having successfully sued the insurance company which denied the claim for the amount representing the fire loss, was entitled concomitantly to the attorney's fee.

Id. We held that, despite being neither a named insured nor a named beneficiary under the policy, All Ways was entitled to an award of its attorney's fees based on an implied assignment from the owner. *Id.*

The circumstances justifying the implied assignment in *All Ways* are distinguishable from the facts in this case. Hartford did not perform under the bond as a result of the insurers' determination that the damage was covered by the CGL policies. To the contrary, the insurers maintain that they disputed liability from the beginning, even before Hartford settled the underlying litigation. Moreover, Hartford had a duty to perform under the surety bond regardless of whether the CGL policies covered the damage. Hartford does not, and simply cannot, allege that it detrimentally relied, as the repair company did in *All Ways,* upon an approval from the insurers prior to performing under the bond. Therefore, there are no circumstances that would justify the existence of either an implied contract or implied assignment between the surety and insurers in this case. To the extent that our decision in *All Ways* appears to recognize an equitable basis for recovering attorney's fees under section 627.428, we limit that case to its unique facts.

Hartford lastly argues that "a denial of fees to the Surety would lead to the Contractor's responsibility to indemnify the Surety for payment of its fees without the possibility of reimbursement from the Primary Insurer and the Excess Insurer." *Continental,* 910 So.2d at 301. Essentially, the argument is that a denial of fees to Hartford would "exalt form over substance," because Ryan is liable for Hartford's fees regardless of the outcome of this appeal. *Id.* Continental and Lumbermens do not agree that the contractor, as ***379** principal, would be liable under the GIA for the surety's attorney's fees in the underlying coverage dispute. We do not interpret the GIA agreement. Even assuming that Hartford is correct, it is outside this Court's purview to correct a potential inequity by interpreting a statute contrary to its plain language.

Our conclusion does not rest on whether it is sound public policy to allow a surety to recover its attorney's fees from the insurer under these circumstances. If there is an injustice that requires the expansion of the statutory class of entities entitled to recover attorney's fees under section 627.428, that argument is one best addressed by the Legislature. *See Parker v. Parker,* 950 So.2d 388, 394 (Fla.2007); *Dowell v. Gracewood Fruit Co.,* 559 So.2d 217, 218 (Fla.1990).

CONCLUSION

As we held in *Roberts* and again reaffirm today, section 627.428 authorizes an award of attorney's fees only to "the named or omnibus insured or named beneficiary" under an insurance policy and to other third parties who obtain coverage based on an assignment from an insured. Ryan, as the named insured under these policies, has always been entitled to its fees in prosecuting this declaratory judgment action against its insurers. However, absent an assignment, Hartford as a surety is not entitled to attorney's fees from the insurer under 627.428.

For the foregoing reasons, we quash the Second District's decision in *Continental* granting attorney's fees in favor of Hartford and approve the First District's decision in *Western World* denying fees to a surety that failed to obtain an assignment. This case is remanded for further proceedings not inconsistent with this opinion.

It is so ordered.

LEWIS, C.J., and QUINCE and BELL, JJ., concur.

WELLS, J., concurs in result only with an opinion.

ANSTEAD, J., concurs in part and dissents in part with an opinion.

CANTERO, J., recused.

WELLS, J., concurring in result only.
I concur with the decision of the majority to quash the decision of the Second District Court of Appeal in this case and to approve the decision of the First District Court of Appeal in *Western World Insurance Co., Inc. v. Travelers Indemnity Co.,* 358 So.2d 602 (Fla. 1st DCA 1978). As the First District did, I would deny attorney fees under section 627.428 because Hartford Fire Insurance Company is not a named or omnibus insured or a beneficiary under the insurance policy.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

ANSTEAD, J., concurring in part and dissenting in part.
I dissent from the majority's conclusion, and conclude that Hartford is entitled to attorney's fees. Since Hartford's claim on the policy is solely through Ryan as an insured under the policy, it should not make a difference whether Hartford is called an assignee or a subrogee, or is claiming insurance benefits for the use and benefit of Ryan as Hartford is entitled to do as Ryan's surety. It makes no sense that Hartford would be entitled to press Ryan's rights to insurance coverage but would be denied attorney's fees after successfully doing so.

In granting Hartford's motion for attorney's fees under section 627.428, the Second District, in a concise and well-reasoned opinion by Judge Wallace, explained:

> ***380** Where, as in this case, a surety properly makes payment to correct defective construction or to complete a construction project undertaken by its principal, the surety becomes subrogated to the rights and remedies of its principal. It follows that the Surety is subrogated to any rights which the Contractor may have against its CGL carriers. For this reason, we conclude that the Surety stands in the shoes of the Contractor as a first party claimant under the CGL policies. As a first party claimant standing in the shoes of the Contractor, the Surety is entitled to an award of fees under the statute. Moreover, the Contractor executed a general indemnity agreement in favor of the Surety, which required it to indemnify the Surety for its court costs and attorney's fees. Thus a denial of fees to the Surety would lead to the Contractor's responsibility to indemnify the Surety for payment of its fees without the possibility of reimbursement from the Primary Insurer and the Excess Insurer. Such a result would be contrary to the goals of section 627.428. Besides, the opposing view exalts form over substance. The Surety could have achieved the same outcome by arranging for the Contractor's attorney to carry the ball in the litigation.

Continental, 910 So.2d at 300–01 (footnote and citations omitted). Despite the fact that Hartford was neither a named or omnibus insured nor a named beneficiary under the CGL policies, the Second District concluded that Hartford, as a surety, was effectively and legally subrogated to the rights and remedies of Ryan, its principal, and therefore entitled to an award of attorney's fees under the statute. *See id.*

"Subrogation is the substitution of one person in the place of another with reference to a lawful claim or right." *Dade County Sch. Bd. v. Radio Station WQBA,* 731 So.2d 638, 646 (Fla.1999) (quoting *W. Am. Ins. Co. v. Yellow Cab Co.,* 495 So.2d 204, 206 (Fla. 5th DCA 1986)). Equitable subrogation, also referred to as legal subrogation, "is not created by a contract, but by the legal consequences of the acts and relationships of the parties." *Dade County,* 731 So.2d at 646. In general, equitable subrogation is appropriate where:

> (1) the subrogee made the payment to protect his or her own interest, (2) the subrogee did not act as a volunteer, (3) the subrogee was not primarily liable for the debt, (4) the subrogee paid off the entire debt, and (5) subrogation would not work any injustice to the rights of a third party.

Id. (citing *Fowler v. Lee,* 106 Fla. 712, 143 So. 613, 614 (1932)). The party who has discharged the debt "stands in the shoes" of the party whose claim has been discharged and therefore is entitled to the "right and priorities of the original creditor." *Id.*

Equitable subrogation is clearly applicable in the context of sureties. *See, e.g., Transamerica Ins. Co. v. Barnett Bank of Marion County,* 540 So.2d 113, 116 (Fla.1989) ("[T]here are few doctrines better established than that a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed.") (quoting *Pearlman v. Reliance Ins. Co.,* 371 U.S. 132, 137, 83 S.Ct. 232, 9 L.Ed.2d 190 (1962)). When a surety performs or

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

pays on behalf of its principal, it becomes “subrogated to the rights” of both its principal and its obligee. *Argonaut Ins. Co. v. Commercial Standard Ins. Co.,* 380 So.2d 1066, 1068 (Fla. 2d DCA 1980); *accord Auto Owners Ins. Co. v. Travelers Cas. & Sur. Co.,* 227 F.Supp.2d 1248, 1259 (M.D.Fla.2002); *Transamerica,* 540 So.2d at 115–16; *U.S. Fid. & Guar. Co. v. N. Am. Steel Corp.,* 335 So.2d 18, 20 (Fla. 2d DCA 1976). Although ***381** limited to the “extent of performance or payment,” the surety is “entitled to all the rights of the person [it] paid to enforce [its] right to be reimbursed.” *Transamerica,* 540 So.2d at 116 (quoting *Pearlman,* 371 U.S. at 137, 83 S.Ct. 232). Hence, to the extent that a surety performs on behalf of its principal an obligation that is covered by the policies of a principal's liability insurers, the surety stands in the shoes of its principal and is subrogated to the rights of its principal under those policies. *See Western World Ins. Co. v. Travelers Indem. Co.,* 358 So.2d 602, 604 (Fla. 1st DCA 1978); *see also Auto Owners,* 227 F.Supp.2d at 1260. Accordingly, a surety who performs its obligations under the surety contract is entitled to assert the rights and remedies available to the principal against an insurer in order to seek reimbursement for its outlays under the surety contract.

The majority contends that even if a surety is entitled to stand in the shoes of an insured, it does so in a limited fashion. Citing to *Western World,* the majority holds that a surety's right to subrogation is limited to the rights the principal is owed under the policy with respect to indemnification and nothing more. However, no one disputes that a principal is entitled to seek recovery from its insurer for damage that is allegedly covered by the policy, and, if the insurer fails to defend the principal, the principal is entitled to recover its attorney's fees because it was forced to sue the insurer to enforce its insurance contract. *See* § 627.428, Fla. Stat. Importantly, when a surety and a principal are forced to sue the principal's liability insurer seeking declaratory judgment that the damage paid by the surety is covered by the policies, the surety is not seeking any rights greater than is already owed to the principal under the policy and under the attorney's fees statute.

An award of “fees has generally been denied when other persons have litigated the issue of insurance coverage on their own behalf,” such as in third party beneficiary cases. *Roberts v. Carter,* 350 So.2d 78, 79 (Fla.1977). Where a third-party is not named in the policy or otherwise standing in the shoes of an insured, courts have been reluctant to award attorney's fees. *See Indus. Fire & Cas. Ins. Co. v. Prygrocki,* 422 So.2d 314, 316 (Fla.1982) (stating that “[t]hird-party claimants, as *Roberts* held, are not within the class of insureds” contemplated by the statute); *Roberts,* 350 So.2d at 79 (refusing to award attorney's fees to a third party beneficiary who was not named in the policy); *see also Am. E. Dev. Corp. v. Everglades Marina, Inc.,* 608 F.2d 123 (5th Cir.1979) (refusing to grant attorney's fees to a third-party beneficiary who was not named in the policy); *Essex Builders Group, Inc. v. Amerisure Ins. Co.,* 429 F.Supp.2d 1274, 1290–91 (M.D.Fla.2005) (refusing to grant attorney's fees to an excess insurer because the excess insurer had not expended any fees on behalf of an insured, which would have allowed it to stand in its shoes to recover under the statute).

However, in situations where a third party has obtained rights by “standing in the shoes” of an insured, the law in Florida has allowed a recovery of attorney's fees. *See, e.g., All Ways Reliable Bldg. Maint., Inc. v. Moore,* 261 So.2d 131 (Fla.1972) (allowing an assignee of an insured to recover its attorney's fees under the statute); *see also Kivi v. Nationwide Mut. Ins. Co.,* 695 F.2d 1285, 1288–89 (11th Cir.1983) (allowing an assignee of an insured to recover its fees); *Stuyvesant Ins. Co. v. Nardelli,* 286 F.2d 600, 604 (5th Cir.1961) (approving an award of attorney's fees to an indemnitee under the statute); *but see Western World,* 358 So.2d at 604 (refusing to grant attorney's fees to a surety who was subrogated to the rights of its principal).

***382** Although this Court has yet to decide a case under the precise circumstances at issue here, it has interpreted section 627.428 in situations involving an insured's assignee. This Court has concluded that an award of attorney's fees is appropriate in favor of an insured's assignee who successfully sues an insurance company that contested a claim under the policy. *See All Ways,* 261 So.2d at 132. In *All Ways,* a house repairer brought suit against both the owner and the insurance company that covered the owner's house for fire damage. *Id.* at 131. The owner filed a cross-claim arguing that the insurer was responsible because the insurer's agent had preapproved All Ways' estimate for the repairs. *Id.* at 132. The trial court awarded judgments in favor of All Ways and the owner, and approved an award of attorney's fees to both parties. *S. Am. Fire Ins. Co. v. All Ways Reliable Bldg. Maint., Inc.,* 251 So.2d 11, 13 (Fla. 4th DCA 1971), *quashed sub nom. All Ways Reliable Bldg. Maint. v. Moore,* 261 So.2d 131 (Fla.1972). In approving the trial court's award on review this Court determined that, although no express contract existed, a contract between All Ways and the insurance company arose by implication of the circumstances. *All Ways,* 261 So.2d at

132. This implied contract "logically included an assignment" of the owner's claim against the insurer. *Id.* Importantly, this Court found that

> *[u]nder such circumstances, it is highly technical and unrealistic to take the view that [the statute] does not authorize an attorney's fee for All Ways Reliable.* All Ways Reliable was found by implication of the related circumstances to be the assignee of the insured Elsie Moore's loss claim against the insurance company; and, having successfully sued the insurance company which denied the claim for the amount representing the fire loss, was entitled concomitantly to the attorney's fee.

Id. (emphasis supplied). Despite being neither a named insured nor a named beneficiary under the policy, we held that All Ways was entitled to an award of its attorney's fees based on an implied assignment from the owner. *Id.* Because it had given such broad interpretations to the attorney's fees provision, this Court stated that "it would appear to follow that an assignee of an insurance claim stands to all intents and purposes in the shoes of the insured and logically should be entitled to an attorney's fee when he sues and recovers on the claim." *Id.; accord Roberts,* 350 So.2d at 79.

I acknowledge that while we have held that an assignee of an insured is clearly entitled to an award under section 627.428, this Court has yet to decide a case involving a subrogee of an insured. However, because assignees and subrogees are treated similarly in terms of the rights acquired from the insured, there is simply no reason for the disparate treatment of the attorney's fee provision in these virtually identical circumstances. In fact, the Court has previously approved an award of attorney's fees to an assignee of an insurance claim based on principles of subrogation. *See Fid. & Deposit Co. of Md. v. First State Ins. Co.,* 677 So.2d 266, 269 (Fla.1996). As discussed in the majority opinion, Fidelity paid a claim on behalf of its insured and in return received an assignment from the insured to sue First State, another insurer that was ultimately responsible for the loss. *Id.* at 267. On appeal, this Court remanded to the trial court for further proceedings, but held that Fidelity, as the insured's "*subrogee,* will be entitled to attorney's fees if it ultimately prevails in this litigation." *Id.* at 269 (emphasis supplied). Although *First State* involved an assignment, this Court used the terms assignee and subrogee interchangeably. *See id.* ***383** By conditionally approving an award of fees to Fidelity as a subrogee, the Court essentially treated assignees and subrogees similarly under section 627.428.

In *Auto Owners,* the United Statutes District Court for the Middle District of Florida addressed a surety's status when pursuing a claim against its principal's liability insurer. A commercial liability insurer brought a declaratory judgment action against a surety to determine whether damage to certain construction projects was covered under the policies. 227 F.Supp.2d at 1254. The court concluded that the surety, as an assignee and a subrogee, had standing as a first party claimant under the policy to pursue counterclaims against the insurance company. *Id.* at 1259–60. Specifically, the surety had performed on behalf of its principal, an insured under the CGL policy, and thus "[stood] in [the surety's] shoes[,] ... [was] equitably subrogated to the rights of [the surety], and [was] considered a first party claimant on the CGL policies." *Id.* at 1260. Although the attorney's fees provision was not at issue in *Auto Owners,* it seems relatively clear that the court concluded that an insured's assignee obtains the same rights and is entitled to the same status as an insured's subrogee. *Id.* at 1259. Both entities can "stand in the shoes" of the insured to protect their interests, both entities have standing to sue the insured's liability insurer, and more importantly, both parties are entitled to receive *all* the rights an insured has against its insurance company. *Id.* at 1259–60.

Additionally, the decision in *Western World* supports the conclusion that a subrogee, like an assignee, is equally entitled to all of the rights of the subrogor. In *Western World,* a surety paid a judgment on behalf of its principal under the terms of a security bond. 358 So.2d at 603. Thereafter, the surety and its principal sought recovery from the principal's liability insurer for failing to defend in the underlying litigation. *Id.* The First District concluded the surety was entitled to indemnification from the principal and thus had "the right to be subrogated to *any* rights which [the principals] have against their insurance carrier." *Id.* at 604 (emphasis added). Although the court's refusal to grant attorney's fees to the surety is the basis for the certified conflict in this case, the First District correctly concluded that the surety is subrogated to *any* rights of the principal against its insurer. *Id.*

As previously mentioned, there is no apparent distinction between the types of rights afforded to the assignee of an insured versus the types of rights afforded to a subrogee. *Compare All Ways,* 261 So.2d at 132 (holding that a surety who was an assignee stood in the shoes of the insured to all intents and purposes and was therefore entitled to an award of attorney's fees) *and First State,* 677 So.2d at 269 (holding that an assignee of an insurance claim was entitled to an award

of fees under the statute as the insured's subrogee) *with Dade County,* 731 So.2d at 647 (stating that a subrogee stood in the shoes of the person whose debt had been discharged and thereby acquired all rights as against the wrongdoer). Given that both assignees and subrogees are equally entitled to stand in the shoes of the insured, it would be "highly technical and unrealistic" not to award fees to a subrogee who successfully sues an insurance company that is ultimately responsible for the claim. *All Ways,* 261 So.2d at 132.

In the present case, Hartford, as surety, and Ryan, as principal, executed and delivered performance bonds to 951 Land Holdings, the owner of the property. After 951 Land Holdings brought suit against Ryan and Hartford for supplying contaminated grass to the project, Hartford, in its role ***384** as surety, paid $4.7 million to settle the underlying litigation. *Continental,* 910 So.2d at 301. Thereafter, Hartford and Ryan filed a declaratory judgment action against Ryan's liability insurers seeking reimbursement because the damages satisfied by Hartford on behalf of Ryan were covered by the CGL policies. Once Hartford paid the settlement, as was required by the bond, it became subrogated to the rights of Ryan. *See Dade County,* 731 So.2d at 646; *Transamerica,* 540 So.2d at 115–16; *see also Auto Owners,* 227 F.Supp.2d at 1259; *Western World,* 358 So.2d at 604; *Argonaut,* 380 So.2d at 1068. Because the extent of payment is alleged to be an obligation covered by the CGL policies, Hartford is subrogated to all the rights Ryan may have against petitioners. *See id.* As previously discussed, these rights include an entitlement to attorney's fees under section 627.428.

In reaching its decision, the Second District concluded that a denial of fees to Hartford would "exalt form over substance" because Ryan is ultimately liable to Hartford for its fees based on the indemnity agreement. *Contintental,* 910 So.2d at 301. The court reasoned that the statute's purpose is to reimburse an insured when it is forced to sue its insurer on the policy and that a denial of fees to Hartford, where Ryan will ultimately be liable for those fees anyway, would be contrary to that purpose. *Id.* Petitioners argue that Hartford and Ryan are experienced entities that decided to pursue the claim in this fashion and thus the court erred in forcing petitioners to pay for Hartford's fees simply because Ryan had a contractual obligation to do the same. However, the Second District correctly concluded that if Ryan had decided to carry the ball in the litigation, Ryan unquestionably would be entitled to its fees upon receipt of a favorable judgment against the insurers. Moreover, the mere fact that Hartford and Ryan are both involved in this litigation, each with their own attorney, should not deter this Court from approving an award of fees to Hartford. Indeed, this Court in *All Ways* approved a similar award, allowing both the insured and the insured's implied assignee to recover under the statute because it would have been "highly technical and unrealistic" to reach any other result. 261 So.2d at 132. Therefore, this Court should conclude that Hartford stands in the shoes of Ryan as a first-party claimant under the CGL policies and, if successful in the action against petitioners, should be entitled to an award of attorney's fees under section 627.428.

All Citations

974 So.2d 368, 33 Fla. L. Weekly S59

Footnotes

1 These two consolidated cases arise out of the Second District Court of Appeal's decision in *Ryan Inc. Eastern v. Continental Casualty Co.,* 910 So.2d 298 (Fla. 2d DCA 2005). However, because both Continental Casualty Company and Lumbermens Mutual Casualty Company separately sought review, this Court assigned individual case numbers to those appeals. Additionally, although Ryan Incorporated Eastern is listed in the case caption, it is not a party before this Court because Hartford Fire Insurance Company is the only entity that filed an answer in this appeal.

2 At oral argument, Hartford stated that Ryan paid a portion of this settlement. However, the actual amount contributed is unknown because it is part of a confidential settlement agreement not contained in the record.

3 On the substantive issue of liability coverage, the Second District noted that *J.S.U.B.* would govern the analysis of the policies' coverage provisions, but the court could not determine from its de novo review whether the damage occurred prior to the completion of the project. *See Continental,* 910 So.2d at 299–300.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Accordingly, the court remanded to the trial court to determine when the damage occurred and then decide the case based upon *J.S.U.B. Id.* at 300. The Second District's decision in *J.S.U.B.* was approved by this Court on the underlying coverage issue. *See U.S. Fire Ins. Co. v. J.S.U.B., Inc.,* No. SC05–1295, ––– So.2d ––––, 2007 WL 4440232 (Fla. Dec. 20, 2007).

4 The provisions of section 627.428 were originally codified at section 627.0127. However, they were moved in 1971.

5 We reject the argument that Hartford is precluded from recovering attorney's fees because it can be classified as an insurer. This Court has previously awarded attorney's fees under section 627.428 to entities engaged in the business of insurance. For example, in *Fidelity & Deposit Co. v. First State Insurance Co.,* 677 So.2d 266 (Fla.1996), a fire insurer disputed coverage for a fire-damaged property arguing that it had previously cancelled the policy. *Id.* at 267. The insured settled with its “errors and omissions” insurer and assigned its right to sue the fire insurer for coverage. *Id.* We held that the “errors and omissions” insurer, which had obtained an assignment from the insured, would be entitled to an award of attorney's fees if it was successful in the suit against the fire insurer. *Id.* at 269.

6 At the time of our decision in *Roberts,* the provision authorized an award of fees to “an insured or the named beneficiary under a policy.” § 627.428(1), Fla. Stat. (1975).

7 The insurers argue that the “anti-assignment” clause in the GIA precludes an assignment, even subsequent to the loss. However, “it is a well-settled rule that [anti-assignment provisions do] not apply to an assignment after loss.” *West Fla. Grocery Co. v. Teutonia Fire Ins. Co.,* 74 Fla. 220, 77 So. 209, 210–11 (1917); *accord Better Constr., Inc. v. Nat'l Union Fire Ins. Co.,* 651 So.2d 141, 142 (Fla. 3d DCA 1995).

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-12

2019 WL 3082845
Only the Westlaw citation is currently available.
United States District Court, N.D. California,
San Francisco Division.

CREDITORS ADJUSTMENT BUREAU, INC., Plaintiff,
v.
IBT MEDIA INC., Defendant.

Case No. 19-cv-02305-LB
|
Signed 07/15/2019

Attorneys and Law Firms

Daniel S. Frankston, Law Offices of Daniel Frankston, San Francisco, CA, Kenneth Jay Freed, Law Offices of Kenneth J. Freed, Sherman Oaks, CA, Lorna Ann Walker, Sweet and Walker PC, Daly City, CA, for Plaintiff.

Paul Timothy Llewellyn, Lewis & Llewellyn LLP, San Francisco, CA, for Defendant.

ORDER DENYING DEFENDANT'S MOTION TO DISMISS

Re: ECF No. 8

LAUREL BEELER, United States Magistrate Judge

INTRODUCTION

***1** This case involves a collection agency trying to collect on an alleged debt under a contract involving two other entities, one of whom is not a party in this lawsuit. In 2017, non-party Instart Logic, Inc. and defendant IBT Media Inc. entered into a contract. Plaintiff Creditors Adjustment Bureau, Inc. ("CAB"), a collection agency, alleges that IBT owes Instart $658,974.33 under the contract and that Instart assigned its claim to that debt to CAB. CAB brought this action in state court against IBT to collect. IBT removed this action to federal court on the basis of diversity jurisdiction and moved to dismiss, arguing that its contract with Instart prohibits Instart from assigning its rights (to CAB or to anyone else) without IBT's consent, and thus CAB does not have standing to collect. The court can decide the IBT's motion without oral argument. N.D. Cal. Civ. L.R. 7-1(b). The court denies IBT's motion to dismiss. CAB, as an alleged assignee of Instart, has standing to bring this action.

STATEMENT [1]

In January 2017, Instart and IBT entered into a written Master Services Agreement. [2] The Agreement is governed by California law. [3] The parties agreed to two "service orders" under the Agreement, wherein Instart would provide IBT with certain services and IBT would make certain payments. [4] The Agreement stated that:

> Neither party may transfer and assign its rights and obligations under this Agreement without the prior written consent of the other party. Notwithstanding the foregoing, Instart may transfer and assign its rights under this Agreement without consent from the other party in connection with a change in control, acquisition or sale of all or substantially all of its assets. [5]

IBT owes Instart $658,974.33 under the Agreement. [6] IBT has not paid the money it owes to Instart despite demands for payment. [7]

Instart assigned to CAB its claim against IBT for the money owed under the Agreement. [8]

ANALYSIS

1. Governing Law

"Federal Rule of Civil Procedure 17 governs whether or not a party can bring suit." *Gottlieb v. Alphabet Inc.*, No. 5:17-cv-06860-EJD, 2018 WL 2010976, at *2 (N.D. Cal. Apr. 30, 2018) (citing *U-Haul Int'l, Inc. v. Jartran, Inc.*, 793 F.2d 1034, 1038 (9th Cir. 1986)). "The rule requires that an action 'be prosecuted in the name of the real party in interest.' " *Id.* (quoting Fed. R. Civ. P. 17(a)). "Who or what qualifies as a real party in interest is not defined; 'instead, it allows a

federal court to entertain a suit at the instance of any party to whom the relevant substantive law grants a cause of action.' " *Id.* (internal brackets omitted) (quoting *U-Haul*, 793 F.2d at 1038).

***2** Instart's and IBT's Agreement is governed by California law. "Provisions prohibiting assignment of a contract, or any rights or interests in a contract, are generally valid and enforceable in California." *Id.* (citing *Fluor Corp. v. Super. Ct.*, 61 Cal. 4th 1175, 1189–90 (2015)). "But such restrictions are strictly construed, and California courts have developed a 'distinction between an assignment of a contract and an assignment of the proceeds of the contract.' " *Id.* at *4 (citing *Benton v. Hofmann Plastering Co.*, 207 Cal. App. 2d 61, 67–68 (1962)). " 'A provision in a contract or a rule of law against assignment does not preclude the assignment of money due or to become due under the contract or of money damages for the breach of the contract.' " *Id.* (internal brackets omitted) (quoting *Trubowitch v. Riverbank Canning Co.*, 30 Cal. 2d 335, 339 (1947)). Among other things, a contractual provision that prohibits the assigning of the "rights" under a contract "does not forbid the assignment of a cause of action for breach of contract, or the assignment of money damages for a breach of contract, in the absence of circumstances specifying a different intention by the parties." *Id.* (citing Restatement (Second) of Contracts § 322 ("A contract term prohibiting assignment of rights under the contract, unless a different intention is manifested ... does not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation.") (ellipsis in original)); *accord, e.g.*, *SK Networks Co. Ltd. v. Bentley Forbes Holdings, LLC*, No. CV 12-08997 MMM (SHx), 2013 WL 12131715, at *18–19 (C.D. Cal. Nov. 7, 2013) (holding that under California law, contractual provision that " '[n]one of the Parties to [the] Agreement may sell, assign or otherwise transfer any of its rights or obligations hereunder, without the prior written consent of the other Parties hereto' .... does not preclude assignment of a cause of action for money damages") (citing *Trubowitch*, 30 Cal. 2d at 339; *Rosencrans v. William S. Lozier, Inc.*, 142 F.2d 118, 124 (9th Cir. 1944); *Shiveley v. Semi-Tropic Land & Water Co.*, 99 Cal. 259, 261 (1893)).

2. Application

IBT argues that its Agreement with Instart provides that "[n]either party may transfer and assign its rights and obligations under this Agreement without the prior written consent of the other party."[9] (IBT notes that this provision not only prohibits assignment of the contract but also of all "rights" under the contract.) But as courts have held, a contractual provision prohibiting the assignment of "rights" under the contract does not on its own prohibit the right to assign a claim for damages for a breach of contract. *See, e.g.*, *Gottlieb*, 2018 WL 2010976, at *4; *SK Networks*, 2013 WL 12131715, at *18–19. IBT does not cite any cases that hold to the contrary.[10]

IBT also argues that CAB has not provided sufficient evidence that Instart assigned to CAB its claims for the money owed under the Agreement. IBT cites no cases that hold that CAB needs to provide that evidence at this juncture. *Cf.* *Kniss v. Booth*, No. SA CV 07-1215 AHS (PJWx), 2010 WL 11506619, at *4 (C.D. Cal. Jan. 4, 2010) (holding that there is no requirement under Federal Rule of Civil Procedure 8 for a plaintiff to provide at the pleading stage all documents proving the assignment of a claim) (citing cases). While CAB ultimately will have to prove that there was a valid assignment to prevail on its claims in the end, a supposed failure to do so at the pleading stage is not a basis for dismissal.

CONCLUSION

The court denies IBT's motion to dismiss.

IT IS SO ORDERED.

All Citations

Slip Copy, 2019 WL 3082845

Footnotes

1 Unless otherwise stated, the facts in the Statement are allegations from the complaint and are presumed to be true for the purposes of this order.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

2 Compl. – ECF No. 1-1 at 8 (¶ 19); Compl. Ex. 1 (Agreement) – ECF No. 7.

3 Compl. Ex 1 (Agreement) – ECF No. 7 at 6 (¶ 8.6).

4 *Id.* at 9–16.

5 *Id.* at 6 (¶ 8.2).

6 Compl. – ECF No. 1-1 at 5 (¶ 2), 6–7 (¶ 10).

7 *Id.* at 7 (¶ 10).

8 *Id.* at 5–6 (¶ 4).

9 Def. Mot. – ECF No. 8 at 4–5; Def. Reply – ECF No. 19 at 2.

10 IBT's reliance on *Henkel Corp. v. Hartford Accident and Indemnity Co.*, 29 Cal. 4th 934 (2003) (cited by Def. Reply – ECF No. 19 at 4), *overruled by Fluor*, 61 Cal. 4th 1175, is misplaced. The contractual rights at issue in *Henkel* were the right to defense and indemnity under an insurance contract. *Id.* at 944. The *Henkel* court expressly distinguished those rights from "the assignment of money due or to become due under the contract or of money damages for the breach of contract." *Id.* (internal citations omitted) (quoting *Trubowitch*, 30 Cal. 2d. at 339–40).

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-13

KeyCite Yellow Flag - Negative Treatment
Declined to Follow by Go Computer, Inc. v. Microsoft Corp., D.Md., June 29, 2006

356 F.2d 718
United States Court of Appeals Eighth Circuit.

DUBUQUE STONE PRODUCTS CO., an Iowa Corporation, Appellant,
v.
FRED L. GRAY COMPANY, a Minnesota Corporation, Appellee.
FRED L. GRAY COMPANY, a Minnesota Corporation, Appellant,
v.
DUBUQUE STONE PRODUCTS CO., an Iowa Corporation, Appellee.

Nos. 17804, 17805.
|
Feb. 18, 1966.

Synopsis
Action by insurance agent against defendants as parties to joint venture agreement for unpaid workmen's compensation, public liability and automobile insurance premiums issued to one defendant. From a judgment of the United States District Court for the Northern District of Iowa, Edward J. McManus, Chief Judge, one defendant appealed and from that portion of the judgment which failed to include amount allegedly owing for retrospective workmen's compensation policy premiums, the plaintiff cross-appealed. The Court of Appeals, Matthes, Circuit Judge, held that in view of the evidence defendant's joint venture liability was not subject to the claimed restriction and that plaintiff was entitled to the retrospective premium claimed and computed upon final cancellation of the policy.

Judgment vacated and cause remanded with directions.

Attorneys and Law Firms

***719** F. H. Becker, Dubuque, Iowa, made argument for Fred L. Gray Co. and filed brief with Donald F. Pratt, of Townsend, Pratt, Trench, Ericson & MacGregor, Minneapolis, Minn.

Rolland E. Grefe, Des Moines, Iowa, made argument for Dubuque Stone Products Co. and filed brief with Ross H. Sidney, of Austin, Grefe & Sidney, Des Moines, Iowa.

Before VOGEL, Chief Judge, and MATTHES and RIDGE, Circuit Judges.

Opinion

MATTHES, Circuit Judge.

These are an appeal and cross-appeal from a judgment in a suit brought by Fred L. Gray Company (Gray), a Minnesota corporation, against Schueller & Co., Inc. (Schueller) and Dubuque Stone Products Co. (Dubuque), Iowa corporations, in the United States District Court for the Northern District of Iowa, for unpaid workmen's compensation, public liability and automobile insurance premiums on Standard Accident Insurance Company policies issued to Schueller & Co., Inc. Schueller defaulted and has not appealed from the judgment against it. Dubuque appeals from the judgment of $36,057.18, while Gray appeals from that portion of the judgment which fails to ***720** include $7,232.60 claimed to be owing to it in retrospective workmen's compensation policy premiums.

Diversity of citizenship and the amount in controversy establish jurisdiction. Inasmuch as the parties seemingly agree that Iowa law is controlling as to substantive questions, we, too, recognize the law of that state in disposing of the issues before us.

Gray is a general agent of Standard Accident Insurance Company (Standard), which issues workmen's compensation, public liability, personal liability and property damage policies. Coates Insurance Agency, a sub-agent of Gray, issued, to Schueller, the policies covering the period during which the 'joint venture agreements' were in existence. Gray has paid Standard $19,667.02 of the amount owing on both initial premiums and additional premiums developed by audit and has received, since the filing of the suit, an assignment of Standard's rights against Dubuque.

The theory upon which Gray relies for recovery is that the insurance had been purchased to further joint ventures of Schueller and Dubuque and both are jointly and severally liable for the outstanding premiums. There is little disagreement about the basic facts, many of which are contained in stipulations. For many years prior to 1958, Schueller, primarily a sewer contractor, had purchased materials from Dubuque, a material supplier. Between April and July, 1958, Schueller decided it could successfully bid larger construction projects if it obtained additional capital. Thereupon, Schueller and Dubuque entered into a written agreement, designated a 'Joint Venture Agreement',

in connection with a project at Offutt Air Force Base, Omaha, Nebraska. This agreement, in summary, contained the following sections:

a. A general paragraph describing the job involved.

1. A statement that the parties associated themselves 'as joint venturers' until the contract be fully performed, all obligations incurred therein fully paid and all payments received thereunder fully disbursed.

2. A statement that Schueller was to manage the project and furnish full staff.

3. A statement that Schueller would be reimbursed for equipment furnished, at 60% Of the then current A.E.D. rates.

4. A statement that all equipment was to be rented; none to be purchased.

5. A statement that Dubuque Stone was to furnish all funds for use in the performance of the contract up to $200,000.

6. A statement that a joint account would be established in the First National Bank of Chicago to handle the money of the venture, all venture monies to be channeled through that account and signature control provided for both parties.

7. A statement that C. M. Elrod was selected as manager; provisions for his salary and bonus.

8. A provision for insurance of $100,000 on Elrod's life.

9. A provision for equal division of profits between Schueller and Dubuque.

10. A statement that the agreement was to be binding on successors and assigns.

Nine other projects were assumed, under either written or oral agreements, materially differing from the Offutt agreement only in that the subsequent agreements did not contain the $200,000 limitation on the part of Dubuque. There is disagreement among the parties as to whether two other additional projects (known as the Burkburnett contracts) were of the same 'joint venture' nature.

The first year of their association, Schueller and Dubuque realized a profit of $93,103.70, one-half of which was attributed to each of them. Subsequently, the venture became unprofitable and Dubuque, which had signed indemnity agreements in connection with various contract and performance bonds, was called upon to furnish additional financing. In its 1960 income tax return, Dubuque showed losses of approximately ***721** $345,000, due to the joint venture activities. These losses, denominated 'joint venture losses' were utilized to claim refunds from the Internal Revenue Service.

Before considering the issues raised on this appeal, it should be helpful to review some well known principles of Iowa law with regard to joint ventures. As was succinctly stated in Brewer v. Central Const. Co., (1950), 241 Iowa 799, 43 N.W.2d 131, at 136:

'A joint adventure is defined as an association of two or more persons to carry out a single business enterprise for profit; also as a common undertaking in which two or more combine their property, money, efforts, skill, or knowledge. The outstanding difference between a joint adventure and a partnership is that the former usually relates to a single transaction while the latter usually relates to a continuing business. (Citing authorities).

'As a rule, a joint adventure is characterized by a joint proprietary interest in the subject matter, a mutual right to control, a right to share in the profits and a duty to share the losses. (Citing authority).'

The Iowa court's expression seems to be in accord with the generally recognized and accepted definition and characterization of a joint venture. See, 48 C.J.S. Joint Adventures §§ 1, 2 and 5a; 30 Am. Jur., Joint Adventures, § 6, which contain detailed discussions of the law in this area.

Under Iowa law, liability of a member of a joint adventure may be derived from any one of three sources: 'First, a direct contract with the creditor suing. Second, on the theory of agency arising under the express or implied right of other members of the project to bind a particular one of the group by contracts within the scope of the 'authorized' enterprise. This always depends upon the sufficiency of the circumstances in each case. And, third, when the facts warrant it, this responsibility can be established through the principle of partnership when there is contemplated a mutual bearing of the losses.' Bond v. O'Donnell, 205 Iowa 902, 218 N.W. 898, 902, 63 A.L.R. 901 (1928). It need not explicitly be agreed that losses resulting from the venture will be shared. Rather, this can be inferred from other provisions of the contract, the nature of the business, and the relation of the parties to the business transacted. Brewer v. Central Const. Co., supra, 43 N.W.2d at 136; Bond v. O'Donnell, supra, 218 N.W. at 902.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Dubuque does not challenge the fact that all of the projects, with the exception of the Burkburnett jobs, were joint ventures on the part of Schueller and Dubuque. It does, however, contend: (1) that it is not liable for the 'unpaid insurance premiums because it agreement with Schueller was to provide financing with an express limitation of $200,000, on the amount thereof' and Gray's knowledge of this limitation precludes recovery of the premiums due; and (2) that 'the lower court's finding that Schueller and Dubuque Stone agreed to perform the Burkburnett contracts in the same manner and on the same terms as other joint ventures is not supported by the record evidence.'

Form the very nature of these contentions it is apparent that the district court was basically confronted with fact questions. In this situation, our review must be keyed to two fundamental principles of law. First, in examining the evidence, we must take the view which tends to support the findings and conclusions of the trial court, and we must accept all inferences which reasonably tend to support its conclusions. Minnesota Amusement Co. v. Larkin, 299 F.2d 142, 146 (8 Cir. 1962); United States v. Skolness, 279 F.2d 350, 352-353 (8 Cir. 1960); Barryhill v. United States, 300 F.2d 690, 693-694 (8 Cir. 1962); American Universal Ins. Co. v. Dykhouse, 326 F.2d 694, 695 (8 Cir. 1964). Second, findings of fact are presumed to be correct and may not be set aside unless they are clearly erroneous. F.R.Civ.P. 52(a); United States v. Skolness,supra; Barryhill ***722** v. United States, supra; American Universal Ins. Co. v. Dykhouse, supra.

With regard to Dubuque's first contention, it is undisputed that the $200,000 limitation appeared in only the first joint venture agreement (dealing with the Offutt project) and was intentionally left out of all subsequent joint venture agreements. There was also uncontroverted evidence that Dubuque provided financing, and claimed joint venture losses on its income tax returns, in excess of $200,000. This, along with other evidence, was ample to warrant the inferential finding by the court that Dubuque's joint venture liability was not limited to $200,000. [1]

A subsidiary part of this issue, concerning the extent of Dubuque's liability, is its claim that 'the knowledge of Russell Scherrer, proprietor of the Coates Agency, and sub-agent for Fred L. Gray Company, of the express limitation of $200,000 on Dubuque Stone's financing agreement, is binding upon Gray and precludes any recovery for the premiums on Schueller's insurance contracts'.

Dubuque relies upon the general rule that 'the knowledge of an agent gained in the performance of his authorized work or duty and within its scope and reasonable connection is the knowledge of the one for whom he is acting.' Huff v. United Van Lines, Inc., 238 Iowa 529, 28 N.W.2d 793, 799 (1947). The testimony supporting Dubuque's assertion that the claimed limitation had been disclosed, is that of Dubuque's president, Mr. Spahn:

'* * * Mr. Scherrer was present during some of these conversations in which we were deciding the fact that we would set up this $200,000.00 worth of financing for Schueller & Co., I would say that this occurred on several occasions. * * * At those times we mentioned the fact that we were going to put up $200,000.00 in financing for the Schueller and Company and that that money would be made available to him for the purpose of carrying on additional jobs and we felt that by putting up that money he could get an additional bond. Then in a later conversation we were told that we would have to put up the entire sum of $200,000.00 and have it on deposit at all times or we could elect to become an indemnitor and in becoming an indemnitor then we would only have to put up the money that was required from time to time with a maximum of $200,000.00.'

While this testimony does lead to the conclusion that Mr. Scherrer was informed of the $200,000 'financing' made available by Dubuque, it does not necessarily follow that Mr. Scherrer 'knew' that $200,000 was to be the absolute limit of Dubuque's liability on the joint ventures. Such an interpretation of the knowledge had by Mr. Scherrer (who had died prior to this litigation) is particularly unpalatable in view of the fact that the record, as a whole, does not substantiate Dubuque's contention that its liability was limited to $200,000. Since Dubuque's liability was not so limited, there is no reason for reading into Mr. Spahn's testimony the implication that Mr. Scherrer sold the policies in question knowing that Dubuque's total joint venture liability was subject to a $200,000 restriction.

The court found, contrary to Dubuque's second contention, that the Burkburnett contracts also were joint ventures. There was evidence to warrant the inference that this was the understanding of the parties, that funds derived from these jobs were commingled with funds from other joint ventures, and that reports regarding these projects were given to Dubuque. Although Dubuque's president strenuously urged that the Burkburnett projects were not joint ***723** ventures, the evidence, as a whole, convincingly supports the trial court's finding to the contrary.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Having in mind the scope of our review in this court-tried case, as enunciated, supra, we conclude that there is no basis in fact or law for disturbing the court's finding with regard to either of the two major questions at issue here.

Additionally, it is suggested by Dubuque that 'Fred L. Gray Company was not the real party in interest so as to enable it to bring suit * * * to recover allegedly unpaid insurance premiums of Schueller which by the terms of the policies were due Standard Accident Insurance Company. The insurer-principal was the proper party to enforce such liability, if any.' In essence, Dubuque's theory is that Gray is not the real party in interest, since Gray was not a party to the insurance contract between Schueller and Standard. Dubuque contends that, at best, Gray might properly have been classified as a representative of Standard for purposes of this suit. However, Dubuque insists that, since Gray at no time alleged that it was suing in a representative capacity, '(it) is now too late to do so.' Dubuque further avers that Standard's assignment to Gray, subsequent to filing but prior to trial, did not improve Gray's status.

Gray's counter arguments are (1) that it is the real party in interest, and (2) that Dubuque has waived the objection by failing to raise the issue by motion or answer.

In considering the effect of the assignment we first look to F.R.Civ.P. 17(a), which declares that: 'Every action shall be prosecuted in the name of the real party in interest * * *'. See also, 6 AmJur.2d Assignments, § 131, p. 313, wherein it is said: 'Rule 17(a) of the Federal Rules of Civil Procedure, which provides that every action shall be prosecuted in the name of the real party in interest, with certain exceptions relating to personal representatives, has been applied in the federal courts with respect to suits in his own name by an assignee who is found to be the real party in interest.'

In diversity cases, state substantive law is consulted to determine whether an assignee qualifies as a real party in interest under Rule 17(a). See Hoeppner Const. Co. v. United States, 287 F.2d 108, 111 (10 Cir. 1961); Wright v. Schebler Co., 37 F.R.D. 319, 321 (D.C.S.D.Ia.1965); 6 AmJur.2d, Assignments, § 131. The relevant Iowa law is found in 32 Ia.Code Anno. § 539.3 which provides that an open account of sums of money due on contract may be assigned, and the assignee will have a right of action thereon in his own name, subject to such defenses and counterclaims as the debtor would have had against the assignor before notice of the assignment is given the assignee. [2]

One of the basic purposes of F.R.Civ.P. 17(a) is to protect the defendant from further unnecessary litigation.

'If the judgment, if any, by the plaintiff will protect the defendant from future annoyance or loss, and where, as against the parties suing, the defendant can urge any defenses he could make against the real owner of the claim, then there is an end of the defendant's concern as to the protection he is afforded by having the claim prosecuted by the real party in interest. Blair v. Espeland, 231 Minn. 444, 43 N.W.2d 274.' United States v. Tyler, 220 F.Supp. 386, 395 (D.C.N.D.Ia.1963).

Turning to the assignment in this case. Standard unequivocally and unconditionally sold, assigned and transferred to Gray 'any and all claims, demands or causes of action, if any, which it has, may have or may in the future have against Schueller and Co., Inc. and Dubuque ***724** Stone Products Co. on account of premiums, including retroactive premiums, due or claimed to be due on account of said policies of insurance written by the undersigned through Fred L. Gray Company as its general agent and/or through Coates Insurance Agency as sub-agent for Fred L. Gray Company'. In light of this assignment, there can be no basis for arguing that Gray did not acquire, and does not now own, any cause of action which accrued to Standard by reason of the issuance of the insurance policies.

We cannot accept Dubuque's argument that the assignment was invalid because it was made after this suit had been filed. The assignment occurred after filing, but before trial, and Dubuque suffered no prejudice therefrom, since at, and from, the time of filing Gray was a real party in interest as to $19,667.02, which it had previously paid to Standard on Dubuque's account. It should also be noted that Gray's first complaint only alleged that it was entitled to that $19,667.02. Standard's subsequent assignment merely conveyed its cause of action to Gray, thereby preventing a later suit by Standard. The assignment did not cause Dubuque to lose the right to assert, against Gray, any defenses which it could have asserted against Standard and, in fact, the record discloses that Dubuque fully availed itself of this right.

Although there is some merit in Gray's claim that Dubuque waived the right to complain of Gray's capacity by failing to timely object by motion or answer as required by Rule 9(a) F.R.Civ.P., we need not make a definitive determination of

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

this question because we have found that Gray is the real party in interest, within the meaning of Rule 17(a).

This brings us to Gray's cross-appeal, which presents the question whether the court erred in failing to include in the judgment an additional $7,232.60 in retrospective premiums claimed to be due on a workmen's compensation policy which was effective from March 15, 1960, to August 27, 1960, the date of cancellation.

Exhibits explaining and determining the retrospective premiums were admitted into evidence and two witnesses testified, in detail, as to the meaning of a 'retrospective' premium[3] and the computation thereof under this policy. A retroactive, or retrospective, premium is merely one which is computed, after the termination of the policy, in the basis of the insured's experience during the policy term; in effect, it constitutes a retrospective premium adjustment.

Although the instant policy was a 'three-year retrospective' one and final adjustment would ordinarily await the expiration of the three years, the final cancellation of this policy, within a few months after its issuance, necessitated an immediate final audit, which disclosed that the additional $7,232.60 was owing.

Unfortunately, the trial court did not, in its findings of fact and conclusions of law, indicate why it refused to allow the amount due on the retrospective premium; in fact, the court completely ignored this item in its findings and conclusions. Not only can we find no evidence justifying the court's failure to award judgment for the amount of the retrospective premium, but, to the contrary, the only evidence on this issue stands unrebutted and proves conclusively that the additional 'retrospective' premium is due and owing from the joint venturers, in the amount stated.

Accordingly, the judgment is vacated and the cause is remanded, with directions to the trial court to enter another judgment in favor of Gray in the amount of $43,289.78, plus appropriate interest.

All Citations

356 F.2d 718

Footnotes

1 Although the court did not explicitly make such fact finding, it must have inferentially reached that conclusion, since Dubuque had paid out more than $200,000 prior to the bringing of this suit, in which the court allowed a further recovery against Dubuque for $36,057.18.

2 Rule 7 of the Iowa Rules of Civil Procedure is to the same effect, providing: 'The assignment of a thing in action * * * shall be without prejudice to any defense, counterclaim or cause of action matured or not, if matured when pleaded, existing against the assignor of the party pleading it.'

3 Mr. Reimann, president of Fred L. Gray Company, testified: 'Retrospective rating is used * * * generally on larger size risks, and it is used to make the final premium developed on the policy directly in proportion to the loss experience developed by the company carrying the insurance on that particular policy. If the loss experience is very favorable on the company, the insured can receive a substantial refund or credit. If the loss experience is very poor the insured is liable for additional premium to make up a portion of that loss subject to certain minimums and maximums.'

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-14

414 Fed.Appx. 930
This case was not selected for publication in West's Federal Reporter.
See Fed. Rule of Appellate Procedure 32.1 generally governing citation of judicial decisions issued on or after Jan. 1, 2007.
See also U.S.Ct. of App. 9th Cir. Rule 36-3.
United States Court of Appeals,
Ninth Circuit.

Richard EDWARDS, d.b.a. Eurotrading, Plaintiff–Appellant,
v.
SYMBOLIC INTERNATIONAL, INC., Defendant–Appellee.

No. 09–55890.
|
Submitted Dec. 7, 2010. [*]
|
Filed Feb. 7, 2011.

Synopsis

Background: Buyer filed breach of contract action against seller. The United States District Court for the Southern District of California, Jan M. Adler, United States Magistrate Judge, 2009 WL 1178662, entered summary judgment in seller's favor, and buyer appealed.

Holdings: The Court of Appeals held that:

buyer's failure to pay balance due on payment date specified in contract was material breach of contract, and

liquidated damages provision in contract was reasonable.

Affirmed.

Procedural Posture(s): On Appeal; Motion for Summary Judgment.

Attorneys and Law Firms

***931** James William Harris, James W. Harris Attorney at Law, Corona Del Mar, CA, for Plaintiff–Appellant.

Jeffrey A. Swedo, Esquire, Gordon & Rees LLP, Irvine, CA, for Defendant–Appellee.

Appeal from the United States District Court for the Southern District of California, Jan M. Adler, Magistrate Judge, Presiding. D.C. No. 3:07–cv–01826–JMA.

Before: NOONAN, BERZON, and CALLAHAN, Circuit Judges.

MEMORANDUM [**]

****1** Plaintiff-appellant Richard Edwards, a foreign citizen, who does business as "Eurotrading" ("Edwards") appeals from the district court's grant of summary judgment to defendant-appellee Symbolic International, Inc. ("Symbolic"). [1] The district court concluded, as a matter of law, that by failing to timely pay the balance due on the contract, Edwards was in material breach and that the liquidated damages clause was valid, enforceable and reasonable, therefore summary judgment for Symbolic was appropriate. We affirm.

A district court's grant of summary judgment is reviewed de novo. *See, e.g., F.T.C. v. Network Servs. Depot, Inc.,* 617 F.3d 1127, 1138 (9th Cir.2010). The court must determine, viewing the evidence in the light most favorable to the nonmoving party, whether there are any genuine issues of material fact and whether the district court correctly applied the relevant substantive law. *Balint v. Carson City,* 180 F.3d 1047, 1050 (9th Cir.1999) (en banc).

Under the applicable California contract law, a party may rescind a contract "[i]f the consideration for the obligation of the rescinding party, before it is rendered to him, fails in a material respect from any cause." Cal. Civ.Code § 1689(b)(4). "Delay in performance is a material failure only if time is of the essence, i.e., if prompt performance is, by the express language of the contract or by its very nature, a vital matter." *Johnson v. Alexander,* 63 Cal.App.3d 806, 134 Cal.Rptr. 101 (1976) (citing, inter alia, *Henck v. Lake Hemet Water Co.,* 9 Cal.2d 136, 143, 69 P.2d 849 (1937)). Edwards concedes that he failed to pay the $2.8 million balance on August 13, 2007, the payment date specified in the contract, but he argues that because time was not of the essence, the district court erred in finding there was a material breach of contract. We conclude, however, that pursuant to the parties' pre-contract communications and negotiations, as well as the contract

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

***932** terms, time was of the essence. *Henck,* 9 Cal.2d at 143, 69 P.2d 849 ("The general rule of equity is that time is not of the essence of the contract, unless it clearly appear from the terms of the contract, in the light of all the circumstances, that such was the intention of the parties.").

Specifically, (1) in the pre-contract negotiations, Symbolic repeatedly rejected the thirty working-day time period that Edwards sought to pay the balance and insisted on the shorter thirty calendar-day time period to ensure the balance was paid on or before August 13; (2) Edwards agreed to the August 13 date and it is the date specified in the contract; (3) prior to Edwards' failure to pay, a Symbolic representative repeatedly advised Edwards that time was of the essence; and (4) prior to August 13, Symbolic sent Edwards the "Notice to Complete," which advised him that in order for the transaction to be deemed completed, the balance was due by August 13 or Symbolic would keep the $300,000 deposit "by way of liquidated damages for breach of contract." Edwards' breach by non-payment on the date the balance for the Ferrari was due was therefore material.

****2** Although Edwards contends that the parties' negotiations and intentions as to whether time was of the essence raise disputed issues of material fact, he fails to explain how these allegedly disputed issues "might affect the outcome of the suit under the governing law." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986). First, "the mere state of mind of the parties—with reference to the 'meeting of the minds'—is not the essential object of inquiry, the terms of the promise act being determinable by an external and not by an internal standard." *Zurich General Acc. & Liab. Assur. Co., Ltd. v. Industrial Acc. Com.,* 132 Cal.App. 101, 104, 22 P.2d 572 (1933) (citations omitted). Regardless of Edwards' intentions as to when he might pay, after negotiating with Symbolic over the due date he accepted Symbolic's proposed date of August 13 and had his solicitor prepare the contract with that date. Moreover, there is no legal basis for Edwards' argument that Symbolic breached the contract by sending its "Notice to Complete" letter before the due date for the balance because the contract does not indicate when the notice to complete must be given. In sum, Edwards has not raised any material issue of fact as to whether he breached the contract. *Matsushita Electrical Industrial Co., Ltd. v. Zenith Radio Corp.,* 475 U.S. 574, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986) (nonmoving party "must do more than simply show that there is some metaphysical doubt as to the material facts").

Edwards further asserts that even if he breached the contract, the contract's liquidated damages provision was unreasonable. Liquidated damages provisions are favored in California and are enforceable unless it was "unreasonable under the circumstances existing at the time the contract was made." California Civil Code § 1671(b); *see also Weber, Lipshie & Co. v. Christian,* 52 Cal.App.4th 645, 654, 60 Cal.Rptr.2d 677 (1997). Here, the parties were sophisticated buyers and sellers of high-end vintage cars who agreed to a liquidated damages clause equivalent to 10% of the price of the Ferrari. There was evidence that this was the standard practice in the industry. Viewed under the circumstances at the time of contracting, *see id.*, the liquidated damages provision was reasonable and therefore, as a matter of law, applied to Edwards when he breached the contract. We also reject Edwards' claim that the resolution of the liquidated damages issues should have been submitted to the jury rather than be decided by the district court because under ***933** California law, it is clear that "[t]he question whether a contractual provision is an unenforceable liquidated damages provision is one for the court." *Morris v. Redwood Empire Bancorp,* 128 Cal.App.4th 1305, 1314, 27 Cal.Rptr.3d 797 (2005) (citation omitted).

Finally, Edwards' contention that the district court erred by impermissibly weighing the evidence and acting as a trier of fact is not supported by the record. The record indicates that the court was properly determining whether there were genuine issues of material fact that precluded summary judgment. *Balint,* 180 F.3d at 1054 ("This court does not weigh the evidence or determine the truth of the matter, but only determines whether there is a genuine issue for trial.").

****3** The district court's order granting summary judgment to Symbolic is **AFFIRMED.**

All Citations

414 Fed.Appx. 930, 2011 WL 379171

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Footnotes

* The panel unanimously concludes this case is suitable for decision without oral argument. *See* Fed. R.App. P. 34(a)(2).

** This disposition is not appropriate for publication and is not precedent except as provided by 9th Cir. R. 36–3.

1 Because the parties are familiar with the facts of this case, we repeat them here only as necessary to the disposition of this case.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-15

KeyCite Yellow Flag - Negative Treatment
Distinguished by Omicron Safety and Risk Technologies, Inc. v. UChicago Argonne, LLC, N.D.Ill., March 6, 2015

365 Ill.App.3d 608
Appellate Court of Illinois,
Second District.

In re Mary FOREMAN, Seller (Rapid Settlements, Ltd., Petitioner–Appellee and Cross–Appellant, v. Symetra Life Insurance Company and Symetra Assigned Benefits Service Company, Respondents–Appellants and Cross–Appellees).

No. 2–05–0689.
|
June 8, 2006.

Synopsis

Background: Annuity issuer and structured settlement obligor objected to transfer of payment rights for a lump-sum payment. The Circuit Court, Winnebago County, Janet R. Holmgren, J., approved transfer, but struck from the transfer agreement a provision that granted transferee the right of first refusal on any future transfers.

On cross-appeals, the Appellate Court, Byrne, J., held that antiassignment provision in settlement precluded transfer of right to receive payments.

Reversed and remanded with instructions.

Attorneys and Law Firms

****388** William A. Chittenden III, Craig M. Bargher, Chittenden, Murday & Novotny LLC, Chicago, for Symetra Assigned Benefits Service Company, Symetra Life Insurance Company.

Beatriz M. Olivera, Jasmine De La Torre, Harris, Kessler & Goldstein, LLC, Chicago, for Rapid Settlements, Ltd.

Opinion

Justice BYRNE delivered the opinion of the court:

***608 ***951** This appeal arose from the petition, filed by petitioner, Rapid Settlements, Ltd., pursuant to the Structured Settlement Protection Act (Act) (215 ILCS 153/1 *et seq.* (West 2004)), for court approval of a transfer of a portion of Mary Foreman's structured settlement payment ***609** rights. Respondents, Symetra Life Insurance Company and Symetra Assigned Benefits Service Company (Symetra, collectively), the annuity issuer and the structured settlement obligor, respectively, filed an objection to the petition for approval. The trial court approved the transfer but struck from the transfer agreement paragraph 10, which had granted Rapid Settlements a right of first refusal on any future transfers of the remaining periodic payments not otherwise transferred by Foreman. On appeal, Symetra contends that the trial court erred in approving the transfer. Rapid Settlements cross-appeals and argues that the trial court erred by striking paragraph 10 from the transfer agreement. We reverse the trial court's judgment approving the transfer. Because we reverse, we need not address the cross-appeal.

BACKGROUND

The structured settlement at issue derives from a settlement agreement and release entered into on or about February 8, 1996, between Foreman, administrator of the estate of Dashawna Foreman, and Illinois State Medical Insurance Services, Inc., as insurer for and on behalf of Warren Babcock, Jr., M.D., for the purpose of settling a wrongful death action in the circuit court of Winnebago County. The settlement agreement provides that Foreman was to receive $121,445 at the time of settlement, and the following future periodic payments: $1,000 per month, "beginning on December 1, 1996[,] through June 1, 2005, all 103 payments being guaranteed certain," and $789 per month, "beginning on July 1, 2005, guaranteed for 10 years certain, increasing at 3% annually, and payable thereafter for the life of Mary Foreman." The settlement agreement further provides that "[Foreman] acknowledges that the Periodic Payments described in Section 2 cannot be accelerated, deferred, increased or decreased by [her]; nor shall [she] have the power to sell, mortgage, encumber, or anticipate the Periodic Payments, or any part thereof, by assignment or otherwise." The settlement agreement also states that it "shall be construed and interpreted in accordance with the law of the State of Illinois."

In order to fulfill and discharge its obligation to make the periodic payments to Foreman under the settlement agreement, the insurer made a qualified assignment of its liability to make the periodic payments, to Safeco Assigned

Benefits Service Company, n/k/a Symetra Assigned Benefits Service Company. In order to fulfill its obligations to Foreman under the structured settlement, Safeco purchased an annuity from Safeco Life Insurance Company, n/k/a Symetra Life Insurance Company, naming Foreman as annuitant. Under this annuity, ***610** Symetra Life makes the periodic payments required under the structured settlement agreement directly to Foreman, although Symetra Assigned Benefits Service is still obligated to make *****952** ****389** the periodic payments should Symetra Life fail to do so.

Foreman contacted Rapid Settlements, seeking to transfer a portion of her structured settlement payment rights for a lump-sum payment. On August 9, 2004, Foreman executed an amended transfer agreement under which she agreed to transfer to Rapid Settlements, its successors and/or assigns, the assigned payments in exchange for a lump-sum payment of $10,500.

On September 10, 2004, Rapid Settlements filed in the circuit court of Winnebago County a petition for approval of the transfer of the structured settlement payment rights. Subject to the trial court's approval, Foreman agreed to transfer to Rapid Settlements, its successors and/or assigns, the following periodic payments: "Six (6) monthly payments each in the amount of $942.11 beginning on January 1, 2012[,] through and including June 1, 2012; and Thirty–Six (36) monthly payments each in the amount of $970.37, both sets of payments subject to a 3% annual increase each July 1st, beginning on July 1, 2012[,] through and including June 1, 2015, ultimately increasing to $1,029.47 per month." Foreman signed a written waiver indicating that she chose to waive seeking independent professional advice regarding the financial, legal, and tax implications of the transfer. All interested parties received a notice and a copy of the petition for approval.

On October 12, 2004, Symetra filed an objection to the petition. Symetra argued that the transfer would place unacceptable burdens upon it. Symetra also argued that the transfer failed to comply with the provisions of the Act. Of relevance to this appeal, Symetra contended that under the Act a proposed transfer of settlement rights is not authorized if it would contravene any law. See 215 ILCS 153/30(e) (West 2004). Symetra argued that the proposed transfer would contravene Illinois contract law because the antiassignment clause of the settlement agreement expressly prohibits Foreman from entering into a transfer agreement such as the one with Rapid Settlements.

On October 21, 2004, the court issued a memorandum of decision holding that the transfer agreement was enforceable and complied with the Act and other applicable law in all respects, with the exception of paragraph 10 concerning the right of first refusal. Accordingly, the court severed paragraph 10 from the transfer agreement. As to the enforceability of the antiassignment clause in the structured settlement agreement, the court first noted that it was cognizant that such clauses are looked upon with disfavor and should be narrowly ***611** interpreted. Next, relying on a rule cited in *In re Nitz,* 317 Ill.App.3d 119, 127, 250 Ill.Dec. 632, 739 N.E.2d 93 (2000), that antiassignment provisions are ineffective to prevent assignment where the payment of money is the only obligation remaining and the money is absolutely due to the debtor, the trial court believed that "[t]he [antiassignment] clause in *Nitz* was enforced because a change in the recipient of the payment should have altered the favorable tax treatment afforded the parties." The trial court distinguished *Nitz* on the basis that the tax treatment of a transfer was no longer an issue in the present case. Accordingly, the trial court did not enforce the antiassignment clause and approved the transfer.

On February 25, 2005, the trial court denied Symetra's motion for reconsideration. An order was thereafter entered on June 22, 2005, approving the transfer of the structured settlement payment rights from Foreman to Rapid Settlements but striking paragraph 10 of the transfer agreement regarding the right of first refusal. *****953** ****390** Symetra timely appealed. Rapid Settlements timely cross-appealed.

ANALYSIS

In support of its first contention, that the trial court erred in approving the transfer, Symetra asserts that the assignment of the structured settlement payment rights is prohibited by the unambiguous terms of the underlying settlement agreement, as well as by the qualified assignment and annuity contracts. We agree.

"Construing the language of a contract is a question of law, and we review a trial court's determination of a contract *de novo.*" *Nitz,* 317 Ill.App.3d at 124, 250 Ill.Dec. 632, 739 N.E.2d 93; *Henderson v. Roadway Express,* 308 Ill.App.3d 546, 548, 242 Ill.Dec. 153, 720 N.E.2d 1108 (1999). "When construing a contract, our duty is to effectuate the intent of the parties to the contract." *Henderson,* 308 Ill.App.3d at 548, 242 Ill.Dec. 153, 720 N.E.2d 1108. "Parties to a contract are free to

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

include any terms they choose, as long as those terms are not against public policy and do not contravene some positive rule of law." *Green v. Safeco Life Insurance Co.,* 312 Ill.App.3d 577, 581, 245 Ill.Dec. 140, 727 N.E.2d 393 (2000). "Such a contract is binding on both parties, and it is the duty of the court to construe it and enforce the contract as made." *Green,* 312 Ill.App.3d at 581, 245 Ill.Dec. 140, 727 N.E.2d 393.

The parties do not dispute that the structured settlement agreement in this case contains an antiassignment provision. The plain language of the settlement agreement prohibits all assignments. Paragraph 3 of the settlement agreement specifically states that Foreman does not have "the power to sell, mortgage, encumber, or anticipate the [payments], or any part thereof, *by assignment or otherwise.*" (Emphasis added.) Moreover, similar to the settlement agreement, the qualified assignment and annuity contracts prohibit assignments of the periodic payments. The qualified assignment ***612** contract provides that none of the payments "may be accelerated, deferred, increased or decreased and may not be anticipated, sold, assigned or encumbered." The annuity contract similarly provides that no payment "may be accelerated, deferred, increased, or decreased, or anticipated, sold, assigned, or encumbered in any manner by the annuitant (or either joint annuitant) or any other recipient of the payment."

However, relying on *Nitz,* the trial court did not enforce the antiassignment clause of the settlement agreement, determining that the antiassignment provision was ineffective to prevent assignment because the payment of money was the only obligation remaining and the tax treatment was immaterial. Rapid Settlements adds in support that restraints on alienation, as found in the settlement agreement and the qualified assignment and annuity contracts, were included to preserve the tax-exempt character of the transaction. Rapid Settlements asserts that because that status is not protected by federal and Illinois law, the trial court correctly ignored the antiassignment provision. We disagree for the following reasons.

First, the trial court incorrectly concluded that we enforced the antiassignment clause in *Nitz* solely because the transfer of payments could have altered the parties' favorable tax treatment. A review of *Nitz* as well as other decisions addressing antiassignment provisions shows that the language of the agreements between the parties was the main basis for enforcing the provisions.

Nitz entered into an agreement with Safeco to settle a negligence action. The settlement agreement gave Nitz a life annuity *****954** ****391** and expressly stated that Nitz had no power to sell, mortgage, or encumber his payments or any part thereof, by assignment or otherwise. Nitz commenced an action seeking court approval to assign the future payments in an annuity agreement. Finding that such an antiassignment provision was enforceable as there was no public policy against it, we held that Nitz's attempted assignment of future payments was invalid based on the clear and unambiguous language of the settlement agreement. *Nitz,* 317 Ill.App.3d at 122, 125, 250 Ill.Dec. 632, 739 N.E.2d 93.

In reaching our conclusion, we relied on the *Henderson* and *Green* cases. In *Henderson,* the court concluded that, although Illinois law disfavored antiassignment clauses in contracts, the plain language of the settlement agreement clearly indicated that the parties intended to forbid Henderson from assigning his periodic payments. *Henderson,* 308 Ill.App.3d at 549–50, 242 Ill.Dec. 153, 720 N.E.2d 1108. The court noted that Henderson did not provide any persuasive authority to justify why it should ignore the parties' clear intentions to incorporate a bargained-for provision. Additionally, while the court noted that any adverse tax consequences, as ***613** the insurers warned of in arguing for enforcement, may or may not be real and may or may not actually arise, the important factor was that "the parties implemented the antiassignment provisions with these concerns [(favorable tax treatment)] in mind." *Henderson,* 308 Ill.App.3d at 552, 242 Ill.Dec. 153, 720 N.E.2d 1108. The court further stated that "any general policy of enabling persons to transfer property freely does not outweigh the parties' contractual intentions and the public policy of providing steady income and tax-favorable treatment to claimants of structured settlements, as evidenced by the recent passage" of the Act. *Henderson,* 308 Ill.App.3d at 552, 242 Ill.Dec. 153, 720 N.E.2d 1108. In *Green,* the court noted that public policy strongly favors freedom of contract and concluded that the plain and ordinary meaning of the language of the antiassignment provision controlled. *Green,* 312 Ill.App.3d at 581, 245 Ill.Dec. 140, 727 N.E.2d 393.

Nitz asserted that we should follow the long-held rule that antiassignment provisions are ineffective to prevent assignment where the only obligation remaining is the payment of money and the money is absolutely due to the debtor, as in that case. *Nitz,* 317 Ill.App.3d at 127, 250 Ill.Dec. 632, 739 N.E.2d 93. We disagreed because more than the mere payment of money was involved in the case, as the parties believed that the assignment of future periodic payments to

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

anyone other than Nitz could alter and potentially terminate the tax-preferred status of the payments. *Nitz,* 317 Ill.App.3d at 127–28, 250 Ill.Dec. 632, 739 N.E.2d 93. Accordingly, we held that the terms of the structured settlement agreement, which were agreed to by Nitz, prohibited him from assigning his periodic payments. *Nitz,* 317 Ill.App.3d at 132, 250 Ill.Dec. 632, 739 N.E.2d 93.

Contrary to the trial court's finding here, the tax issue was not the only basis for our decision in *Nitz.* The case was not resolved solely on whether any adverse tax consequences existed. We first examined the language of the settlement agreement itself and determined that the parties intended to restrict assignments, then we found an *additional* reason for finding the assignment void. We determined also that there were potential tax ramifications if assignment were allowed. Thus, *Nitz* does not stand for the proposition that if favorable tax treatment is lacking, a trial court should ignore the parties' clear intent against assignment under the language of *****955** ****392** the settlement agreement, and we will not endorse such a holding.

Rapid Settlements argues that the Victims of Terrorism Tax Relief Act of 2001 (Pub.L. No. 107–134, 115 Stat. 2427 (to be codified at 26 U.S.C. § 5891(b)(2)(A) (2006))) invalidates the antiassignment provision because it eliminates an obligor's concerns about potential tax liability when an obligee attempts to assign a structured settlement agreement. The Victims of Terrorism Tax Relief Act only specifies what tax treatment certain kinds of structured settlements will be afforded; ***614** it leaves to the individual states the question of assignability. The clear and unambiguous language of the settlement agreement controls our analysis here.

Rapid Settlements argues that the new version of the Act (215 ILCS 153/1 *et seq.* (West 2004)) allows Illinois courts to approve transfers of structured settlement payment rights despite antiassignment provisions in structured settlement agreements. We disagree.

In *In re Shaffer,* 319 Ill.App.3d 1048, 253 Ill.Dec. 837, 746 N.E.2d 285 (2001), noting that there is no general rule or public policy invalidating antiassignment clauses, the court enforced a settlement agreement prohibiting assignment. With respect to Shaffer's argument that section 155.34 of the Illinois Insurance Code (215 ILCS 5/155.34 (West 2000) (now 215 ILCS 153/25 (West 2004))) applies to all settlement agreements whether they contain antiassignment provisions or not, the court disagreed. The court held that the plain language of section 155.34 does not indicate one way or another whether the section is affected by contractual antiassignment provisions or whether, when such a provision exists, the section is inapplicable, and the legislative history provides no insight into the validity of antiassignment provisions. *Shaffer,* 319 Ill.App.3d at 1057, 253 Ill.Dec. 837, 746 N.E.2d 285. The court believed that the legislative history demonstrated that the legislature was concerned with protecting structured settlement payment recipients from unscrupulous factoring companies, that no other concern or intent was evident from the legislative discussions, and that there was no other basis for enacting section 155.34. *Shaffer,* 319 Ill.App.3d at 1057–58, 253 Ill.Dec. 837, 746 N.E.2d 285. Similarly, we find nothing in the current Act indicating that the legislature intended to invalidate contractual provisions against assignment.

Like the former version, the current Act does not guarantee a payee any right to transfer payments merely because the trial court finds that the elements of the Act have been satisfied. See 215 ILCS 153/15 (1), (3) (West 2004). "Where a structured settlement agreement does not permit the payments to be assigned, the [trial] court's authority to act on a petition seeking approval of the assignment of payments under such an agreement is not invoked * * *." *Nitz,* 317 Ill.App.3d at 123, 250 Ill.Dec. 632, 739 N.E.2d 93; see also *Shaffer,* 319 Ill.App.3d at 1058, 253 Ill.Dec. 837, 746 N.E.2d 285 (although trial court has discretion under the Act to approve proposed transfer, it has that discretion only when a petitioner has a right to assign pursuant to settlement agreement). In this case, the structured settlement agreement does not permit the assignment of periodic payments, and therefore, the trial court had no authority under the Act to approve the petition. Accordingly, because the parties intended by agreement not to assign the periodic payments, the petition for approval must be dismissed.

***615** We also reject Rapid Settlements' application of section 322 of the Restatement (Second) of Contracts (Restatement (Second) of Contracts § 322 (1981)) to the facts of this case. Specifically, section 322, *****956** ****393** which Rapid Settlements misquotes by adding language that does not exist, provides in relevant part:

> "(1) *Unless the circumstances indicate the contrary,* a contract term prohibiting assignment of '*the contract*' bars only the delegation to an assignee of the performance by the assignor of a duty or condition.

(2) A contract term prohibiting assignment of rights under the contract, *unless a different intention is manifested,*

* * *

(c) is for the benefit of the obligor, and does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition." (Emphasis added.) Restatement (Second) of Contracts §§ 322(1), (2)(c) (1981).
Section 322(1) limits contract terms that prohibit assignment of the contract as a whole by restricting the prohibition against assignment only to performance of specific duties or conditions under the contract, and only in cases in which the circumstances do not "indicate the contrary." In this case, the antiassignment provision is very specific as it expressly prohibits the payee's right to assign the payments. Section 322(2)(c) does not restrict enforcement of antiassignment provisions in those cases where the parties' intentions to enforce the provisions are manifest.

Furthermore, the antiassignment provision of the settlement agreement benefits Foreman by assuring her of a continuing cushion of income, preventing her from "binging away" the asset and effectively becoming indigent. See *Nitz,* 317 Ill.App.3d at 123, 250 Ill.Dec. 632, 739 N.E.2d 93 ("legislature was concerned that such persons were accepting offers of ready, but deeply discounted, cash from companies in exchange for their settlement annuity payments and then ending up penniless and without resources in the future"); *J.G. Wentworth S.S.C. Ltd. Partnership v. Callahan,* 256 Wis.2d 807, 817, 649 N.W.2d 694, 699 (App.2002), citing *Wentworth v. Jones,* 28 S.W.3d 309, 313 (Ky.App.2000). The antiassignment provision also benefits Symetra by guarding against administrative risks and burdens, the potential for multiple liability, and the loss of predictability. It protects Symetra Life from the need to deal with individuals other than those named in the policy and from the risk of "determining at its peril which of several claimants may be entitled to the fund. Especially * * * in cases providing for regular periodical payments." ***616** *Hoffman v. Hoffman,* 8 N.J. 157, 161, 84 A.2d 441, 442 (1951); see also *Nitz,* 317 Ill.App.3d at 122, 250 Ill.Dec. 632, 739 N.E.2d 93 (acknowledging the "burdensome administrative problems" and "increased legal and administrative expenses" the insurer stated it would face if the court approved the transfer); *Henderson,* 308 Ill.App.3d at 552, 242 Ill.Dec. 153, 720 N.E.2d 1108 (structured settlements help guarantee predictability for insurers, which is important for transactions involving long-term liabilities); *Singer Asset Finance Co. v. CGU Life Insurance Co. of America,* 275 Ga. 328, 331, 567 S.E.2d 9, 11 (2002) (enforcing an antiassignment provision and noting that "the assignment of a structured settlement agreement exposes the obligor to potential litigation and administrative risks"). Accordingly, we find that the clear and unambiguous language of the settlement agreement prohibiting assignment, of any kind and for any duration, of the periodic payments, to which the parties agreed, should be given full effect.

In passing, we observe that by our holding we may be enforcing a transaction that *****957 **394** will place Foreman in significantly greater financial need today. However, Foreman freely made the agreement that she seeks to avoid now. Absent a violation of public policy, we will not approve the voiding of unambiguous, bargained-for contract terms.

Based upon the foregoing, because the structured settlement agreement in this case contained an enforceable antiassignment provision, the Act does not apply and the petition must be dismissed. We therefore reverse the order of the trial court and remand the cause to the trial court for the entry of an order dismissing Rapid Settlements' petition. Further, based on our decision, we need not address Symetra's argument that the proposed transfer was not an effective transfer under the provisions of the Act or address Rapid Settlements' cross-appeal that the trial court erred in striking paragraph 10 of the transfer agreement regarding Rapid Settlements' right of first refusal.

The judgment of the circuit court of Winnebago County is reversed, and the cause is remanded for the entry of an order dismissing the petition.

Reversed and remanded with instructions.

BOWMAN and HUTCHINSON, JJ., concur.

All Citations

365 Ill.App.3d 608, 850 N.E.2d 387, 302 Ill.Dec. 950

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-16

284 Or.App. 47
Court of Appeals of Oregon.

Marshall JOHNSON, Plaintiff-Respondent,
v.
J.G. WENTWORTH ORIGINATIONS, LLC, a Nevada limited liability company, Defendant-Respondent,
and
Metropolitan Life Insurance Company; and Metropolitan Tower Life Insurance Company, aka Metlife Tower Resources Group, Inc., Other-Appellants.

A156843
|
Argued and submitted May 27, 2015.
|
March 1, 2017

Synopsis
Background: Factoring company filed petition seeking to obtain court approval of beneficiary's transfer of his interest in future payments under structured settlement agreement to the company. The Circuit Court, Multnomah County, No. 140201933, Christopher J. Marshall, J., issued judgment approving the transfer. Obligor under the structured settlement agreement appealed.

The Court of Appeals, Hadlock, C.J., held that under California law, obligor was entitled to enforce agreement's anti-assignment clause to prevent beneficiary from transferring his interest in future payments under the agreement to factoring company.

Reversed and remanded.

Procedural Posture(s): On Appeal.

****866** Multnomah County Circuit Court, 140201933, Christopher J. Marshall, Judge.

Attorneys and Law Firms

Stephen R. Harris, Pennsylvania, argued the cause for appellants. With him on the briefs were Michael T. Stone, Christopher Allnatt, and Brisbee & Stockton LLC.

Julie A. Weis, Portland, argued the cause for respondent J.G. Wentworth Originations, LLC. With her on the brief was Sara Ghafouri.

No appearance for respondent Marshall Johnson.

Before Sercombe, Presiding Judge, and Hadlock, Chief Judge, and Tookey, Judge.

Opinion

HADLOCK, C. J.

***49** Marshall Johnson is the beneficiary of a right to periodic payments under a structured settlement agreement. Petitioner J. G. Wentworth Originators, LLC (J. G. Wentworth) brought this special proceeding under ORS 33.857 to ORS 33.875 (2005), [1] seeking to purchase at a discount Johnson's right to one future annuity payment and a portion of a future lump sum payment. The trial court issued a judgment approving the transfer, and Metropolitan Tower Life Insurance Company (Met Tower), the obligor under the structured settlement agreement, appeals. We conclude that the trial court erred in approving the transfer, because the structured settlement agreement included an anti-assignment clause that Met Tower has a right to enforce and that prohibited Johnson from transferring his interest in the payments. We therefore reverse.

The facts are undisputed. In 2006, Johnson, who was then a minor, was injured an automobile accident. In 2008, the tortfeasor's insurer, State Farm, and Johnson's guardian ad litem settled a personal injury claim on behalf of Johnson through a structured settlement agreement. Under the agreement, Johnson was entitled to receive a first payment of $ 5,000 on October 5, 2008, five annual payments of $ 10,000 each, beginning in October 5, 2010, and a final payment of $ 41,970.25 on October 5, 2020. The structured settlement agreement contained a clause stating that Johnson did not "have the power to sell, mortgage, encumber, or anticipate the Periodic Payments, or any part thereof, by assignment or otherwise." It is not disputed that the clause prohibited Johnson from transferring his interest in future payments, that is, that it is an anti-assignment clause. Thus, on its face,

the structured settlement agreement prohibited the transfer of Johnson's interest in the future payments.

***50** But State Farm could assign *its* obligation under the settlement agreement. Under Internal Revenue Code, 26 USC section 130, a tortfeasor or its insured may assign an obligation under a structured settlement agreement to a "qualified assignee"—an independent third party who assumes the obligation for making the periodic payments. The third-party assignee receives favorable income tax treatment, because the funds received by the assignee from the original obligor (to be used for the purchase of an annuity to fund the periodic payments) are excluded from the assignee's income. 26 USC § 130(a). To meet the requirements of a "qualified assignment," the payments "cannot be accelerated, deferred, increased, ****867** or decreased by the recipient of such payments." 26 USC section 130(c)(2)(B).

Consistent with 26 USC section 130(c)(2)(B), Johnson's structured settlement agreement with State Farm provided that State Farm could assign its payment obligation to Met Tower, and that Johnson was required to accept the assignment. [2] Contemporaneously with the structured settlement agreement, State Farm and Met Tower executed a qualified assignment agreement (QAA) under which Met Tower assumed responsibility for making the structured settlement payments to Johnson. [3] Like the settlement agreement, the QAA included a paragraph prohibiting Johnson from transferring his right to receive payments under the structured settlement agreement, except that a transfer could be made with advance approval of a court, pursuant to ***51** Internal Revenue Code section 5891(b)(2), [4] if the transfer "otherwise complie[d] with applicable state law." [5]

In 2013, Johnson, who was then 23 years of age, was in need of funds. He contacted J. G. Wentworth, a factoring company, expressing an interest in selling at a discount his annuity payment due in 2014, and half of his final payment ***52** due in 2020. Together, the sums had a discounted present value of just over $ 29,000. J. G. Wentworth agreed to pay Johnson $ 17,250 for the right to receive those sums in the future. In December 2013, Johnson signed an agreement for the transfer of the future payments to J. G. Wentworth. This litigation arises out of J. G. ****868** Wentworth's petition to obtain court approval of the transfer.

In Oregon, transactions like the one executed by J. G. Wentworth and Johnson for the transfer of structured settlement payment rights are subject to the provisions of ORS 33.850 to 33.875, which the legislature enacted in 2005 to implement 26 USC section 5891. [6] In February 2014, J. G. Wentworth filed a petition in Multnomah County Circuit Court seeking an order approving the transfer. As obligor under the QAA, Met Tower participated in the proceeding and objected to the transfer. After a hearing in which the trial court met with Johnson in chambers to discuss his need for the funds, the court issued an order and judgment approving of the transfer.

Met Tower now appeals from the judgment, raising several challenges. As relevant to our analysis, there are no factual disputes, and the questions presented are purely legal, involving issues of contract interpretation and statutory construction; accordingly, we review the trial court's decision for errors of law. *State v. Gaines*, 346 Or. 160, 171-72, 206 P.3d 1042 (2009) (questions of statutory construction reviewed for errors of law, first examining the text and context of the statute and any useful legislative history to determine the legislature's intent); *Yogman v. Parrott*, 325 Or. 358, 361, 937 P.2d 1019 (1997) (trial court's construction of a contract reviewed for errors of law).

ORS 33.855 describes payments subject to transfer under Oregon law and sets forth the procedural requirements for such a transfer. ORS 33.860 specifies the disclosures that ***53** the transferee (in this case, J. G. Wentworth) must make to a structured settlement beneficiary (Johnson) who seeks to transfer the right to future payments. ORS 33.865 describes the findings that a court must make in its order approving a transfer. [7] On its face, the order entered by the trial court in this case complied with ORS 33.865, in that it included all of the required findings. However, Met Tower asserts on appeal that the trial court erred, because Met Tower is entitled to enforce the anti-assignment provision in the structured settlement agreement, thereby preventing Johnson from assigning his right to future payments. [8]

The structured settlement agreement in this case was executed and approved by a court in California, and it provides that its construction is subject to California law. Therefore, we address whether, under California law, the anti-assignment provision in the structured settlement agreement was enforceable by Met Tower. ORS 15.350 ("[t]he contractual rights and duties of the parties are governed by the law or laws that the parties have chosen."); *see M+W Zander v. Scott Co. of California*, 190 Or.App. 268, 78 P.3d 118 (2003) (when parties specify their choice of law in a contract, that

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

choice will be effectuated subject to limitations under the *Restatement (Second) of Conflicts of Laws* (1971)); *Pinela v. Neiman Marcus Group, Inc.*, 238 Cal.App.4th 227, 251, 190 Cal.Rptr.3d 159 (2015) (contractual choice of law clauses are generally construed to designate the substantive law of the chosen jurisdiction as well as the interpretation of the agreement).

Under California law, although public policy strongly favors the free transferability ****869** of property, that policy must ***54** be weighed against the right of parties to freely contract. *Parkinson v. Caldwell*, 126 Cal.App.2d 548, 552, 272 P.2d 934 (1954). Thus, although contractual clauses restricting assignment of interests are strictly construed, a clear prohibition against assignment of money due under a contract will be enforced, if not waived by the obligor. *Masterson v. Sine*, 68 Cal.2d 222, 230, 65 Cal.Rptr. 545, 436 P.2d 561 (1968) ("In the absence of a controlling statute the parties may provide that a contract right or duty is nontransferable."); *Parkinson*, 126 Cal.App.2d at 552, 272 P.2d 934 ("Where [contract] language is clear, an agreement not to assign a debt is effective."); *see San Francisco Newspaper Printing Co. v. Superior Court*, 170 Cal.App.3d 438, 442, 216 Cal.Rptr. 462 (1985) (an anti-assignment clause is not inherently suspect and is "routinely enforced"); *see also Johnson v. First Colony Life Ins. Co.*, 26 F.Supp.2d 1227, 1229 (C.D. Cal. 1998) (upholding anti-assignment clause in structured settlement agreement). [9]

Nonetheless, the California Court of Appeal has held that a contractual anti-assignment clause will not bar court-approved transfers of structured settlement rights, if no interested party objects to the transfer. *See 321 Henderson Receivables Origination LLC v. Sioteco*, 173 Cal.App.4th 1059, 93 Cal.Rptr.3d 321 (2009). *Sioteco* involved an anti-assignment clause in a structured settlement agreement, which, if enforced, would bar the transfer of structured settlement payments that otherwise met the requirements of the state's "Structured Settlement Transfer Act." 173 Cal.App.4th at 1065, 1072-73, 93 Cal.Rptr.3d 321. Although no party had objected to the proposed transfers of payments under the settlement agreement at issue in *Sioteco*, the trial court had nonetheless concluded that they were barred, in part because they violated the anti-assignment provision. *Id.* at 1072, 93 Cal.Rptr.3d 321.

***55** In reversing the trial court, the Court of Appeal first noted its disagreement with the federal district court's holding in *Johnson*, 26 F.Supp.2d at 1230, that a section of the California Commercial Code generally disapproving of contractual restrictions on assignments of intangible assets did not apply to the assignment or transfer of a structured settlement payment right. The *Sioteco* court concluded that the commercial-code provision did apply to such transfers, and it also observed that the California Structured Settlement Transfer Act favored court-approved transfers of structured settlement payments. 173 Cal.App.4th at 1075, 93 Cal.Rptr.3d 321. However, the court acknowledged that "it is possible that the annuity issuer or the settlement obligor might be able to enforce those anti-assignment provisions in certain situations." *Id.* Thus, the court did not hold that anti-assignment provisions are always ineffective in the structured-settlement context; instead, it held only that, "where no interested parties object to the transfer of structured settlement payment rights," the anti-assignment provision in the structured settlement agreement "do not bar" a court-approved transfer of structured settlement payments. *Id.* at 1076, 93 Cal.Rptr.3d 321.

Sioteco is distinguishable from this case on its facts, but as the most recent California appellate decision addressing the effect of anti-assignment provisions in structured settlement agreements on the transfer of structured settlement payments, it, along with the other cases we have discussed, guides our reasoning. Here, as in *Sioteco*, the anti-assignment clause in the structured settlement agreement prohibits a transfer of the right to payments. But in this case, unlike in *Sioteco*, Met Tower, as State Farm's assignee and as the obligor under the structured settlement agreement, has objected to the transfer and seeks to enforce the anti-assignment provision. Under those circumstances, ****870** and based on our reading of *Sioteco* and California's case law regarding the general enforceability of anti-assignment clauses, we conclude that Met Tower was entitled to enforce the anti-assignment clause in the structured settlement agreement, barring the transfer.

In arguing to the contrary, J. G. Wentworth focuses on the provision in the QAA that explicitly permits a transfer of payments approved by a "qualified order." It argues ***56** that, when the settlement agreement and that provision of the QAA are considered *together*, it shows that the parties contemplated the possibility that the beneficiary would seek to transfer future payments, and that Met Tower implicitly agreed to permit such a transfer, if approved in a qualified order. Met Tower responds that under the QAA, transfer is permitted only if it "otherwise complies with applicable state law." Met Tower contends that when, as here, applicable state law permits enforcement of an anti-assignment provision by

the obligor, and the obligor seeks to enforce it, a transfer would not comply with state law.

We agree with J. G. Wentworth that the structured settlement agreement and the QAA must be construed together, because of their contemporaneous execution and related subject matters.[10] *Vertopoulos v. Siskiyou Silicates, Inc.*, 177 Or.App. 597, 602-603, 34 P.3d 704 (2001) (under California law, several documents related to the same subject matter and as parts of substantially one transaction are to be construed together as one contract). The basic goal of contract construction under California law is to give effect to the parties' mutual intentions, *Bank of the West v. Superior Court*, 2 Cal.4th 1254, 1264, 10 Cal.Rptr.2d 538, 833 P.2d 545 (1992), as evidenced by the words of the contract, *Cedars-Sinai Medical Center v. Shewry*, 137 Cal.App.4th 964, 980, 41 Cal.Rptr.3d 48 (2006). In construing seemingly conflicting provisions, the goal, when possible, is to reconcile them so as to give effect to all the provisions. *See Epic Communications, Inc. v. Richwave Technology, Inc.*, 237 Cal.App.4th 1342, 1352, 188 Cal.Rptr.3d 844, 188 Cap. Rptr. 3d 844 (2015) (conflicting contract provisions must be reconciled, if possible, by such interpretation as will give some effect to the repugnant clauses). As explained below, we conclude that Met Tower's interpretation is more consistent with the goal of reconciling the two contract provisions.

First, the express terms of the settlement agreement prohibit a transfer of the beneficiary's interest in future payments, thereby creating an anti-assignment right belonging to the obligor. It is undisputed that, by the terms ***57** of the QAA, Met Tower became the obligor under the structured settlement agreement, assuming all of State Farm's obligations. And, under California law, as the obligor under the structured settlement agreement, Met Tower is entitled to enforce the anti-assignment provision. *See Newspaper Printing Co.*, 170 Cal.App.3d at 442, 216 Cal.Rptr. 462 (an anti-assignment clause is not inherently suspect and is "routinely enforced").

Second, nothing in the QAA suggests that, by signing it, Met Tower somehow abandoned its right to enforce the anti-assignment clause in the settlement agreement, as J.G. Wentworth seems to suggest. Rather, the QAA simply describes the only set of conditions under which a transfer of the beneficiary's interest may occur *if* Met Tower chooses not to enforce the anti-assignment clause—that is, the transfer must be approved in advance by a court, pursuant to the pertinent Internal Revenue Code provisions, and must otherwise comply with state law. Thus, the QAA is consistent with the settlement agreement in that it reflects both Met Tower's explicit contractual right to enforce the anti-assignment provision and Met Tower's implicit right *not* to enforce that provision. *See Sioteco*, 173 Cal.App.4th at 1075, 93 Cal.Rptr.3d 321. Put differently, if Met Tower had not objected to Johnson transferring his right to receive structured settlement payments, then the QAA's requirements for compliance with state and federal law would have kicked in.

****871** As noted, J.G. Wentworth attaches greater significance to the QAA's description of the conditions under which a transfer may occur, suggesting that, by signing the QAA, Met Tower must have agreed never to enforce the anti-assignment clause in the settlement agreement. That proposed interpretation of the contracts would not only read the anti-assignment clause out of the settlement agreement, but would read something close to a waiver into the QAA. That interpretation does not reconcile the provisions, but instead significantly changes both contracts. Such a result is not favored under California law. *See Pinela*, 238 Cal.App.4th at 251 n. 13, 190 Cal.Rptr.3d 159 (avoiding construction that would render contract provision superfluous).

J.G. Wentworth makes a second argument, contending that Met Tower's decision to object to the transfer ***58** in this case is arbitrary and that, in light of the provision in the QAA permitting a qualified transfer when approved by the court, the documents together must be construed to impose on Met Tower an implied duty of good faith and fair dealing to permit the transfer. But the duty of good faith and fair dealing does not require a party to take action that is inconsistent with the express terms of a contract. *Carma Developers (Cal.), Inc. v. Marathon Development California, Inc.*, 2 Cal.4th 342, 371, 6 Cal.Rptr.2d 467, 826 P.2d 710 (1992) ("[A]s a general matter, implied terms should never be read to vary express terms.") *Tollefson v. Roman Catholic Bishop*, 219 Cal.App.3d 843, 854, 268 Cal.Rptr. 550 (1990) (The implied duty of good faith and fair dealing is designed to effectuate the intentions and reasonable expectations of the parties reflected within their mutual promises within the contract but cannot be used to imply an obligation which would completely obliterate a right expressly provided by a written contract.) Having reconciled the conflicting contractual provisions so as to sustain the enforceability of the anti-assignment provision, we conclude that Met Tower did not have an implied duty of good faith and fair dealing to either waive or not object to the enforcement of that provision.

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

In view of our conclusion that Met Tower was entitled to enforce the anti-assignment clause preventing Johnson from transferring his interest in the future payments under the structured settlement agreement, we conclude that Met Tower's objection to the judgment is well-taken and that the trial court erred in approving the transfer. We therefore do not reach Met Tower's remaining contentions.

Reversed and remanded.

All Citations

284 Or.App. 47, 391 P.3d 865

Footnotes

1 The statutes were amended in 2013. Or. Laws 2013, ch. 236. The amendments were effective January 1, 2014, and are not applicable to this case. All subsequent references are to the 2005 version of the statutes.

2 As relevant, the settlement agreement provided:

> "Claimant acknowledges and agrees that the Respondent and/ or the Insurer may make a 'qualified assignment,' within the meaning of Section 130(c) of the Internal Revenue Code of 1986, as amended, of the Respondent's and/or the Insurer's liability to make the Periodic Payments set forth in [the agreement] to MetLife Tower Resources Group, Inc., ('Assignees'). The Assignees' obligation for payment of the Periodic Payments shall be no greater than that of the Respondent and/ or the Insurer * * * immediately preceding the assignment of the Periodic Payment obligation."

3 The QAA was actually executed 11 days *before* the execution of the structured settlement agreement.

4 The term "factoring" has come to be associated with at least some such transfers, that is, with a secondary market in which "factoring companies"—like J.G. Wentworth—purchase rights to receive future payments associated with structured settlements, sometimes at a substantial discount. *See* Daniel W. Hindert & Craig H. Ulman, *Transfers of Structured Settlement Payment Rights: What Judges Should Know about Structured Settlement Protection Acts*, 44 No. 2 Judges' J 19, 20 (Spring 2005). 26 USC section 5891(a) imposes a "tax equal to 40 percent of the factoring discount as determined under subsection (c)(4) with respect to such factoring transaction" on any person who "acquires * * * structured settlement payment rights in a structured settlement factoring transaction" except when "the transfer of structured settlement payment rights is approved in advance in a qualified order."

26 USC section 5891(b)(2) defines a "qualified order" as a "final order, judgment, or decree" that:

"(A) finds that the transfer described in paragraph (1)—

"(i) does not contravene any Federal or State statute or the order of any court or responsible administrative authority, and

"(ii) is in the best interest of the payee, taking into account the welfare and support of the payee's dependents, and

"(B) is issued—

"(i) under the authority of an applicable State statute by an applicable State court, or

> "(ii) by the responsible administrative authority (if any) which has exclusive jurisdiction over the underlying action or proceeding which was resolved by means of the structured settlement."

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Congress enacted 26 USC section 5891 in 2001 to combat abuses associated with structured settlement factoring. *See* Hindert & Ulman, 44 No. 2 Judges' J at 20.

5 The QAA provided:

"**Acceleration, Transfer or Payment Rights.** None of the Periodic Payments and no rights to or interest in any of the Periodic Payments * * * can be

"I. * * *

"II. Sold, assigned, pledged, hypothecated or otherwise transferred or encumbered, either directly or indirectly, unless such sale, assignment, pledge, hypothecation or other transfer or encumbrance * * * has been approved in advance in a 'Qualified Order' as described in Section 5891(b)(2) of the [Internal Revenue] Code (a 'Qualified Order') and otherwise complies with applicable state law, including without limitation any applicable state structured settlement protection statute.

"No claimant or Successor Payee shall have the power to affect any Transfer of Payment Rights except as provided in sub-paragraph (II) above."

6 Provisions similar to ORS 33.850 to 33.875 have been enacted in almost every state, and are commonly described as "structured settlement protection acts." *See* Hindert & Ulman, 44 No. 2 Judges' J at 20. A lump sum payment received by a beneficiary in exchange for transferring future payment rights, pursuant to a structured settlement protection act, retains its tax exempt status. 26 USC § 5891(d).

7 Under ORS 33.865, the court must find that (1) the transfer is in the best interests of the payee, taking into account the welfare and support of all persons for whom the payee is legally obligated to provide support; (2) the payee has been advised in writing to seek advice from an attorney, certified public accountant, actuary or other licensed professional adviser regarding the transfer, and the payee has either received the advice or knowingly the waived advice in writing; and (3) the transfer "does not contravene any applicable statute or order of any court[.]"

8 Met Tower also challenges other aspects of the court's order, including its finding that the transfer is in Johnson's best interests, as required by ORS 33.865(1), and its conclusion that the transfer does not contravene any applicable statute, as required by ORS 33.865(3). In view of our conclusion relating to the anti-assignment clause, we do not reach those contentions.

9 Anti-assignment provisions are also generally enforceable in Oregon. *See, e.g.*, *Holloway v. Republic Indemnity Co. of America*, 341 Or. 642, 651-52, 147 P.3d 329 (2006) (anti-assignment provision in insurance contract was not ambiguous and rendered invalid insured's assignment of payment rights under policy). In *Holloway*, the court said that an unambiguous anti-assignment clause in an insurance contract was enforceable against the insured. In that case, the insurance policy provided: "Your rights or duties under this policy may not be transferred without our written consent." 341 Or. at 645, 147 P.3d 329. The court concluded that the clause was unambiguous and prohibited the insured's assignment of rights under the policy. *Id.* at 651, 147 P.3d 329.

10 That conclusion is consistent with the pertinent Oregon statutes. For purposes of ORS 33.850 to 33.875, ORS 33.850(8) defines the "terms of the structured settlement agreement" to include the terms of the QAA.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-17

50 F.Supp.3d 1221
United States District Court, N.D. California,
Oakland Division.

Mike MAPLES, Jr., Plaintiff,
v.
SOLARWINDS, INC., and Does 1–5, Defendants.

Case No: C 12–6066 SBA
|
Signed June 20, 2014
|
Filed June 23, 2014

Synopsis

Background: Advisor to information technology (IT) corporation filed state court suit against the company, alleging breach of stock option agreement, breach of advisor agreement, breach of contract based on covenant of good faith and fair dealing, wrongful discharge, unjust enrichment, promissory fraud, and unfair competition. Following removal, defendant moved for summary judgment.

Holdings: The District Court, Saundra Brown Armstrong, J., held that:

genuine issue of material fact as to whether stock options had expired precluded summary judgment on claims for breach of stock option agreement and breach of advisor agreement;

agreements did not require company to notify advisor that his role within the company had ended; and

express contract precluded claim for unjust enrichment.

Motion granted in part and denied in part.

Procedural Posture(s): Motion for Summary Judgment.

Attorneys and Law Firms

***1223** Tania Beth Rose, Law Offices of Tania Rose, San Francisco, CA, Benjamin Francis Foster, Demetrios Anaipakos, Ahmad, Zavitsanos, Anaipakos, Alavi Mensing, P.C., Houston, TX, for Plaintiff.

Gloria C. Franke, Zia Modabber, Tami Kameda Sims, Katten Muchin Rosenman LLP, Los Angeles, CA, for Defendants.

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT'S MOTION FOR SUMMARY JUDGMENT

Dkt. 43

SAUNDRA BROWN ARMSTRONG, United States District Judge

This is a diversity jurisdiction action brought by Plaintiff Mike Maples ("Plaintiff" or "Maples"), who alleges that Defendant SolarWinds, Inc. ("Defendant" or "SolarWinds") is refusing to allow him to exercise his stock options in violation of their written agreements. The parties are presently before the Court on Defendant's Motion for Summary Judgment, or in the Alternative, Partial Summary Judgment. Dkt. 43. Having read and considered the papers filed in connection with this matter and being fully informed, the Court hereby GRANTS IN PART and DENIES IN PART the motion for the reasons set forth below. The Court, in its discretion, finds this matter suitable for resolution without oral argument. *See* Fed. R. Civ. P. 78(b); N.D. Cal. Civ. L.R. 7–1(b).

I. *BACKGROUND*

A. FACTUAL SUMMARY

SolarWinds is a Texas-based company that develops enterprise information technology ("IT") infrastructure management software for IT professionals. In 2007, SolarWinds became interested in retaining Maples, a venture-capitalist with experience in the technology sector, as an advisor. Foster Decl. Ex. 4 ("Van Zant Decl.") ***1224** ¶ 4, Dkt. 58–5. Kenny Van Sant ("Van Sant"), then SolarWinds' Chief Product Strategist, knew Maples from having worked with him at Motive Communications, a company Maples co-founded. *Id.* ¶ 4. Then Chief Executive Officer Michael Bennett ("Bennett") and Van Zant discussed the terms and structure of the proposed relationship with Maples, and envisioned that the consulting agreement would "auto-renew" after the initial four-year term, until one party explicitly cancelled it. *Id.* ¶ 9.

On August 6, 2007, SolarWinds sent an offer letter ("Advisor Agreement") to Maples to memorialize their agreement. Compl. Ex. C. The first paragraph of the Advisor Agreement states:

> This letter confirms SolarWinds.net, Inc.'s ("SolarWinds") invitation to you to serve as an Advisor for SolarWinds. Although currently, we do not expect to have any formal meeting of the Advisory Board, we would like you to provide advice to various members of our executive team from time-to-time as described below over a *four year term beginning August 13, 2007....*

Id. at 1. The services Maples was expected to provide included an introductory half-day meeting; bi-weekly hour-long telephone calls and informal calls with the Vice–Presidents of Marketing, Strategy and Product Marketing; and quarterly meetings with various executives. *Id.* In exchange for providing these services, SolarWinds agreed to compensate Maples solely in the form of stock options:

> In consideration of your willingness to serve on our advisory board and attend its meetings, SolarWinds agrees to compensate you as follows:
>
> • SolarWinds will grant you a non-statutory stock option to purchase 5000 shares of SolarWinds common stock..... *The options will be granted pursuant to, and subject to the terms of, SolarWinds' standard stock option plan.* Assuming an optionee's continued membership on the advisory board and participation in its meetings from the date of grant until four years from the grant date, these options will vest and will be become fully exercisable on that date. *The options will expire on the earlier of three months after the termination of service on the advisory board* (or such period as SolarWinds' board of directors may permit) *or ten years from the date of the grant.*

Id. at 2 (emphasis added). The Advisor Agreement was signed by Bennett on behalf of SolarWinds, and countersigned by Maples. *Id.*

In connection with his retention, Maples also executed a Stock Option Agreement.[1] Section I of that agreement, entitled "Notice of Stock Option Grant," specifies that 5,000 stock options were granted as of October 25, 2007, and that the "Term/Expiration Date" of those options is October 25, 2017. *Id.* Ex. D at 1. That section also states that: "This Option shall be exercisable for *ninety (90) days after the Participant ceases service or employment with the employer* for reasons other than Cause, death or Disability.... Notwithstanding the foregoing, in no event may this Option be exercised after the Term/Expiration Date as provided above...." *Id.* at 2 (emphasis added). The Stock Option Agreement "is governed ***1225** by the substantive laws but not the choice of law rule of Oklahoma." *Id.* at 5.

Though SolarWinds contemplated hiring additional advisors and forming an advisory board, that never transpired. Van Zant Decl. ¶¶ 6–8. Nonetheless, Maples provided advisory services in person, by telephone and email to various individuals at SolarWinds, including Van Zant, Bennett and Rita Selvaggi ("Selvaggi"), SolarWinds' Vice–President of Marketing. *Id.* ¶ 11; Foster Decl. Ex. 2 ¶ 4, Dkt. 58–3. By 2010, Bennett, Van Zant and Selvaggi had left SolarWinds. Foster Decl. Ex. 4 ¶ 2; Sims Decl. Ex. A at 19:4–5, Dkt. 44–1; *id.* Ex. E at 9:8–18. The last time Maples provided consultation to anyone at SolarWinds was some time in 2010. Sims Decl. Ex. B at 150:3–11. However, Maples testified in his deposition that neither side has given notice to the other that his role as an advisor had been terminated, and to this day he remains willing and available to provide advice to SolarWinds. Foster Decl. Ex. 3 at 153:6–154:12, Dkt. 58–4.

Towards the end of 2011, Maples was going through a divorce. Foster Decl. Ex. 3 at 183:21–184:18. While having the means to support himself independently, Maples was concerned that his wife did not. *Id.* As a result, Maples believed that, given the high stock valuation[2], it was an opportune time to exercise his options. *Id.* Maples consulted his wife, and she agreed with his plan. *Id.* To that end, on December 2, 2011, Maples contacted SolarWinds through its Investor Relations email address, stating:

> Hi! I am an advisor to SolarWinds and was awarded some options by Mike Bennett in 2007.
>
> I was hoping to exercise and sell them but I am not sure who the best contact at SolarWinds is to close the loop. Could you please help me to file the right person to connect with?
>
> Thanks!

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Foster Decl. Ex. 11. On January 12, 2012, Mike Berry ("Berry"), then Chief Financial Officer of SolarWinds, responded to Maples' inquiry. *Id.* Ex. 12. Berry stated:

> *I checked with our Legal team,* you were granted 5,000 options in October 2007 and there was a subsequent 3 for 1 split *so you have 15,000 options with a strike price of $4.3467 per option.* I have attached a statement from our option system with the details.
>
> If you have any questions or want to exercise these in the future you would need to contact Michael Snyder or Jason Bliss in our legal department, they are copied on this email for your future reference.

Id. (emphasis added). The attached Optionee Statement indicates that as of November 11, 2011, Maples had 15,000 options that expire on "10/25/2017." *Id.* [3]

On April 17, 2012, Maples emailed Jason Bliss ("Bliss"), then SolarWinds' Associate General Counsel, stating that he wanted to exercise his options. *Id.* Ex. 17. The next day, Bliss responded, "Mike, no worries—I'll get you an answer by tomorrow." *Id.* Bliss did not follow up with Maples; instead, on April 20, 2012, Maples received an email from Berry asking him to call. *Id.* Ex. 18. Maples called Berry, who stated that his options had expired, and that "there was nothing he could do." Maples Decl. ¶ 7. The following Monday, Maples emailed Berry, explaining that he never ***1226** resigned from his advisor role and that SolarWinds should honor the options, particularly since they were the sole compensation for his services. Foster Decl. Ex. 19. Berry did not respond. Instead, Bryan Sims ("Sims"), General Counsel for SolarWinds, emailed Maples claiming that his options expired "90 days after the advisory agreement ended [on August 12, 2011]." *Id.* Sims also rhetorically questioned what possible advice Maples could have provided to SolarWinds since Bennett, the CEO who had hired Maples, left the company in 2010. *Id.*

B. PROCEDURAL HISTORY

On August 17, 2012, Maples filed the instant action against SolarWinds in San Mateo County Superior Court. The Complaint alleges seven causes of action, styled as follows: (1) Breach of Contract (Stock Option Agreement); (2) Breach of Agreement (Advisor Agreement); (3) Breach of Contract (Covenant of Good Faith and Fair Dealing); (4) Wrongful Discharge in Violation of Public Policy; (5) Unjust Enrichment; (6) Promissory Fraud; (7) Unfair Competition. On November 29, 2012, Solarwinds removed the action on the basis of diversity jurisdiction.

SolarWinds has now filed a motion for summary judgment, or alternatively, partial summary judgment, as to all causes of action alleged in the Complaint. Maples opposes the motion, except as to his causes of action for wrongful discharge and promissory fraud, which he seeks to voluntarily dismiss. The motion is fully briefed and is ripe for adjudication. [4]

II. *LEGAL STANDARD*

Federal Rule of Civil Procedure 56 provides that a party may move for summary judgment on some or all of the claims or defenses presented in an action. Fed. R. Civ. P. 56(a)(1). "The court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." *Id.*; *see Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 247–48, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986). The movant bears the initial burden of demonstrating the basis for the motion and identifying the portions of the pleadings, depositions, answers to interrogatories, affidavits, and admissions on file that establish the absence of a triable issue of material fact. *Celotex Corp. v. Catrett,* 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986); Fed. R. Civ. P. 56(c)(1)(A) (requiring citation to "particular parts of materials in the record"). If the moving party meets this initial burden, the burden then shifts to the non-moving party to present specific facts showing that there is a genuine issue for trial. *See Celotex,* 477 U.S. at 324, 106 S.Ct. 2548; *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.,* 475 U.S. 574, 586–87, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986).

"On a motion for summary judgment, 'facts must be viewed in the light most favorable to the nonmoving party only if there is a 'genuine' dispute as to those facts.' " *Ricci v. DeStefano,* 557 U.S. 557, 586, 129 S.Ct. 2658, 174 L.Ed.2d 490 (2009) (quoting in part *Scott v. Harris,* 550 U.S. 372, 380, 127 S.Ct. 1769, 167 L.Ed.2d 686 (2007)). "Only disputes over facts that might affect the outcome of the suit under ***1227** the governing law will properly preclude the entry of summary judgment. Factual disputes that are irrelevant or unnecessary will not be counted." *Anderson,* 477 U.S. at 248, 106 S.Ct. 2505. A factual dispute is genuine if it "properly can be resolved in favor of either party." *Id.* at 250, 106 S.Ct. 2505. Accordingly, a genuine issue for trial exists if the non-movant presents evidence from which a reasonable

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

jury, viewing the evidence in the light most favorable to that party, could resolve the material issue in his or her favor. *Id.* "If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted." *Id.* at 249–50, 106 S.Ct. 2505 (internal citations omitted). Only admissible evidence may be considered in ruling on a motion for summary judgment. *Orr v. Bank of Am.,* 285 F.3d 764, 773 (9th Cir.2002).

III. *DISCUSSION*

A. CHOICE OF LAW

Federal courts sitting in diversity apply the substantive law of the forum state, which, in this case, is California. *See Gasperini v. Center for Humanities,* 518 U.S. 415, 427, 116 S.Ct. 2211, 135 L.Ed.2d 659 (1996) ("[F]ederal courts sitting in diversity apply state substantive law and federal procedural law"). When an agreement contains a choice-of-law provision, California courts apply the parties' choice-of-law unless the approach set forth in Restatement (Second) of Conflict of Laws § 187 dictates a different result. *Bridge Fund Capital Corp. v. Fastbucks Franchise Corp.,* 622 F.3d 996, 1002 (9th Cir.2010). Under the Restatement, the court first determines "(1) whether the chosen state has a substantial relationship to the parties or their transaction, or (2) whether there is any other reasonable basis for the parties' choice of law." *Nedlloyd Lines B.V. v.Super. Ct.,* 3 Cal.4th 459, 465–466, 11 Cal.Rptr.2d 330, 834 P.2d 1148 (1992). If neither of these tests is met, "the court need not enforce the parties' choice of law." *Id.* But if either test is met, the court must then determine whether the chosen state's law is contrary to a fundamental policy of California. *Id.* If so, the court must assess whether California has a materially greater interest than the chosen state in the determination of the particular issue; if so, the court applies California law, notwithstanding the parties' choice-of-law provision. *Id.* at 1002–1003.

Here, the Advisor Agreement does not contain a choice of law clause and therefore California law presumptively applies to issues relating to that agreement. In contrast, the Stock Option Agreement contains a choice of law clause which states that "[it] is govered by the internal substantive laws but not the choice of law rules of Oklahoma." Compl. Ex. D § II.12. Maples argues that, notwithstanding this choice of law clause, California law applies to this action.[5] The Court agrees. There is no indication that Oklahoma has a substantial relationship to the parties or their transaction or that there is any other reasonable basis for applying Oklahoma law. To the contrary, the record shows that Maples is a California resident, while SolarWinds is a Delaware corporation headquartered in Austin, Texas. Thus, the states with a substantial interest are those other than Oklahoma. *See Nedlloyd Lines B.V.,* 3 Cal.4th at 467, 11 Cal.Rptr.2d 330, 834 P.2d 1148; *see also* ***1228** Restatement (Second) of Conflict of Laws § 187 cmt. f (recognizing that a "substantial relationship" with the chosen state exists where "one of the parties is domiciled or has his principal place of business" there). Accordingly, the Court finds that California law applies to the instant claims at issue in the instant motion to dismiss.

B. BREACH OF CONTRACT

"[T]he elements of a cause of action for breach of contract are (1) the existence of the contract, (2) plaintiff's performance or excuse for nonperformance, (3) defendant's breach, and (4) the resulting damages to the plaintiff." *Oasis West Realty, LLC v. Goldman,* 51 Cal.4th 811, 821, 124 Cal.Rptr.3d 256, 250 P.3d 1115 (2011). In his first two causes of action, Maples alleges that SolarWinds breached the Advisor Agreement and Stock Option Agreement by failing to allow him to exercise his stock options. Compl. ¶¶ 30–37. SolarWinds denies that it breached these agreements, claiming that by the time Maples sought to exercise his options in 2011, they had already expired. Mot. at 8–14, Dkt. 43.

1. Rules Governing Contract Interpretation

Under California law, contracts are to be interpreted to give effect to the mutual intention of the parties at the time of contracting. Cal. Civ. Code § 1638; *Waller v. Truck Ins. Exch.,* 11 Cal.4th 1, 18, 44 Cal.Rptr.2d 370, 900 P.2d 619 (1995). "[S]uch intent is to be inferred, if possible, solely from the written provisions of the contract," read in their ordinary and popular sense, unless it appears the parties used the terms in some special sense. *AIU Ins. Co. v. FMC Corp.,* 51 Cal.3d 807, 822, 274 Cal.Rptr. 820, 799 P.2d 1253 (1995) (citing Cal. Civ. Code § 1639). "[T]he meaning of a contract must be derived from reading the whole of the contract, with individual provisions interpreted together, in order to give effect to all provisions and to avoid rendering some meaningless." *Zalkind v. Ceradyne, Inc.,* 194 Cal.App.4th 1010, 1027, 124 Cal.Rptr.3d 105 (2011). "When interpreting contracts, the language used controls if it is clear and explicit." *Segal v. Silberstein,* 156 Cal.App.4th 627, 633, 67 Cal.Rptr.3d 426 (2007). But where a contract is "capable of two or more constructions, both of which are reasonable," it is considered ambiguous. *TRB Invs., Inc. v. Fireman's Fund Ins. Co.,* 40

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Cal.4th 19, 27, 50 Cal.Rptr.3d 597, 145 P.3d 472 (2006). "When ambiguities ... cannot be dispelled by application of the other rules of contract interpretation, they are resolved against the drafter." *Badie v. Bank of Am.,* 67 Cal.App.4th 779, 798–799, 79 Cal.Rptr.2d 273 (1998) (citing Cal. Civ. Code § 1654).

Aside from its obligation to ascertain whether a contract is clear or ambiguous, a court has a duty to construe a contract to avoid a forfeiture, if at all possible. *See* Cal. Civ. Code § 1442 (contractual conditions involving forfeitures strictly construed against "party for whose benefit it is created"). "Forfeitures are not favored by the courts, and, if an agreement can be reasonably interpreted so as to avoid a forfeiture, it is the duty of the court to avoid it." *Universal Sales Corp. v. Cal., Press Mfg. Co.,* 20 Cal.2d 751, 771, 128 P.2d 665 (1942)); *Chase v. Blue Cross of Cal.,* 42 Cal.App.4th 1142, 1157, 50 Cal.Rptr.2d 178 (1996) ("Forfeiture of a contractual right is not favored in the law"). "Forfeitures, as such, are not favored by the courts, and are never enforced if they are couched in ambiguous terms." *McNeece v. Wood,* 204 Cal. 280, 284, 267 P. 877 (1928).

2. Contentions

SolarWinds contends that the Advisor Agreement specifically limits Maples' term ***1229** to four years, from August 13, 2007, to August 12, 2011, and that under the terms of the Stock Option Agreement, he had only ninety days after the end of his term to exercise his options, such that they expired after November 10, 2011. Mot. at 9–11; Reply at 1–5. The starting point for determining whether Maples' options have expired is "the language of the contract itself." *Mount Diablo Med. Ctr. v. Health Net of Cal., Inc.,* 101 Cal.App.4th 711, 722, 124 Cal.Rptr.2d 607 (2002). Here, the two agreements at issue—the Advisor Agreement and the Stock Purchase Agreement—each contain different language concerning the time period within which Maples must exercise his options. The Advisor Agreement provides that "[t]he options will expire on the earlier of three months after the termination of service on the advisory board (or such period as SolarWinds' board of directors may permit) or ten years from the date of the grant." *Id.* In contrast, the Stock Option Agreement specifies that "[t]his Option [i.e., the 5,000 stock options] shall be exercisable for ninety (90) days after the Participant ceases service or employment with the employer for reasons other than Cause, death or Disability," but in no event "may this Option be exercised after the Term/Expiration Date as provided above...." Compl. Ex. D at 2.

According to Maples, although he fully performed under the Advisor Agreement, SolarWinds never actually created an advisory board. Maples posits that because no advisory board ever existed, he could not have been terminated from "service on the advisory board," meaning that the second deadline—"ten years from the date of the [option] grant"—controls, and the options have yet to expire. [6] SolarWinds does not dispute that Maples' proposed construction of the Advisor Agreement is facially reasonable, but instead argues that the Court should disregard the expiration language of the Advisor Agreement on the ground that the grant of the options is controlled exclusively by the Stock Option Agreement. Unlike the Advisory Agreement, the Stock Option Agreement makes no reference to service on the advisory board and specifies only that the options must be exercised within ninety days of the date Maples "ceases service or employment with the employer." SolarWinds maintains that Maples ceased providing services to SolarWinds after August 12, 2011, and that under the Stock Option Agreement, his options expired ninety days thereafter—irrespective of the fact that he was never actually terminated from an advisory board. Reply at 1–3. [7]

***1230** The Court is unpersuaded that SolarWinds is entitled to summary judgment in its favor on Maples' breach of contract claims. As an initial matter, SolarWinds' argument fails to account for the conflicting provisions regarding the expiration of Maples' stock options. As noted, the triggering provisions are different; i.e., "termination of service on the advisory board" versus "ceases service ... with the employer." [8] SolarWinds offers no explanation for these discrepancies or how to reconcile them. SolarWinds simply argues that because the options are subject to the terms of the Stock Option Agreement, the Court should simply disregard the language in the Advisor Agreement pertaining to the timeframes by which Maples must exercise his options. The flaw in that argument is that it overlooks the fundamental rule of contract interpretation that specific terms of a contract cannot be ignored. *See Lyons v. Fire Ins. Exch.,* 161 Cal.App.4th 880, 886–887, 74 Cal.Rptr.3d 649 (2008) (a court cannot read contract so as to ignore certain of its provisions, as "such a reading would be contrary to the rule that all words in a contract are to be given meaning" with the "language in the contract 'interpreted as a whole ' "). [9] At the very least, these conflicting expiration provisions create

an ambiguity which is construed against SolarWinds. *See Garvey v. State Farm Fire & Cas. Co.,* 48 Cal.3d 395, 433, 257 Cal.Rptr. 292, 770 P.2d 704 (1989) (ambiguities are to be construed against the drafter). [10]

Moreover, SolarWinds' contention that the options have expired is contrary to the rule that where there are two or more reasonable interpretations of a contract, the court is obligated to adopt the interpretation that avoids a forfeiture. *See Milenbach v. C.I.R.,* 318 F.3d 924, 936 (9th Cir.2003) ("Where there are two possible interpretations of a contract, one that leads to a forfeiture and one that avoids it, California law requires the adoption of the interpretation that avoids forfeiture, if at all possible"); *Ballard v. MacCallum,* 15 Cal.2d 439, 444, 101 P.2d 692 (1940) ("We have two possible constructions, one of which leads to a forfeiture and the other ***1231** avoids it. In such a case the policy and rule are settled, both in the interpretation of ordinary contracts and instruments transferring property, that the construction which avoids forfeiture must be made if it is at all possible."). Here, Maples has provided a reasonable interpretation of the subject agreements; to wit, that because he was never terminated from the advisory board, the options are exercisable up to ten years after the options grant. The fact that the Stock Option Agreement specifies a contradictory expiration provision underscores the lack of merit underlying SolarWinds' position. *See McNeece,* 204 Cal. at 284, 267 P. 877 (ambiguous contracts cannot support a forfeiture); *Universal Sales Corp.,* 20 Cal.2d at 771, 128 P.2d 665 ("A contract is not to be construed to provide a forfeiture, unless no other interpretation is reasonably possible."). Accordingly, SolarWinds' motion for summary judgment on Maples' first and second causes of action for breach of contract is DENIED. [11]

C. BREACH OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

"[E]very contract contains an implied covenant of good faith and fair dealing that neither party will do anything which will injure the right of the other to receive the benefits of the agreement." *Wolf v. Walt Disney Pictures & Tel.,* 162 Cal.App.4th 1107, 1120, 76 Cal.Rptr.3d 585 (2008) (internal quotations omitted). To establish a claim for breach of the implied covenant, the plaintiff must show that the defendant "lacked subjective good faith in the validity of its act" or that "the act was intended to and did frustrate the common purpose" of the underlying contract. *Id.* at 1123, 76 Cal.Rptr.3d 585.

In the instant case, Maples alleges that SolarWinds breached the implied covenant of good faith and fair dealing by terminating him "in August 2011 retroactively without notifying him, and while he was still acting as an advisor, it breached the covenants of good faith and fair dealing in the Stock Option Agreement and in the Advisor Agreement." Compl. ¶ 40. To the extent that Maples is claiming that SolarWinds should have informed him in August 2011 that his Advisor role had ended so that he would have known to timely exercise his options, no such obligation is stated or implied in either of the agreements at issue. *See* ***1232** *Vons Cos., Inc. v. U.S. Fire Ins. Co.,* 78 Cal.App.4th 52, 59, 92 Cal.Rptr.2d 597 (2000) ("We do not have the power to create for the parties a contract that they did not make and cannot insert language that one party now wishes were there.").

In his opposition, Maples posits a new claim that SolarWinds breached the implied covenant of good faith and fair dealing by declining to extend the time period within which to exercise his stock options. Opp'n at 17–18, Dkt. 58. On a motion for summary judgment, the plaintiff's allegations and theories of liability are confined to those found in the operative complaint. *See Coleman v. Quaker Oats Co.,* 232 F.3d 1271, 1292 (9th Cir.2000) ("A complaint guides the parties' discovery, putting the defendant on notice of the evidence it needs to adduce in order to defend against the plaintiff's allegations."). Since this particular claim is not alleged in the pleadings, it not properly before the Court. *See Pickern v. Pier 1 Imps. (U.S.), Inc.,* 457 F.3d 963, 968–69 (9th Cir.2006) (refusing to allow the plaintiff to assert new specific factual allegations in support of a claim when they were "presented for the first time in [the plaintiff's] opposition to summary judgment"). But even if it were alleged, SolarWinds cannot be found liable simply for declining to extend the time period for Maples to exercise his options in the absence of any legal or contractual obligation to do so. Accordingly, SolarWinds' motion for summary judgment on Maples' third cause of action for breach of the implied covenant of good faith and fair dealing is GRANTED.

D. UNJUST ENRICHMENT

The elements of unjust enrichment are: (1) receipt of a benefit; and (2) the unjust retention of the benefit at the expense of another. *Peterson v. Cellco P'ship,* 164 Cal.App.4th 1583, 1593, 80 Cal.Rptr.3d 316 (2008). "[U]njust enrichment is an action in quasi-contract, which does not lie when an enforceable, binding agreement exists defining the rights of the parties." *Paracor Fin. v. Gen. Elec. Capital Corp.,*

96 F.3d 1151, 1167 (9th Cir.1996); *Cal. Med. Ass'n v. Aetna U.S. Healthcare of Cal., Inc.,* 94 Cal.App.4th 151, 172, 114 Cal.Rptr.2d 109 (2001) ("[A]s a matter of law, a quasi-contract action for unjust enrichment does not lie where, as here, express binding agreements exist and define the parties' rights."). Because express agreements (i.e., the Advisor Agreement and the Stock Option Agreement) define Maples' right to the options, his stand-alone claim for unjust enrichment claim cannot survive.

Citing *Hernandez v. Lopez,* 180 Cal.App.4th 932, 103 Cal.Rptr.3d 376 (2009), Maples contends that he should be able to proceed on an unjust enrichment theory in the event he is precluded from recovery under the two agreements at issue. The court in *Hernandez,* however, explained that unjust enrichment "does not describe a theory of recovery, but an effect: the result of a failure to make restitution under circumstances where it is equitable to do so." *Id.* at 939, 103 Cal.Rptr.3d 376 (internal quotations and citations omitted). As such, the court recognized that "a plaintiff need not amend his pleading to seek compensation under an unjust enrichment theory, but could do so based on the pleaded cause of action for breach of contract." *Id.* Here, the fact that Maples cannot state an independent claim for unjust enrichment will not preclude his recovery on an unjust enrichment theory. *See Unique Functional Prods., Inc. v. JCA Corp.,* No. 9–cv–265–JM–MDD, 2012 WL 367245, at *3 n. 2 (S.D.Cal. Feb. 3, 2012) ("The court notes that the disposition of this issue [i.e., the dismissal of the unjust enrichment claim] will not preclude JCA's recovery on an unjust enrichment ***1233** theory if the facts eventually demonstrate that no contract covers the dispute at issue"). Accordingly, SolarWinds' motion for summary judgment on Maples' fifth cause of action for unjust enrichment is GRANTED.

E. UNFAIR COMPETITION

California's Unfair Competition Law ("UCL") makes actionable any "unlawful, unfair or fraudulent business act or practice." Cal. Bus. & Prof. Code § 17200. "Each prong of the UCL is a separate and distinct theory of liability." *Birdsong v. Apple, Inc.,* 590 F.3d 955, 959 (9th Cir.2009).

SolarWinds briefly contends that Maples' UCL claim is derivative of his other causes of action, and since those claims fail, so too must his claim under the UCL. Mot. at 19. Maples agrees that his UCL claim stands or falls depending on the Court's assessment of his other causes of action. Opp'n at 2. Accordingly, SolarWinds' motion for summary judgment as to Maples seventh cause of action under the UCL is GRANTED IN PART and DENIED IN PART, as set forth in this Order.

F. REMAINING CAUSES OF ACTION

With regard to his fourth cause of action for wrongful termination in violation of public policy and sixth cause of action for promissory fraud, Maples states that he is "voluntarily withdrawing" those claims. Opp'n at 2. In response, SolarWinds faults Maples for not abandoning these claims earlier, and urges the Court to grant summary judgment on both claims. *Id.* [12] SolarWinds' contention lacks merit. The proper course of action is to construe Maples' voluntary withdrawal as a motion to amend under Federal Rule of Civil Procedure 15(a). *Hells Canyon Preservation Council v. U.S. Forest Serv.,* 403 F.3d 683, 689 (9th Cir.2005)("what the district court should have done, and what we believe it did do, was treat [plaintiff's] oral withdrawal of its Wilderness Act claim as a motion to amend its complaint under Rule 15(a)."). Since SolarWinds does not object to Maples' withdrawal of the claims, the Court construes such withdrawal as a motion to amend, which is GRANTED. Accordingly, SolarWinds' motion for summary judgment as to these claims is DENIED as moot. *Id.*

IV. *CONCLUSION*

For the reasons stated above,

IT IS HEREBY ORDERED THAT:

1. Plaintiff's motion for leave to file a surreply is DENIED as moot.

2. Defendant's motion for summary judgment is DENIED as to the causes of action for breach of contract; GRANTED as to the causes of action for breach of the implied covenant of good faith and fair dealing and unjust enrichment; and GRANTED IN PART and DENIED IN PART as to the cause of action for violation of the UCL.

3. Plaintiff's requests to withdraw his causes of action for wrongful termination in violation of public policy and promissory fraud are construed as a motion to amend under Rule 15(a), and such motion is GRANTED. Defendant's motion for summary judgment as to these two causes of action is DENIED as moot.

***1234** 4. The parties are ordered to appear before Magistrate Judge Donna Ryu for a further, mandatory settlement

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

conference. Magistrate Judge Ryu will notify the parties of the date and time of said conference.

IT IS SO ORDERED.

All Citations

50 F.Supp.3d 1221

Footnotes

1 The Advisor Agreement references "SolarWinds' standard stock option plan." Compl. Ex. C at 1. That "plan" appears to refer to the Stock Option Agreement, attached to which is a Stock Incentive Plan. *Id.* Ex. D.

2 SolarWinds became a publicly-traded company following its initial public offering in 2009.

3 SolarWinds' December 2011 10–K also indicated that Maples' options were outstanding. *Id.* Ex. 12.

4 In its reply, SolarWinds objects to certain statements in the Maples and Van Zant declarations. Dkt. 59. Because those statements are not germane to the Court's ruling, the objections are overruled as moot. Separately, Maples has filed a motion for leave to file a surreply to address arguments raised by SolarWinds for the first time in its reply. Dkt. 62. The Court finds that consideration of the surreply is unnecessary and therefore Maples' request for leave is denied as moot.

5 SolarWinds does not directly respond to Maples' contention, other than to note there are no substantive differences in the contract laws of California or Oklahoma and that the choice of law provision in the Stock Option Agreement "does not alter the analysis." Reply at 1 n.2.

6 SolarWinds contends that if Maples never served on an advisory board, he could not have earned the options in the first instance. Reply at 3. Since SolarWinds did not predicate its motion for summary judgment on Maples' alleged failure to perform, this argument is not properly before the Court. *See Zamani v. Carnes,* 491 F.3d 990, 997 (9th Cir.2007) ("The district court need not consider arguments raised for the first time in a reply brief."). In any event, the record shows that, pursuant to the Advisor Agreement, Maples routinely provided consulting services to SolarWinds. There no evidence that SolarWinds ever expressed any concern to Maples that he was not satisfactorily performing under the agreement.

7 SolarWinds contends that if Maples never served on an advisory board, he could have earned the options in the first instance. Reply at 3. Since SolarWinds did not predicate its motion for summary judgment on Maples' alleged failure to perform, this argument is not properly before the Court. *See Zamani v. Carnes,* 491 F.3d 990, 997 (9th Cir.2007) ("The district court need not consider arguments raised for the first time in a reply brief."). In any event, the record shows that, pursuant to the Advisor Agreement, Maples routinely provided consulting services to SolarWinds. There no evidence that SolarWinds ever expressed any concern to Maples that he was not performing under the agreement. To the contrary, the evidence presented shows that SolarWinds was satisfied with his services.

8 The operative time periods are different, as "three months" is not the same as "ninety (90) days." *See Allen v. Stoddard,* 212 Cal.App.4th 807, 811, 152 Cal.Rptr.3d 71 (2013) (noting a "three month" deadline is "distinct" from a "ninety day" deadline).

9 Arguably, SolarWinds' argument might have been colorable if the Advisor Agreement were silent as to when Maples must exercise his options. *See St. Paul Mercury Ins. Co. v. Am. Safety Indem. St. Paul Mercury Ins. Co. v. Am. Safety Indem. Co.,* No. C 12–5952 LHK, 2014 WL 2120347, at *10 (N.D.Cal. May 21, 2014) ("The doctrine of incorporation by reference allows a document or provision to be read into an agreement despite being omitted from the agreement itself.") (citing 11 Richard A. Lord, Williston on Contracts § 30:25 (4th ed.2011)). However, the Advisor Agreement is not silent, and, in fact, provides explicit criteria and deadlines governing the exercise of the options which are inconsistent with those purportedly incorporated by reference from the Stock Option Agreement.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

10 Indeed, SolarWinds, after consulting with its legal counsel, originally believed that Maples had 15,000 shares (due to the 3–to–1 stock split) that were exercisable at the time of his inquiry in 2011. SolarWinds counters that its ostensibly erroneous belief carries no legal effect. Mot. at 12. The cases cited by SolarWinds, i.e., *Jones v. Bank of Am.,* N.A., 311 F.Supp.2d 828, 834 (D.Ariz.2003) and *Roy v. General Electric Company,* 544 F.Supp.2d 103, 109 (D.R.I.2008), are inapposite, as neither involved a situation where the plaintiff was subject to two conflicting provisions regarding when he must exercise his options. In any event, even if SolarWinds' mistake carries no legal consequence, it certainly an underscores the ambiguity in the contracts that form the basis of this action.

11 As an alternative matter, Maples argues that even if the Stock Option Agreement "ceases service ... with the employer" provision controlled to the exclusion of the Advisor Agreement, he remained an advisor to SolarWinds after his initial four-year term expired because the agreement auto-renewed after the initial four-year term and neither party sought to terminate the relationship thereafter. SolarWinds counters that Maples' evidence on this point—i.e., statements by Van Zant regarding the SolarWinds' intent in entering into a contract with Maples, *see* Van Zant Decl. ¶ 9, are inadmissible as parol evidence on the ground that they contradict the terms of the Advisor Agreement. *See Haggard v. Kimberly Quality Care, Inc.,* 39 Cal.App.4th 508, 518, 46 Cal.Rptr.2d 16 (1995) ("If the proposed parol evidence directly contradicts an express provision of the written agreement, however, it cannot reasonably be presumed that the parties intended to integrate two directly contradictory terms in the same agreement.") (internal quotations omitted). No direct contradiction is apparent. The Advisor Agreement clearly contemplates service beyond four years, otherwise it would not have included a provision that the options would expire three months after termination from the advisory board *or* up to ten years from the option grant. SolarWinds also contends that Maples provided no consultations after 2010. However, there is some evidence that both parties comported themselves as if the relationship were continuing. Ultimately, the Court need not resolve these particular arguments in light of its conclusion that the expiration provisions of the subject agreements are ambiguous.

12 It is somewhat troubling that Maples failed to dismiss his wrongful termination and promissory fraud claims earlier—at the very least after the close of discovery and before SolarWinds briefed its motion for summary judgment. A meaningful meet and confer process should have resulted in the elimination of these claims before SolarWinds expended time and resources addressing them in its summary judgment motion.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-18

8 Cal.App.3d 216
Court of Appeal, Second
District, Division 4, California.

Alvin J. McCOWN, Plaintiff and Appellant,
v.
James R. SPENCER, Jr., et al.,
Defendants and Respondents.

Civ. 34311.
|
May 27, 1970.
|
Rehearing Denied June 17, 1970.
|
Hearing Denied July 22, 1970.

Synopsis

Action by intended buyer of realty against vendors for damages caused by vendor's alleged breach of escrow agreement. The Superior Court of Los Angeles County, Bayard Rhone, J., granted judgment for defendant notwithstanding the verdict and, alternatively, ordered new trial and plaintiff appealed. The Court of Appeal, Dunn, J., held that under escrow agreement, which provided that before specified date buyer or his nominee would deliver specified sum of cash and seller would deliver deed, that time was of the essence and that if conditions were not complied with by specified date party who had complied could, in writing, demand return of performance and that if no such demand were made escrow was to be closed as soon as conditions were complied with, either party could satisfy his obligations after specified date and require escrow to close, in absence of written demand by other for return of his deposit, and that vendors were estopped from asserting nominee's failure to timely perform where nominee replied on vendor's statements on specified date that he need not worry, that escrow would close and that he would sign amendment on approval of attorney and nominee was never informed that attorney had disapproved papers and did not learn of purported termination of escrow until property had been sold to another.

Judgment and order reversed.

Procedural Posture(s): On Appeal.

Attorneys and Law Firms

****215** ***219** Culliton & Hunter, and Daniel J. Culliton, Los Angeles, for plaintiff and appellant.

Boyle, Atwill & Stearns, and James B. Boyle, Pasadena, for defendants and respondents.

Opinion

DUNN, Associate Justice.

This is an action brought by the intended buyer of real property against the sellers for damages caused by the sellers' alleged breach of their escrow agreement. The case went to trial on the basis of the first and fifth causes of action pleaded in a second amended complaint. The first cause of action was for breach of contract. The fifth cause of action ***220** purported to sound in fraud but merely alleged statements made by the sellers, after a closing date specified in the escrow agreement, upon which statements plaintiff relied for an extension of the time for performance. Accordingly, the trial court treated it as pleading an excuse, by way of estoppel, for nonperformance by plaintiff.

A verdict was returned for plaintiff and, on defendants' motions, the court thereafter granted judgment for the defendants notwithstanding the verdict for plaintiff[1] and, alternately, ordered a new trial. (Code Civ.Proc. s 629.) Plaintiff appeals from the judgment and from the order granting the new trial. (Code Civ.Proc. s 904.1, formerly s 963.)

The evidence disclosed that on May 14, 1963 escrow instructions were prepared and signed by the parties at a branch of Union bank, as escrow holder. They provided for a total sale price of $160,000, of which $75,000 was to be in cash, an encumbrance of $75,000 was to be assumed by the buyer and $10,000 was to be evidenced by a promissory note bearing 6 percent interest. Outside of escrow, plaintiff had handed to defendants a check for $5,000, apparently as earnest money, to be deposited by defendants in the escrow and credited against the cash required of plaintiff.

Pertinent parts of the escrow instructions read:
'Prior to August 14, 1963 Buyer will hand or cause to be handed to you, $75,000, $5,000 of which is deposited herewith by Seller. Seller will hand you a deed * * * to enable you to comply with these instructions, all of which funds and documents you are instructed to use or deliver at any time

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

if prior to said date, As qualified by the provisions set forth in paragraph 5 (emphasis added) * * * all conditions of this escrow have been complied with

......

'......
'The unsecured promissory note shall be drawn on form to be approved by the principals hereto, in the principal amount of $10,000.00, executed by Alvin J. McCown, a married man, or nominee, in favor of James R. Spencer, Jr. and Kathryn Spencer, husband and wife, as joint tenants * * * with interest at six (6) % Per annum * * *. Principal payable on or before thirty (30) days from date of close of escrow.

'......
'5. If any of the conditions of this escrow are not complied with prior to the date specified on the first line on page one of these instructions any party who **216 has fully complied with his instructions may, in writing, subsequent *221 to that date * * * demand return of his money, documents and/or property, upon receipt of which demand * * * you shall withhold action except to mail copies of such demand to all other parties * * *. If no such demand is made you are to close the escrow as soon as the conditions (except as to time) have been complied with.

'* * * * * *

'8. THESE AND ALL ADDITIONAL OR AMENDED INSTRUCTIONS SHALL BE SUBJECT TO THE FOLLOWING:

'* * * * * *

'(g) Time is of the essence of these and all additional or changed instructions.'

A brief review of the evidence is required. In considering appellant's appeal from the judgment notwithstanding the verdict, the evidence must be considered in the light favoring appellant, all inferences therefrom being drawn in appellant's favor. Hergenrether v. East, 61 Cal.2d 440, 442, 39 Cal.Rptr. 4, 393 P.2d 164 (1964); Bufano v. City and County of San Francisco, 233 Cal.App.2d 61, 68, 43 Cal.Rptr. 223 (1965). This is contrary to the usual rule on appeal whereby all inferences are drawn in favor of sustaining the judgment and therefore in favor of a respondent.

The evidence discloses that appellant and the respondents had been acquainted for several years. Respondent, Dr. James Spencer, Jr., informed appellant that he had received an offer of $150,000 for his property. Appellant offered to buy it for $160,000 and the escrow ensued. By an oral side-agreement, with which we are not here concerned, respondents retained an option to maintain a one-sixteenth interest in the property, representing the proportion that the $10,000 (to be evidenced by the promissory note) bore to the total purchase price. Because of this interest, respondents joined in appellant's successful efforts to have the property rezoned so that it might be improved by the construction of a convalescent hospital. After the rezoning, they tried to obtain $200,000 as a price for the property whereupon, being unsuccessful, appellant suggested recontacting respondents' original offeror, Mr. Milligan who, on learning of the rezoning, offered to purchase the property for $180,000. Appellant then named Milligan as his nominee.

A modification of the escrow instructions, dated June 24, 1963, was signed by both sides and by Milligan, calling for a payment by Milligan of $25,000 to appellant, $5,000 of which is deposited herewith,' following which title to the property was to be vested in Milligan (or his nominee) contingent upon approval of a tract subdivision map by responsible authorities. *222 The modification provided: 'Upon receipt in escrow of written waiver from E. J. Milligan of the aforementioned contingency, you are instructed to accept all further instructions in this escrow from said nominee, and all funds deposited by me herein are to be used for the credit of and upon instructions of said vestee.'

Thereafter several discussions were had with Milligan, or his representative, who desired to extend the term of the escrow; but on June 26th and again on July 11th, 1963, respondents sent letters to the escrow holder, to appellant and to Milligan advising of respondents' intention to abide strictly by the time provisions of the escrow and stating no time extension had been, or would be, granted.

Before August 13, 1963, respondents deposited in escrow an executed deed granting title in the property, and also deposited a form of promissory note acceptable to them. Neither on nor before August 13th did appellant perform under the escrow and on August 23, 1963 respondents sold the property for $170,000 to a savings and loan association with whom

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Milligan had arranged to 'warehouse' it, I.e.: to purchase it, giving him an option to repurchase ****217** it at a later date. Appellant's lawsuit followed soon thereafter. A number of points are raised, requiring separate discussion.

I. Did Respondents' Sale Of The Property Constitute A Breach Of The Escrow Contract?

As noted, sellers and buyer agreed that, before August 14, 1963, each would deliver a deed, or cash and a note, respectively, to the escrow holder, further agreeing that 'time is of the essence.' Paragraph 5 of the instructions went on to provide that if a condition of the escrow was not met before August 14th, then any party who had fully complied could, in writing, After that date demand the return of whatever he had deposited with the escrow holder; and, 'If no such demand is made you are to close the escrow as soon as the conditions (except as to time) have been complied with.'

Appellant contends, and respondents dispute, that paragraph 5 does away with 'prior to August 14, 1963' as the closing date of the escrow. This means that, though respondents performed, appellant nevertheless could satisfy his escrow obligations after August 13th and require the escrow to close unless respondents, after August 13th but before appellant performed, made a written demand for return of the papers they deposited. We agree this is the correct interpretation. (See: Weisberg v. Ashcraft, 223 Cal.App.2d 793, 36 Cal.Rptr. 188 (1963).) Since time was of the essence, strict compliance with the date of performance was required, if ***223** demanded after the date specified, and performance within a 'reasonable' time after demand would be impermissible. Accordingly, if the buyer had not performed by the end of August 13th, then on August 14th the sellers could have given a written demand for return of the deed they had deposited. But the sellers gave no such demand until August 23rd, when a demand letter was addressed to appellant and the bank. Since appellant had not fully performed by that date, the sale of the property by respondents to a third party on August 23rd would not constitute a breach of the contract, absent other considerations.

This leads us to the next question, namely, whether the sellers were estopped to terminate the escrow by their letter dated August 23rd. If they were, their sale of the property that date constituted a breach of the agreement.

II. Were Respondents Estopped From Terminating The Escrow and Selling The Property To A Third Party?

The trial court instructed the jury on the nature of an estoppel in the terms of Code Civ.Proc. s 1962, subd. 3 (now contained in Evid. Code, s 623) and submitted to the jury a number of special verdicts. (Code Civ.Proc. s 625.) One of these inquired: 'Do you find that defendants by their conduct or action are estopped to claim that plaintiff or his nominee did not perform the contract in time?' to which the jury responded 'Yes.' The special verdict went on to inquire, 'If yes, what action or conduct of defendants constituted such estoppel?' The jury found that: 'The defendant gave no indication that anything was wrong with the escrow; however, he refused to sign papers before consulting with his lawyer.'

After the hearing on respondents' motion for judgment n.o.v. the court made a minute order of its ruling. In it was stated, among other things: 'There was no evidence of any fraud or anything whatever that might constitute an estoppel whereby the plaintiff or his nominee was justified or led to believe that the time was extended. The action of the defendant which the jury characterized as estoppel occurred after the time had already run out.' (Emphasis added.) We consider whether there was any evidence of estoppel. If there was, then the granting of the judgment n.o.v. on this ground was error.

It is apparent from the quotation of the minutes that the trial judge misconstrued the contract, concluding the agreement ****218** terminated by its own terms on August 14th and that respondents' conduct thereafter could not work an extension of the time for performance. As pointed out, we hold otherwise.

***224** The evidence disclosed that at noontime on August 14, 1963, Dr. Spencer, one of the two respondents, went to the bank branch holding the escrow. A Mr. Allen was there, representing the nominee, Mr. Milligan. Allen requested that respondents sign a document '* * * which stated that the total consideration in this escrow was $180,000 * * *.' Dr. Spencer testified this was the first time he had heard such a figure and, as a result, he refused to sign the document, returning to his office. Later that afternoon, appellant and his attorney went to the office of respondent Dr. Spencer. They found Milligan already there. He had procured some papers from the escrow clerk which he desired Spencer to sign.

Appellant's attorney, as a witness for appellant, testified: 'He (Dr. Spencer) said he was sure that everything was in proper order, that he didn't think there were any problems and everything was sailing along all right, that he just wanted to talk to his lawyer before he signed these papers.' Spencer told them his own attorney was out of town but he intended to see

him the next day. Dr. Spencer never signed the documents but on August 15th his wife did, so that if the attorney approved them when he returned, only the signature of her husband would be needed.

Between August 15th and 19th appellant telephoned respondents several times. On two of these occasions Dr. Spencer told him that he believed everything was in order, saying 'that the escrow would close and not to worry about it.' Despite this reassurance, appellant concluded that closure of the escrow was being held up because his nominee, Milligan, was not acceptable to respondents. For that reason he secured a cashiers check for $72,000 and on August 21st took it to the escrow, instructing the bank by letter to hold it until respondents deposited a grant deed in escrow (he apparently was unaware a grant deed already was deposited) and complied with the terms of the original escrow instructions. With the $5,000 previously paid into escrow, a total of $77,000 was thus made available.

Subdivision 3 of former Code of Civ.Proc. s 1962 reads: 'Whenever a party has, by his own declaration, act, or omission, intentionally and deliberately led another to believe a particular thing true, and to act upon such belief, he cannot, in any litigation arising out of such declaration, act, or omission, be permitted to falsify it.' This states a rule of estoppel. The evidence recited would support a finding that respondents were estopped from terminating the escrow on the date and in the manner which they attempted. Appellant relied upon Spencer's statements to him that he need not worry, that the escrow would close and he would sign the amendments on the return of, and approval by, his attorney. Appellant's failure completely to perform was thus excusable and respondents were estopped to contend otherwise. Appellant was never informed that the ***225** attorney disapproved of these papers nor did he learn of respondents' attempted termination of the escrow until he received respondents' letter dated August 23rd. But before receiving it, respondents, by their absolute sale of the property on August 23rd, had placed it beyond their own ability to perform and had thus breached the contract.

III. Did Appellant Assign His Rights As Buyer Under The Escrow Agreement, Resulting In Loss Of Standing To Sue?

Respondents urged that appellant did more than designate Milligan as his nominee; that, in fact, he assigned all of his rights to Milligan and as a result had no standing in court. This issue was presented to the jury by instructions, the court also submitting a special verdict which read: 'Did plaintiff assign his rights as purchaser under the escrow agreement with ****219** James R. Spencer, Jr. and Kathryn Spencer to E. J. Milligan?' The jury responded, 'No'.

Despite this verdict the court, in ruling on the motion for judgment n.o.v., made a finding in its minute order as follows: 'From a careful review of all the evidence, the Court concludes that Milligan was not a mere nominee, but he had 'bought the deal' and was in legal effect an assignee. Therefore, on the two grounds: i.e. (1) (that plaintiff and nominee did not perform in time) and (2) the plaintiff had assigned his contract to purchase to Milligan, the motion for judgment notwithstanding the verdict be and is hereby granted.'

An assignor may not maintain an action upon a claim after making an absolute assignment of it to another; his right to demand performance is extinguished, the assignee acquiring such right. (5 Cal.Jur.2d Rev. 478, 'Assignments' s 71; Vol. I, Restatement of the Law of Contracts 180, s 150.) To 'assign' ordinarily means to transfer title or ownership of property (Commercial Discount Co. v. Cowen, 18 Cal.2d 610, 614, 116 P.2d 599 (1941)), but an assignment, to be effective, must include manifestation to another person by the owner of his intention to transfer the right, without further action, to such other person or to a third person. (Cockerell v. Title Ins. & Trust Co., 42 Cal.2d 284, 291, 267 P.2d 16 (1954).) It is the substance and not the form of a transaction which determines whether an assignment was intended. (Bergin v. van der Steen, 107 Cal.App.2d 8, 16, 236 P.2d 613 (1951); Anglo California Nat. Bank, etc. v. Kidd, 58 Cal.App.2d 651, 655—656, 137 P.2d 460 (1943).) If from the entire transaction and the conduct of the parties it clearly appears that the intent of the parties was to pass title to the chose in action, then an assignment will be held to have taken place. Goldman v. Murray, 164 Cal. 419, 422, 129 P. 462 (1912); Norton v. Whitehead, 84 Cal. 263, 268, 24 P. 154 (1890); California Pac. Title Co., etc. v. Moore, 229 Cal.App.2d 114, 117, 40 Cal.Rptr. 61 (1964).

***226** From the foregoing it will be evident that 'intent' is of major significance. Appellant testified that after August 14, 1963 he told respondents' attorney, 'My position is that I am entitled to buy this property.' He called respondents on August 15, 16, 17, 18 and 19, successfully reaching Dr. Spencer twice, to discuss the close of escrow; on August 21st he deposited a check for $72,000 and advised the escrow holder to close it on performance by the sellers. This evidence, and inferences reasonably deducible from it, tends to negate any intent by appellant to assign his rights to Milligan.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

A basic requirement for sustaining a judgment n.o.v. is that no substantial conflict in the evidence exists. Robinson v. North American Life & Cas. Co., 215 Cal.App.2d 111, 118, 30 Cal.Rptr. 57 (1963). The judgment ordered for defendants, notwithstanding the verdict for plaintiff, must be reversed since the evidence was in conflict on the points foundational to the trial court's rulings: that appellant's rights were assigned to Milligan and that respondents were not estopped to contend appellant's failure fully to perform excused their termination of the escrow.

We now come to a discussion of the trial court's granting of respondents' motion for new trial.

IV. Did The Trial Court Properly Grant A New Trial To Respondents?

Respondents' 'Notice of Intention To Move For New Trial' stated three grounds as follows: (1) accident or surprise, (2) insufficiency of the evidence and (3) the verdict is against the law. The sole support for the motion was that it was 'on the minutes of the Court.' No affidavits were filed in support.

Code of Civil Procedure, section 657 requires that, if a motion for a new trial be granted, the court specify its grounds **220 and its reasons.[2] Purporting to comply with this section, the court's minute order stated:
'1. Insufficiency of the evidence. The evidence is insufficient in the same particulars as set out specifically above in granting the motion for judgment notwithstanding the verdict and they are incorporated herein at this place with the same changes and effect as if repeated at this point.
*227 '2. Accident or suprise, (sic) which ordinary prudence would not have guarded against. The Court submitted to the jury the issue of estoppel but this issue was not raised by the pleadings nor in the pretrial statement and the Court now concludes that it was in error to submit this issue to the jury.

'3. The verdict is against the law. As indicated above, the evidence is insufficient. The evidence showed without contradiction that the defendants fully performed their agreement and that neither the plaintiff nor his 'nominee' ever performed his or their agreement.

'The special verdict of the jury shows that the defendants did nothing by way of fraud or estoppel to prevent the plaintiff ro his nominee from closing the contract. Hence the general verdict which is contrary to the special verdict must be set aside.'

Insufficiency of the evidence. First to be considered is the adequacy of the trial court's statement of insufficiency. The Ground is fully stated; we look to see if the Reason behind it is adequately supporting. (Mercer v. Perez, 68 Cal.2d 104, 65 Cal.Rptr. 315, 436 P.2d 315 (1968).)

The court's 'reason' merely refers to the order granting the judgment n.o.v. The latter order stated only that: 'There was no evidence of any fraud or anything whatever that might constitute an estoppel * * *. The action of the defendant which the jury characterized as estoppel occurred after the time had already run out.' (Emphasis added.) That minute order also concluded that Milligan was an assignee as a matter of law. (See: fn. 1.) As we have noted, the trial court's legal conclusions were erroneous on both issues. It is apparent the court granted a new trial on this ground because it believed there was a total lack of any material evidence to support the verdict, rather than because the court, after weighing it, believed the evidence failed to proponderate and the jury should have reached a different verdict.
In Mercer v. Perez, Supra, 68 Cal.2d pp. 116—117, 65 Cal.Rptr. p. 323, 436 P.2d p. 323, the following is said: 'Thus in Greenwood v. Boque, 53 Wash.2d 795, 337 P.2d 708, * * * (a Washington case) the only 'reason' stated by the trial court for granting the plaintiffs' motion for new trial after a verdict for the defendants in an automobile accident case was that 'there was no evidence to justify a verdict except on behalf of the plaintiffs' * * *. The Supreme Court of Washington observed that the trial court's statement 'is of no assistance to an appellate court. It amounts to no more than an invitation to search the record, * * *'' In the case at bench, the trial court's order states in part: 'There was no evidence of any fraud or anything whatever that might constitute an estoppel.' Such a specification is inadequate **221 and is of little assistance to us and, as we have noted, the conclusion expressed is incorrect. We do not read a later case, *228 Kincaid v. Sears, Roebuck & Co., 259 Cal.App.2d 733, at page 738, 66 Cal.Rptr. 915 (1968), as placing any different interpretation upon the intent of Mercer. Accordingly, we hold the granting of a new trial on the ground stated is insufficiently supported.

Accident or surprise which ordinary prudence could not have guarded against. One ground stated for granting the new trial was 'accident or surprise.' The court's stated reason was: 'The Court submitted to the jury the issue of estoppel but this issue

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

was not raised by the pleadings nor in the pretrial statement and the Court now concludes it was in error to submit this issue to the jury.' The foregoing is not a recital of 'accident or surprise', as that term is used in Code Civ.Proc. s 657. Rather, it states the court's conclusion that it instructed the jury on an issue not raised by the pleadings and therefore committed an error at law.

The terms 'accident' and 'surprise', as used in Code Civ.Proc. s 657, are given substantially the same meaning. Kauffman v. De Mutiis, 31 Cal.2d 429, 432, 189 P.2d 271 (1948); South Santa Clara etc. Dist. v. Johnson, 231 Cal.App.2d 388, 406, 41 Cal.Rptr. 846 (1964). Section 658 of the Code of Civil Procedure specifies that an application for new trial made on such ground '* * * must be made upon affidavits.' No affidavits were filed by respondents in support of their motion for new trial. Under some circumstances, the absence of a supporting affidavit is noncalamitous and other support appearing in the record may be accepted (see: Webber v. Webber, 33 Cal.2d 153, 163—164, 199 P.2d 934 (1948)), but such circumstances are not here present.

During argument of respondents' motion for directed verdict, the court stated, for the first time of record, that it interpreted appellant's fifth cause of action as spelling out estoppel. Counsel for respondents did not then claim surprise and move for a continuance, ask to reopen the case and produce further evidence, or move for a mistrial. The rule has been stated: '* * * where a situation arises which might constitute legal surprise, counsel cannot speculate on a favorable verdict. He must act at the earliest possible moment for the 'right to a new trial on the ground of surprise is waived if, when the surprise is discovered, it is not made known to the court, and no motion is made for a mistrial or continuance of the cause.'' Kauffman v. De Mutiis, Supra, 31 Cal.2d at 432, 189 P.2d at 273. (Also see: Baker v. Berreman, 61 Cal.App.2d 235, 241, 142 P.2d 448 (1943).) There here being no supporting affidavit and no timely claim of surprise, the granting of a new trial on this ground was error.

The verdict is against the law. As its third and last ground for ***229** granting a new trial the court stated 'the verdict is against the law.' [3] The minute order shows that the court granted a new trial on this ground on the premise that the evidence was totally insufficient. Such a reason, if supported by the record, is a proper one. Thus: '(6) A decision can be said to be 'against law' only: * * * (3) where the evidence is insufficient in law and without conflict in any material point. * * * (8) '(T)he words 'against law' do not import a situation in which the court weighs conflicting evidence and merely finds a balance against the judgment.'' Kralyevich v. Magrini, 172 Cal.App.2d 784, 789, 342 P.2d 903, 906, (1959). (And see: Thompson v. Guyer-Hays, 207 Cal.App.2d 366, 375, 24 Cal.Rptr. 461 (1962); Opp v. Sykes, 194 Cal.App.2d 208, 211, 15 Cal.Rptr. 1 (1961).)

****222** Counsel for respondents entertained an erroneous concept of the application of estoppel in this case. During the hearing of his motion for judgment n.o.v. and for a new trial, he argued: '* * * to invoke the doctrine of estoppel evidence had to be produced that the defendants did something Prior to August the 14th * * *.'; '* * * there is no evidence of any kind produced which would lead the plaintiff to believe that he didn't have to perform Prior to August the 14th.'; and 'the estoppel issue goes to the point as to whether or not we did anything Before August the 14th * * *.' (Emphasis supplied in each instance.)

The trial court accepted this concept. Had the court been correct in deciding that only conduct before August 14th could create an estoppel, then the granting of a new trial because the verdict was 'against the law' would have been proper; there was no evidence of such conduct before August 14th. But, as we have noted, an estoppel could be based upon acts occurring after August 14th and evidence of such acts was received.

The court's minute order also stated: 'The special verdict of the jury shows that the defendants did nothing by way of fraud or estoppel to prevent the plaintiff or his nominee from closing the contract. Hence the general verdict which is contrary to the special verdict must be set aside'. Actually, in its special verdict the jury Did find that respondents were estopped to claim appellant failed to perform in time. That being so, the general verdict conformed precisely with the special verdict.

The jury did Not find the conduct occurred After August 14th, but this is implicit in its finding that: 'The defendant gave no indication that anything was wrong with the escrow; however, he refused to sign papers before consulting with his lawyer.' Without dispute, the refusal to sign papers ***230** occurred after August 14th. The trial judge believed any conduct after that date was immaterial to establish an estoppel. There being no evidence of estoppel before that date, he concluded the general verdict was contradicted by the special verdict. We hold just the opposite.

We have reviewed the entire record with an eye to affirming the order granting a new trial on the two grounds last

discussed, as directed by the language of section 657.[4] However, we have been unable to find any substantial error which would support either ground. Accordingly, the order granting a new trial on any of the three grounds specified cannot be sustained.

Judgment for defendants notwithstanding the verdict for plaintiff is reversed; the order granting defendants a new trial likewise is reversed.

FILES, P.J., and JEFFERSON, J., concur.

All Citations

8 Cal.App.3d 216, 87 Cal.Rptr. 213

Footnotes

1 The court specified two grounds for ordering judgment n.o.v.: '(1) that there was not performance by the plaintiff or his 'nominee' within the time specified; and (2) the plaintiff had assigned his contract to purchase to Milligan * * *.'

2 Code Civ.Proc. s 657 states in part: 'When a new trial is granted, on all or part of the issues, the court shall specify the ground or grounds upon which it is granted and the court's reason or reasons for granting the new trial upon each ground stated. * * * On appeal from an order granting a new trial * * * (a) the order shall not be affirmed upon the ground of insufficiency of the evidence to justify the verdict * * * unless such ground is stated in the order granting the motion and (b) on appeal from an order granting a new trial upon the ground of insufficiency of the evidence * * * it shall be conclusively presumed that said order as to such ground was made only for the reasons specified in said order * * * and such order shall be reversed as to such ground only if there is no substantial basis in the record for any of such reasons.'

3 Such ground is to be distinguished from the confusingly similar seventh ground furnished by Code Civ.Proc. s 657, subd. 7, namely, 'error in law'. (See: 3 Witkin Cal.Procedure, 1954 ed., pp. 2062—2063, 'Attack On Judgment In Trial Court' s 17.)

4 This reads: 'On appeal from an order granting a new trial the order shall be affirmed if it should have been granted upon any ground stated in the motion, whether or not specified in the order or specification of reasons, except * * * (b) on appeal from an order granting a new trial upon the ground of the insufficiency of the evidence * * *.'

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-19

35 Cal.2d 109
Supreme Court of California.

MERCHANTS SERVICE CO.
v.
SMALL CLAIMS COURT OF CITY & COUNTY OF SAN FRANCISCO et al.

S. F. 18069.
|
April 12, 1950.

Synopsis
The Merchants Service Company, a corporation, petitioned for a writ of mandate to compel Ivan L. Slavich, Clerk of the Small Claims Court of the City and County of San Francisco, to accept a claim for filing therein. From a judgment of the Superior Court, San Francisco County, Edward P. Murphy, J., granting a peremptory writ, defendants appealed. The Supreme Court, Spence, J., held that the claim was based on an assignment to petitioner and hence not cognizable in the small claims court.

Judgment reversed.

Prior opinion, Cal.App., 210 P.2d 543.

Attorneys and Law Firms

****846** ***110** Fred N. Howser, Attorney General, Clarence A. Linn and B. Abbott Goldberg, Deputy Attorneys General, John J. O'Toole and Dion R. Holm, City Attorneys, and C. Wesley Davis, Deputy City Attorney, San Francisco, for appellants.

John H. Brill, San Francisco, for respondent.

Opinion

SPENCE, Justice.

Plaintiff petitioned the superior court for a writ of mandate to compel the clerk of the Small Claims Court in San Francisco to accept for filing therein a claims for $14.13. Defendants interposed a demurrer to the petition, thereby submitting the matter 'on the papers of the applicant.' Code Civ.Proc., s 1094; Scannell v. Wolff, 86 Cal.App.2d 489, 491-492, 195 P.2d 536. The demurrer was overruled and the court ordered a peremptory writ to issue. From the judgment accordingly entered, defendants appeal.

Plaintiff's claim was rejected by the clerk of the ground that it appeared to be based on an assignment. Section 117f of the Code of Civil Procedure provides that 'No claim shall be filed or prosecuted in such small claims court by the assignee of such claim.' An analysis of the two papers constituting plaintiff's claim attached to the petition for a writ of mandate and designated Exhibits A and B sustains the propriety of the clerk's action.

Exhibit A is on the form provided by the clerk for the use of claimants, consisting of a completed questionnaire and an affidavit and order as prescribed by section 117b of the Code of Civil Procedure. It thereby appears that Mrs. Wilma Bradford, defendant, is indebted to plaintiff, Merchants Service Company, in the sum of $14.13 for money due under a written contract; that a demand was made and refused and nothing paid; and the residence of defendant and the place of business of plaintiff are given.

Exhibit B is the 'written contract' to which reference is made in Exhibit A. It consists of a printed form containing questions calling for information respecting the ****847** financial responsibility and resources of a prospective customer. Below ***111** this form it appears that the subject of sale was a 'ladies ring' for the price of $12.50 plus 38 cents sales tax and 'Service and/or Excise Taxes' $1.25, total $14.13; and that the sale was on 'Budget Account Terms $1,00 each week Beginning January 17, 1948.' Printed on the reverse side is the purchaser's agreement, signed by Mrs. Bradford, acknowledging 'receipt * * * of (the) merchandise * * * described * * *, for which payment is to be made to the Merchants Service Company, * * * called Creditor, in the sum there specified on the terms set forth.' This agreement is reproduced in full below, omitting a form to be executed by co-signers or guarantors and which was not executed. [1]

Immediately following and as a part of the same printed document appears a formal statement signed by Sol Michaels, ***112** showing him to 'relinquish, disclaim, and quitclaim any right, title, or interest in and ****848** to the merchandise or demands there in described unto Merchants Service Company' and to 'guarantee' the validity of 'the above contract.' This agreement by Michaels is likewise reproduced in full below. [2]

***113** From these 'papers' it is apparent that Mrs. Bradford purchased a ring from the seller, Sol Michaels, and that she was obligated to make 'payment' therefor 'to the Merchants Service Company.' Such transaction, plaintiff maintains, evidences a contract of sale for its express benefit, Civ.Code, s 1559; Hartman Ranch Co. v. Associated Oil Co., 10 Cal.2d 232, 244, 73 P.2d 1163, an original obligation in its favor, J. F. Hall-Martin Co. v. Hughes, 18 Cal.App. 513, 516, 123 P. 617, which it, as the primary creditor of the purchaser, was trying to enforce directly in the court having jurisdiction of its claim as so limited in amount, Code Civ.Proc., s 117. But such argument gives effect only to part one of Exhibit B above quoted, the agreement signed by Mrs. Bradford and establishing a debtor-creditor relationship between her and plaintiff; and it disregards the purport of part two of Exhibit B above quoted, the relinquishment signed by Sol Michaels, the merchant, as a factor affecting the three-party undertaking and indicating the derivative basis of plaintiff's claim against the purchser. A consideration of the two parts of the agreement together compels the conclusion that plaintiff's status is that of an assignee rather than that of the ordinary third party beneficiary, and that its claim is therefore not cognizable in the small claims court. Schwartz, Inc., v. Burnett Pharmacy, 112 Cal.App.Supp. 781, 785, 295 P. 508.

The writing signed by Michaels shows on its face that he was the original claimant against the purchaser by reason of his sale and delivery of the ring to her. It was only by reason of his relinquishment of his right to make a demand upon her for the purchase price that plaintiff's corresponding right against her arose, and so plaintiff was substituted for the normal creditor, the seller, in the transaction. Thus the writing executed by Michaels speaks in the past tense of 'demands therein described' which are relinquished and quitclaimed, and it shows that the contract of sale had been consummated, for Michaels guaranteed that 'the above contract (part one of Exhibit B, supra), is a valid, bona fide and ****849** subsisting agreement' (emphasis added), and that the merchandise sold had been delivered. The 'demands therein described' constitute a chose in action, consisting of the right to receive from the buyer the deferred payments of the purchase price which became owing to the seller, Michaels, as soon as he delivered the ring. Such transfer of rights in connection ***114** with property ordinarily indicates an assignment, 4 Am.Jur. sec. 2, p. 229; In re Estate of Beffa, 54 Cal.App. 186, 189, 201 P. 616; see, also, Commercial Discount Co. v. Cowen, 18 Cal.2d 610, 614, 116 P.2d 599, and the studious avoidance of the word 'assign' in the language of the relinquishment cannot affect its proper classification as an assignment. Moreover, Michaels' guarantees as to (1) the validity of the 'subsisting' contract for payment of the purchase price and (2) the genuineness of 'all signatures appearing thereon' are warranties that are typical of those which ordinarily accompany an assignment. (See 4 Am.Jur. sec. 100, pp. 308-309.)

While the writing signed by the purchaser (part one of Exhibit B, supra) shows a debtor-creditor relationship existing between her and Merchants Service Company, the same relationship must first have existed between her and the seller Michaels, for otherwise Michaels had no 'demands' to relimquish. In short, the significant events in the three-party transaction clearly appear to have transpired in this sequence: (1) the purchaser's obligation to pay arose immediately upon delivery of the ring; (2) the ring had been delivered before Michaels signed the relinquishment; and (3) the debtor-creditor relationship between the purchaser and Merchants Service Company as evidenced in the writing over the buyer's signature (part one of Exhibit B, supra) came into being only because Michaels relinquished to the company the purchaser's obligation to pay him as seller of the ring. By signing the relinquishment, Michaels extinguished his right to sue for collection of the purchase price and this right was transferred to the company, so that it thereafter stood in the place of Michaels. While plaintiff urges that the purchaser's original promise of payment ran in its favor, creating a primary obligation which could not be affected by Michaels' undertaking, such argument necessarily involves treatment of the two parts of the agreement covering the sale of the ring (Exhibit B, supra) as separate writings, having no bearing one on the other. However, that view cannot prevail, for the 'papers' constituting the record here show this to be one entire transaction, and the three-party dealings evidenced thereby must be construed as a whole and given a normal interpretation consistent with their purport. Civ.Code, s 1641; 6 Cal.Jur. s 165, p. 258. As the two parts of this single transaction are so related and integrated one with the other, plaintiff's right to sue on the claim in question appears clearly to have accrued only as the result of Michaels' assignment thereof upon consummating ***115** the sale and delivery of the ring to the purchaser.

Section 117f of the Code of Civil Procedure, supra, does not confine its prohibition, in use of the small claims court, to assignees for collection or assignees for the purposes of suit. Rather it prohibits the filing of a claim by any and every 'assignee'; and as so used without limitation, the word suggests a broad meaning was intended to attach thereto and to include any one who stands in the place of the original creditor. So here, any realistic appraisal of the substance

of the three-party transaction, Civ.Code, s 3528, shows that Michaels by his 'relinquishment' thereby made to Merchants Service Company a present assignment of his claim against the purchaser arising out of his sale and delivery of the ring to her, a type of transaction coming within the express terms of section 117f of the Code of Civil Procedure; and the clerk of the small claims court was therefore justified in refusing to file plaintiff's claim.

The judgment is reversed.

GIBSON, C. J., and SHENK, EDMONDS, CARTER, TRAYNOR, and SCHAUER, JJ., concur.

All Citations

35 Cal.2d 109, 216 P.2d 846

Footnotes

1 'The undersigned hereby acknowledges receipt from the concern named of merchandise and/or services described on reverse side, for which payment is to be made to the Merchants Service Company, hereinafter called Creditor, in the sum there specified on the terms set forth. Receipt of said merchandise in good order, satisfactory fit and construction in every detail is hereby acknowledged by the undersigned.

'If any representation herein made by the Undersigned is false or if the Undersigned defaults in any payment or violates any of the conditions of this agreement, the unpaid balance hereunder shall immediately become due at the option of the creditor.

'Should Creditor institute action to recover the purchase price or any part of it, the title and right of possession of any merchandise referred to shall remain in the Creditor until paid for, with the right of repossession before or after judgment rendered, until satisfaction of such judgment. The Undersigned agrees to return the merchandise purchased and referred to on demand should the Undersigned be in default in any payments or have made any material misstatement in connection herewith, and agrees to pay the Creditor a reasonable amount for any actual damage suffered thereby. Should this contract be placed in the hands of an attorney or collection agency for collection or breach of contract, the Undersigned agrees to pay all actual court costs, collection expense including collection agency fee and attorney fees incurred, with or without suit.

'The Undersigned agrees to make all payments under this contract at the office of the Merchants Service Company. In the event of default by Undersigned in any of the obligations herein, Creditor may, without notice of demand, enter any premises where said merchandise may be found and take possession thereof and at its option sell said merchandise at public or private sale, and the proceeds thereof, less the expense of repossessing and selling said merchandise, shall be credited upon the amount unpaid hereunder, or without such sale there may be credited upon the amount unpaid the fair market value of said merchandise at the time of such repossession, and in either event, in consideration of the use and depreciation of said merchandise, Undersigned agrees to pay forthwith any remaining unpaid balance hereunder. In no event shall Creditor be entitled to receive in excess of the original purchase price unless Creditor elects to reclaim the merchandise, in which event Undersigned shall be released from all further liability.

'The Undersigned hereby agrees that the period of the running of the statute of limiations on the within account will be extended ten (10) years from date hereof.

'The undersigned agrees to insure said chattels against loss by fire, theft, damage and mysterious disappearance in favor of the Creditor or its assignee and furnish Creditor or its assignee with a copy of the insurance policy. Should the Undersigned fail to furnish the Creditor of its assignee with a copy of its insurance policy, the Creditor or its assignee may insure the above described chattels at the expense of the Undersigned and the Undersigned agrees to pay the premium on said policy within thirty (30) days after demand thereof.

'The Undersigned hereby waives all right for a change of venue and expressly consents to any suit for collection being filed in San Francisco. Time is of the essence of this agreement.

'This contract may be assigned or sold and all rights and conditions of the Creditor or assignor shall inure to the benefit of the purchaser or assignee.
Signed: Mrs. Wilma Bradford
Dated Jan. 10, 1948
(Buyer)'

2 'We hereby relinquish, disclaim, and quitclaim any right, title, or interest in and to the merchandise or demands therein described unto Merchants Service Company. We guarantee that the above contract is a valid, bona fide and subsisting agreement; that all laws have been complied with; and that all signatures appearing thereon are gunuine and are of the persons of whom they purport to be and that such persons are competent to make this contract. It is specifically represented that no part of this contract arose out of any delinquent account previously on our books; that all merchandise as set forth thereon as having been sold has been delivered to the Debtor; and/or that all services agreed to be performed have been rendered and completed to the personal satisfaction of the Debtor, after which I/we shall not be responsible for the payments on this contract. The debtor is not obligated to us or our assignee on prior purchases. Additional credit will not be granted to any Debtor until the balance on a prior contract has been paid in full or unless such additional credit has previously been approved by Merchants Service Company. Should we violate this provision Merchants Service Company may elect to require us and we hereby agree to pay to Merchants Service Company any balance due it from the Debtor on a prior contract or Merchants Service Company may elect to collect and retain the entire balance due from the Debtor including the amount due from the Debtor of such unauthorized sale. We agree to act as agent to collect the money due on this contract until notified to the contrary by Merchants Service Company, and we shall immediately remit same to Merchants Service Company, and prior to such remittance shall hold such collection and/or deposit same in a place of or account separate and distinct from collections and/or funds of our own, and such receipt and/or collections shall be and remain the property of said Merchants Service Company. Merchants Service Company by, or through its agent, shall have a right to examine my and/or our books of account at any reasonable time.
(Firm Name) Sol Michaels
915 Pierce St.'

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-20

Distinguished by Camacho Family Partnership v. Patricial I. Romero, Inc., D.Guam, October 17, 2016

318 F.3d 924
United States Court of Appeals,
Ninth Circuit.

Sheldon R. MILENBACH; Phyllis Milenbach, et al.; Los Angeles Raiders, a California Limited Partnership, Allen Davis, Tax Matters Partner; Los Angeles Raiders, a California Limited Partnership, A.D. Football, Inc., Tax Matters Partner, Petitioners–Appellants,
v.
COMMISSIONER OF INTERNAL REVENUE, Respondent–Appellee.

No. 97–70123.
|
Argued and Submitted Oct. 9, 2002.
|
Filed Feb. 6, 2003.

Synopsis
Order was entered by United States Tax Court, Cohen, J., 1994 WL 891961, upholding federal income tax deficiencies assessed against owners of professional football team, and owners appealed. The Court of Appeals, Tashima, Circuit Judge, held that: (1) discretion accorded to owners of professional football team as to timing of construction of luxury suites from whose revenues a $4 million "loan" from municipality was to be repaid did not render illusory their obligation to repay this alleged "loan," so that, this $4 million advance did not constitute taxable income to owners in year that it was received; (2) while settlement between owners and municipality, as to damages claims arising out of municipality's unsuccessful eminent domain action, recited that it was to compensate owners for loss of value of franchise rather than for any lost income, Tax Court was not bound by this characterization and did not clearly err in finding that settlement compensated owners, at least in part, for lost profits; and (3) Tax Court's determination, that obligation on part of owners to repay city's $10 million advance on the $115 million of financing that it agreed to provide for construction of football stadium was forgiven, pursuant to terms of memorandum of understanding between parties, when California legislature enacted law that prevented city from using general obligation bonds as funding mechanism, was clearly erroneous.

Affirmed in part, reversed in part and remanded.

Procedural Posture(s): On Appeal.

Attorneys and Law Firms

***928** Jerome B. Falk, Jr., Stuart S. Lipton, Douglas A. Winthrop, Clara J. Shin, Howard, Rice, Nemerovski, Canady, Falk & Rabkin, A Professional Corporation, San Francisco, CA, for the petitioners-appellants.

Kenneth W. Rosenberg, Department of Justice, Tax Division, Washington, D.C., for the respondent-appellee.

Appeal from the United States Tax Court. T.C. Nos. 1571–93, 1572–93, 1573–93, 1574–93, 12129–94 and 28514–92.

Before: TASHIMA, THOMAS, and PAEZ, Circuit Judges.

Opinion

TASHIMA, Circuit Judge.

The Commissioner of Internal Revenue determined deficiencies in Petitioners–Appellants Sheldon and Phyllis Milenbach's federal income taxes for the years 1980 through 1982. The Commissioner also issued notices of Final Partnership Administrative Adjustments determining adjustments to the income of the Los Angeles Raiders, a California Limited Partnership, for the years 1983 through 1989. Petitioners (collectively the "Raiders") appeal from the Tax Court decisions affirming the contested determinations. *See Milenbach v. Comm'r,* 106 T.C. 184, 1994 WL 891961 (1996).

The Raiders own a professional football team and belong to the National Football League (the "NFL"). Prior to 1980, the Raiders played their home games at the Oakland–Alameda County Coliseum (the "Oakland Coliseum"). The Raiders' lease of the Oakland Coliseum expired at the end of the 1979 NFL season. During 1979, the Raiders negotiated with the Los Angeles Memorial Coliseum Commission (the "LAMCC") to allow the Raiders to begin playing their home games in the Los Angeles Memorial Coliseum (the "LA Coliseum"). In 1980, the Raiders announced that they intended to leave Oakland and play their home games at the LA Coliseum. This announcement set in motion a series of events that resulted in enormous controversy for the

team, including several lawsuits, and a number of business transactions whose tax consequences are at issue here. Specifically, the Raiders challenge the Tax Court's decisions regarding three discrete transactions related to the Raiders' relocation of their team. We analyze each in turn.

I. THE LAMCC PAYMENTS

A. Background

On March 1, 1980, the Raiders entered into a Memorandum of Agreement ("MOA") with the LAMCC providing for the relocation of the Raiders to Los Angeles beginning with the 1980 NFL season. The parties never implemented this MOA, however, because the City of Oakland ("Oakland") filed an action in eminent domain against the Raiders, seeking to condemn for public use the Raiders' NFL franchise, business, and physical assets. Both Oakland and the NFL obtained preliminary injunctions preventing the Raiders from relocating.

***929** As a result, the Raiders played their 1980 and 1981 home games at the Oakland Coliseum. When the NFL injunction was lifted in 1982, the Raiders resumed negotiations with the LAMCC. On July 5, 1982, these negotiations produced a new Memorandum of Agreement (the "1982 MOA"). Pursuant to the 1982 MOA, in 1984, the parties executed a promissory note (the "Note") and a lease agreement for the LA Coliseum (the "Lease").

The 1982 MOA, the Note, and the Lease (collectively, the "LAMCC Agreement") provided that the LAMCC would loan the Raiders $6.7 million at 10 percent interest. The Raiders were to repay the loan from 12 percent of the net receipts from the operation of luxury suites to be constructed by the Raiders at the LA Coliseum. The repayment was to begin in the third year of suite rentals. The loan was secured by the to be-constructed suites, with no recourse to the Raiders. The loan consisted of a $4 million cash payment to the Raiders in 1984 and credits totaling $2.7 million against rent due from the Raiders for the years 1982 through 1986.

As to the construction of the suites, the 1982 MOA provided that the Raiders "shall construct" approximately 150 private suites. The MOA went on to state that the construction "shall commence as soon as practicable as determined by [the Raiders] in [their] reasonable discretion, having in mind pending and potential litigation involving the parties hereto, or either of them, financial considerations, and other considerations reasonably deemed important or significant to the [Raiders]." The Lease further provided that the Raiders "shall use [their] best efforts to begin and complete Suite construction as soon as possible." The LAMCC Agreement was the result of arm's-length bargaining between the Raiders and the LAMCC.

The Raiders began playing their home games at the LA Coliseum starting with the 1982 season. Plans to construct the suites prior to the 1984 Summer Olympics were abandoned after the Los Angeles Olympic Committee voiced concerns over the timing of the construction. The Raiders worked with architects and contractors on the planning of the suites throughout 1985 and 1986.

Actual construction began in early 1987, but was halted on February 18 of that year. On that date, the LAMCC demanded that suite construction stop because the Raiders had not obtained necessary performance bonds. The Raiders responded that they were willing and able to provide the required bonds, but stated that construction would cease because of the LAMCC's failure to make certain improvements to the LA Coliseum. Due to this dispute, construction never resumed and the suites were never completed.

The Raiders never made any payments on the LAMCC loan. In September 1987, the LAMCC filed a lawsuit claiming that the Raiders had breached the Lease by failing to construct the suites "as soon as practicable" and for failing to repay the $6.7 million loan. In January 1988, the Raiders answered the LAMCC's complaint, alleging that the LAMCC had breached a commitment to modernize and reconfigure the stadium. The lawsuit was settled on September 11, 1990.

In a Notice of Deficiency for 1982 and FPAAs for 1983 through 1986, the Commissioner disallowed the Raiders' rent deductions because the rent was not currently payable and was part of the loan from the LAMCC. In the alternative, if the rent deductions were allowed, the Commissioner determined that the amount of the rent credits were includable in gross income as advance payment of income. The Commissioner also determined that the $4 ***930** million advance paid in 1984 was includable in the Raiders' 1984 gross income.

The Tax Court held that the "loan" payments from the LAMCC were includable in the Raiders' income in the years in which they were received. *Milenbach,* 106 T.C. at 198. It held that the obligation to construct the suites was illusory and, therefore, the LAMCC payments did not qualify as loans

for tax purposes because the Raiders "controlled whether or not repayment of the $6.7 million would be triggered." *Id.* at 196.

B. Analysis

We review decisions of the Tax Court under the same standards as civil bench trials in the district court. *Custom Chrome, Inc. v. Comm'r,* 217 F.3d 1117, 1121(9th Cir.2000). Therefore, conclusions of law are reviewed de novo, and questions of fact are reviewed for clear error. *Id.* This court owes no special deference to the Tax Court's decisions on issues of state law. *Harbor Bancorp & Subsidiaries v. Comm'r,* 115 F.3d 722, 727 (9th Cir.1997). The interpretation and meaning of contract provisions are questions of law reviewed de novo. *Kassbaum v. Steppenwolf Prods., Inc.,* 236 F.3d 487, 490 (9th Cir.2000).

A loan is generally not taxable income because the receipt of the loan is offset by the obligation to repay the loan. *Comm'r v. Tufts,* 461 U.S. 300, 307, 103 S.Ct. 1826, 75 L.Ed.2d 863 (1983). For this rule to apply, however, the loan must be an "existing, unconditional, and legally enforceable obligation for the payment of a principal sum." *Noguchi v. Comm'r,* 992 F.2d 226, 227(9th Cir.1993); *see also Geftman v. Comm'r,* 154 F.3d 61, 68 (3d Cir.1998) (requiring "an unconditional obligation on the part of the transferee to repay the money, and an unconditional intention on the part of the transferor to secure repayment") (citation and internal quotation marks omitted).

Whether a transaction is a loan for federal income tax purposes is ultimately a question of federal law. *See Helvering v. Stuart,* 317 U.S. 154, 162, 63 S.Ct. 140, 87 L.Ed. 154 (1942) ("Once rights are obtained by local law, whatever they may be called, these rights are subject to the federal definition of taxability."). Initially, however, state law determines the rights and obligations of the parties to a transaction. *See id.* at 161–62, 63 S.Ct. 140. But once an obligation is created by local law, it is subject to the federal definition of taxability. *Id.* Here, the dispositive question is whether the LAMCC Agreement was sufficient, under California law, to subject the Raiders to a non-illusory and enforceable obligation to repay the LAMCC advances. If the Raiders were subject to an "existing, unconditional, and legally enforceable obligation" to repay the LAMCC advances, the advances are properly treated as loans for federal income tax purposes. *Noguchi,* 992 F.2d at 227.

Contrary to the Tax Court's conclusion, the Raiders' broad discretion in the timing of the construction of the suites did not make the contract illusory. Under California law, an obligation under a contract is not illusory if the obligated party's discretion must be exercised with reasonableness or good faith. *See Storek & Storek, Inc. v. Citicorp Real Estate, Inc.,* 100 Cal.App.4th 44, 122 Cal.Rptr.2d 267, 281 (2002) (holding that a promise to pay only if satisfied is not illusory if the ability to claim dissatisfaction is limited by the standard of reasonableness); *24 Hour Fitness, Inc. v. Superior Court,* 66 Cal.App.4th 1199, 78 Cal.Rptr.2d 533, 541 (1998) ("[W]here the contract specifies performance the fact that one party reserves the ***931** power to vary it is not fatal if the exercise of the power is subject to prescribed or implied limitations such as the duty to exercise it in good faith and in accordance with fair dealings.") (citation and internal quotation marks omitted); *Frankel v. Bd. of Dental Exam'rs,* 46 Cal.App.4th 534, 54 Cal.Rptr.2d 128, 136 (1996) (holding that a contract is not illusory when the power to withdraw from the contract must be exercised in good faith).

Here, the Raiders were required to exercise their discretion reasonably and nothing in the LAMCC Agreement indicates that construction of the suites was optional. Both the 1982 MOA and the Lease state that the suites "shall be" constructed and both require the Raiders to use their "reasonable" discretion in deciding the exact timing in the construction of the suites. The Lease also required the Raiders to use their "best efforts" both to construct the suites as soon as possible and to operate them in such a way as to maximize the profits to be derived from them. At no point were the Raiders free to ignore their obligation to construct the suites. They could only delay the construction for a reasonable time and were required to use their best efforts to complete the suites and begin repayment of the loan. These limitations on the Raiders' discretion were sufficient to create a non-illusory obligation both to construct the suites and to repay the loan that would have been enforceable under California law. The fact that the obligations were later extinguished by the settlement of the 1987 lawsuit does not indicate that the obligation was illusory at the time the contract was made. Accordingly, we conclude that the Tax Court erred in holding that the LAMCC Agreement was illusory.

Because the Raiders had a non-illusory, unconditional obligation to repay the LAMCC loan, the payments were properly treated as loans and were excludable from income in the year in which they were received. [1]

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

II. THE OAKLAND SETTLEMENT

A. Background

The eminent domain suit filed by Oakland in 1980 was ultimately decided in favor of the Raiders. After it was decided that Oakland could not lawfully seize the Raiders' franchise, the Raiders sought damages arising from Oakland's condemnation action by filing a Notice of Claim for Damages in that proceeding. The Raiders sought recovery under the California and United States Constitutions, the common law, and California Code of Civil Procedure § 1268.620. Section 1268.620 allows the recovery of "all damages proximately caused by" a failed eminent domain action. Cal.Civ.Proc.Code § 1268.620(b). The Raiders claimed that Oakland had denied the Raiders "the free and untrammeled possession and use of the team." The Raiders claimed that they suffered damages from Oakland's failed condemnation action in the following ways: (1) they were compelled to maintain a summer training camp in Santa Rosa, California; (2) they were compelled to lease the Oakland Coliseum; (3) they were prevented ***932** from constructing the luxury suites in the LA Coliseum, and were thereby deprived of income from the sale and rental of those suites; (4) they suffered reduced attendance for home games played in the LA Coliseum; (5) they were deprived of income from radio contracts; and (6) they were forced to pay extra expenses for the relocation of personnel.

Oakland objected to the Claim for Damages on procedural grounds. To avoid these procedural objections, the Raiders, at the suggestion of the Superior Court, filed a complaint of inverse condemnation against Oakland for damages arising out of the eminent domain action. The Raiders reiterated their Claim for Damages, and stated that they had suffered damages in excess of $26 million. The Superior Court consolidated the two actions.

During discovery in the consolidated actions, the Raiders proffered a study detailing approximately $25 million in damages they claimed had been caused by Oakland's eminent domain action. Over $18 million of the damages claimed were attributed to lost income from suite rentals. Three million dollars were attributed to lost income from a contract with the Los Angeles Olympic Committee for use of the luxury suites, which the Raiders were prevented from constructing. The Raiders also claimed damages resulting from relocation and per diem expenses, lost radio income, lost attendance income, and lost food and beverage income.

In November 1988, the Raiders and Oakland settled the lawsuit. Oakland agreed to pay the Raiders $4 million in four yearly installments of $1 million plus interest. The settlement agreement stated that it was entered into for the "purpose of settling disputed claims involving the restoration of lost franchise value."

For each of the tax years 1988 and 1989, the Commissioner determined that settlement proceeds of $600,000 ($1 million less $400,000 attorney's fees) received by the Raiders constituted taxable income. The Tax Court found that the Oakland settlement represented recovery of lost profits and, therefore, constituted taxable income. *Milenbach,* 106 T.C. at 201.

The Raiders argue that no portion of the settlement represented recovery of lost profits. They assert that the settlement represented recovery of lost value to the franchise and therefore should be treated as non-taxable return of capital. The Raiders claim that they never sought to recover lost profits in their action against Oakland, only the lost value of their franchise. They argue that their Claim for Damages can only be read as seeking recovery for lost franchise value because they based their claim on Oakland's denial of "the free use and enjoyment" of their franchise. The Raiders also point to the fact that the settlement agreement with Oakland provided that the payment compensated the Raiders for "lost franchise value."

B. Analysis

The nature of a settlement payment is a question of fact reviewed for clear error. *See Langer v. Comm'r,* 989 F.2d 294, 296 (8th Cir.1993) (per curiam); *Wolfson v. Comm'r,* 651 F.2d 1228, 1230 (6th Cir.1981); *Spangler v. Comm'r,* 323 F.2d 913, 916–17 (9th Cir.1963); *Pac. Magnesium v. Westover,* 183 F.2d 584, 584 (9th Cir.1950) (per curiam). When a claim is resolved by settlement, the relevant question for determining the tax treatment of a settlement award is: "In lieu of what were the damages awarded?" *Getty v. Comm'r,* 913 F.2d 1486, 1490 (9th Cir.1990); *Raytheon Prod. Corp. v. Comm'r,* 144 F.2d 110, 113 (1st Cir.1944). We take a "broad approach in determining the true nature and basis of a party's claim." ***933** *Getty,* 913 F.2d at 1491. If the payments are in lieu of lost profits, then they are taxable income. *Shakertown Corp. v. Comm'r,* 277 F.2d 625, 628 (6th Cir.1960); *Raytheon,* 144 F.2d at 113. If, however, the payments are for loss of franchise value due to damage to goodwill, then the payments are nontaxable return of capital. *Raytheon,* 144 F.2d at 113. The taxpayer bears the burden of establishing that proceeds of

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

a settlement are what the taxpayer contends them to be. *Getty,* 913 F.2d at 1492.

The Tax Court did not clearly err in finding that some portion of the Oakland settlement represented recovery for lost profits. The Raiders' list of damages included several items that consisted entirely of lost profit. Nothing in the language of the Claim for Damages or the inverse condemnation complaint suggests that the Raiders intended to limit their recovery to the reduction in value of their franchise caused by loss of goodwill. In addition, almost every item listed in the damages report would have been taxable had it been received by the Raiders. Any settlement amount meant to replace this lost income would have been "in lieu" of taxable income and would itself be taxable. *Getty,* 913 F.2d at 1490.

The Raiders argue that it is inherent in the nature of an inverse condemnation action that their potential recovery is limited to the damage done to the value of their franchise, and that the lost income was mentioned only as a measure of that damage. We need not decide whether an award in an inverse condemnation action represents recovery only for damage to the property, however, because the Raiders' attempts to recover damages were not limited to an inverse condemnation action.

The Raiders also sought recovery under California Code of Civil Procedure section 1268.620. Although the Raiders later filed an inverse condemnation action, the Claim for Damages under section 1268.620 was not dismissed prior to the settlement. Section 1268.620 allows the property owner in an unsuccessful eminent domain action to recover "all damages proximately caused by the proceeding and its dismissal as to that property." Cal.Civ.Proc.Code § 1268.620(b). In *Community Development Commission v. Shuffler,* 198 Cal.App.3d 450, 243 Cal.Rptr. 719, 725 (1988), the California Court of Appeal noted how "broadly worded" the provision was and stated that the statute allowed recovery of all damages caused by the eminent domain proceeding. The *Shuffler* court went on to note that this statute did not limit any claim the defendant might have under inverse condemnation for damage to property during litigation. *Id.* An action under section 1268.620 is separate and distinct from an inverse condemnation action. Any limits on the types of damages a plaintiff can recover in an inverse condemnation action do not apply to property owners seeking to recover damages under section 1268.620.

The Raiders also contend that the language of the settlement agreement should be dispositive in determining the nature of the settlement payments. The settlement agreement stated that payments were meant to settle disputed claims "involving the restoration of lost franchise value." The Raiders claim that the Tax Court should not have looked beyond the language of the settlement agreement in the absence of collusion or bad faith.

Although the allocation set forth in a settlement agreement by the parties is one factor in determining the nature of a settlement payment, "[w]hen assessing the tax implications of a settlement agreement, courts should neither engage in speculation nor blind themselves to a settlement's realities." *Bagley v. Comm'r,* 121 F.3d 393, 395 (8th Cir.1997). A court should take a broad approach in ***934** determining the nature of a settlement payment and is not bound by any allocation made by the parties in their settlement agreement if there is evidence that the payment represented something else. *See* *Bagley,* 121 F.3d at 395; *Delaney v. Comm'r,* 99 F.3d 20, 23–24 (1st Cir.1996). This is especially true in a case, such as this one, where one party (Oakland) apparently had no interest in classifying damages one way or the other. Oakland had no motive to ensure that the allocation in the settlement agreement accurately represented the nature of the settlement payments. [2]

Given the broad recovery allowed under section 1268.620 and the nature of the damages that the Raiders claimed to have suffered, the Tax Court did not clearly err in determining that some portion of the Oakland settlement represented taxable lost profits. Because the Raiders did not meet their burden of providing some basis for allocating the settlement between taxable lost profits and non-taxable damage to franchise, the Tax Court correctly upheld the Commissioner's allocation of the entire amount to taxable lost profits.

III. THE CITY OF IRWINDALE LOAN

A. Background

The ongoing dispute between the Raiders and the LAMCC prompted the Raiders to enter into a Memorandum of Agreement (the "Irwindale MOA") with the City of Irwindale ("Irwindale") in August, 1987. The Irwindale MOA provided that the Raiders would construct a new stadium in Irwindale and play their home games in that stadium, starting in 1992, at the expiration of the Lease with the LAMCC. The Irwindale MOA also provided that Irwindale would loan the Raiders $115 million, to be repaid exclusively from revenue from the to-be-constructed stadium. The loan was to be secured by a

deed of trust on the improvements the Raiders were obligated to build on the site provided for the proposed stadium.

Under the agreement, Irwindale advanced the Raiders $10 million of the loan. The Irwindale MOA provided that, should Irwindale fail to perform its obligations under the MOA, then all of the Raiders' obligations under the MOA would be extinguished, including the obligation to repay the advance. The Raiders would then be entitled to keep all funds advanced to them "as consideration for the execution" of the MOA. The MOA stated that Irwindale proposed to finance the project by issuing general obligation bonds.

The Irwindale MOA made allowances for some obstacles to the performance of the MOA:

> 8.5 If any obstacle is imposed by third parties (such as litigation, legislation, or failure to cooperate) it is agreed that both parties pledge good faith cooperation to overcome such obstacle. However, these obstacles will not be construed as a tolling event for the project itself, nor will it be construed as a reason to refund any exchange of monies, nor will it be construed as a forfeiture. It is further agreed, that both parties will move forward with the project and mutually work to resolving the problem....
>
> 8.6 Any third party obstacle will not excuse either party from proceeding with the project except to the extent ordered by court, e.g. an injunction.

In September 1988, the California Legislature enacted a statute that prohibited ***935** Irwindale from using general obligation bonds to fund construction of a stadium that would be turned over to a private company, such as the Raiders. This new law made it impossible for Irwindale to finance the project in the way proposed in the Irwindale MOA.

Despite this obstacle, the Raiders continued to negotiate with Irwindale through 1990 in an attempt to reach an agreement that would allow construction of a stadium in Irwindale. All alternative financing schemes were rejected, however, and, by late December 1989, one of Irwindale's negotiators declared that the parties were back where they had started two years earlier. In early 1990, the Raiders sought further proposals from Irwindale, but none was ever produced. The Raiders were never required to repay the $10 million advance.

At trial, the Commissioner argued that the Irwindale advance was not a bona fide loan and that it was taxable income in 1987, the year it was received. In the alternative, the Commissioner argued that the debt had been discharged in either 1987, 1988, or 1989.

The Tax Court held that the Irwindale advance was properly treated as a loan, rejecting the Commissioner's argument that it should be treated as taxable income in the year in which it was received. *Milenbach,* 106 T.C. at 201–02. The court also rejected the Commissioner's contention that the Irwindale debt was discharged in 1987. *Id.* at 203. Instead, the court found that the debt had been discharged in 1988, and that the Raiders realized $10 million in taxable income as a result. *Id.* at 204. The court based this finding primarily on the passage of the law in September 1988 which made financing the stadium with general obligation bonds impossible.[3] *Id.* at 203–04. The court reasoned that because the 1988 legislation prohibited the use of general obligation bonds to fund the project as proposed in the MOA, negotiations that continued beyond 1988 "were not conducted under the Irwindale MOA." *Id.* at 203.

B. Analysis

The Tax Court's determination of the timing of a discharge of indebtedness is reviewed for clear error. *Friedman v. Comm'r,* 216 F.3d 537, 542 (6th Cir.2000). Clear error exists only when the reviewing court is left with a "definite and firm conviction that a mistake has been committed." *Gonzalez–Caballero v. Mena,* 251 F.3d 789, 792 (9th Cir.2001) (citation omitted).

The discharge of a valid debt is treated as taxable income. 26 U.S.C. § 61(a)(12). A debt is discharged for tax purposes when "it becomes clear that the debt will never have to be paid." *Friedman,* 216 F.3d at 546. Determining the timing of a discharge of debt requires "a practical assessment of the facts and circumstances relating to the likelihood of payment." *Id.* Courts look at all of the facts concerning repayment, requiring only that the time of discharge be fixed by ***936** "some identifiable event which fixes the loss with certainty." *Id.* at 547–48. Repayment of the loan need not become absolutely impossible before a debt is considered discharged. *Exch. Sec. Bank v. United States,* 492 F.2d 1096, 1099(5th Cir.1974). A slim possibility that a debt may still be enforced does not prevent a debt from being treated as discharged for federal tax purposes. *Id.* at 1099–1100.

Although the test for discharge of debt requires the examination of the practical probability that a debt will be repaid, the Tax Court expressly based its holding that the Raiders debt was discharged in 1988 on its

conclusion that passage of the 1988 legislation "prohibited the implementation of the Irwindale MOA." *Milenbach,* 106 T.C. at 203. It concluded that, under California law, the terms of the contract required Irwindale to fund the loan with general obligation bonds or forfeit the advance.

Under California law, the mutual intention of the parties at the time the contract is formed governs interpretation of the contract. Cal. Civ.Code § 1636; *AIU Ins. Co. v. Superior Court,* 51 Cal.3d 807, 274 Cal.Rptr. 820, 799 P.2d 1253, 1264 (1990). Such intent is to be inferred, if possible, solely from the written provisions of the contract. Cal. Civ.Code § 1639; *AIU Ins. Co.,* 274 Cal.Rptr. 820, 799 P.2d at 1264. Forfeitures are not favored, however, and courts must strictly construe forfeiture provisions against the party on whose behalf they are invoked. Cal. Civ.Code § 1442; *Deutsch v. Phillips Petroleum Co.,* 56 Cal.App.3d 586, 128 Cal.Rptr. 497, 501 (1976). Where there are two possible interpretations of a contract, one that leads to a forfeiture and one that avoids it, California law requires the adoption of the interpretation that avoids forfeiture, if at all possible. *Ballard v. MacCallum,* 15 Cal.2d 439, 101 P.2d 692, 695 (1940).

Here, the terms of the MOA can, and must, be interpreted to avoid a forfeiture based on Irwindale's inability to fund the stadium with general obligation bonds. The terms of the forfeiture provision state that the advance would be forfeited only if Irwindale was unable "to provide the full funding of the entire amount of the loan provided for in paragraph 4.7." Although paragraph 4.7 mentions passage of a general obligation bond as a triggering date for two of the payments, it does not require that the loan actually be funded from such bonds. While it is clear that the parties assumed that Irwindale would be funding the loan with these general obligation bonds, there is no indication that either party intended to require such funding. Rather, the MOA required the forfeiture of the advance only if Irwindale was unable to come up with the full amount of the loan. Forfeiture would occur only if Irwindale was unable to provide the funds, from whatever source. The MOA did not require forfeiture if financing by general obligation bonds became impossible, as long as Irwindale could provide the funds from some other source. The passage of the 1988 legislation was simply another obstacle that the parties to the MOA had agreed to attempt to overcome. Had alternate funding become available, the Raiders would have continued to be bound by the Irwindale MOA, provided that Irwindale met all of its other obligations. Thus, the Tax Court erred in holding that the MOA ceased to bind the parties after the passage of the 1988 legislation.

On remand, the Tax Court must determine whether the Irwindale debt was discharged in any of the challenged years. ***937** The court must perform a "practical assessment of the facts and circumstances relating to the likelihood of payment." *Friedman,* 216 F.3d at 546. The court must determine when, as a practical matter, it became clear that Irwindale would not be able to fund the entire loan and that the stadium would not be built. It was at that point that a forfeiture resulted and the Irwindale debt was discharged. [4]

CONCLUSION

We affirm the Tax Court's decision that the Oakland settlement represented recovery of taxable lost profits. We reverse, however, the Tax Court's decision that the LAMCC loan payments were taxable upon receipt and that the Irwindale debt was discharged in 1988, and remand this case for further proceedings consistent with this opinion. Each party shall bear his, her, or its own costs on appeal.

AFFIRMED in part, REVERSED in part, and REMANDED.

All Citations

318 F.3d 924, 91 A.F.T.R.2d 2003-818, 2003-1 USTC P 50,229, 03 Cal. Daily Op. Serv. 1142, 2003 Daily Journal D.A.R. 1464

Footnotes

1 Our holding may or may not end the inquiry with respect to the taxability of the LAMCC loan. Although the Raiders were obligated to repay the loan at the time the payment was received and the rental offsets were made, at some point in time since then, that obligation was extinguished. Such a discharge of indebtedness must be treated as taxable income in the year in which the discharge occurred. 26 U.S.C. § 61(a)(12).

The record does not disclose when, if ever, the Raiders recognized the LAMCC loan proceeds as income. Presumably, the Commissioner can further challenge that timing decision, but that issue is not before us.

2 In fact, it would be in Oakland's interest to allow the Raiders to claim that the payments represented non-taxable loss of franchise value, if doing so would achieve a reduction in the amount of the settlement.

3 The Tax Court also noted that during litigation related to the Irwindale project both Irwindale and the Raiders stated that the Raiders was entitled to "keep the $10 million 'regardless of what happen[ed].' " *Milenbach,* 106 T.C. at 203. It is not clear what weight, if any, the Tax Court gave to these statements. In the context of the lawsuit in which these statements were made, they indicated only that the Raiders would be entitled to keep the advance even if the state court prevented the Irwindale stadium from being built. The statements cannot be reasonably interpreted as an admission that the Raiders were not ever obligated to repay the advance. Such a reading would clearly conflict with the plain terms of the MOA. Nor can Irwindale's statement be reasonably read as releasing the Raiders from its obligation to repay the advance.

4 Although we have concluded that, as a matter of California law, the Tax Court erred in holding that the Irwindale MOA *required* that the loan be funded with general obligation bonds, we express no opinion on the outcome on the merits of this issue, including how much weight the Tax Court should give to the passage of the 1988 legislation in its weighing of the factors as to when funding of the Irwindale stadium became a practical impossibility.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-21

Modern Law of Contracts § 21:6

Modern Law of Contracts | March 2020 Update
Howard O. Hunter

Chapter 21. Assignment

B. Mechanics of Assignment

§ 21:6. Manifesting intent to assign

Intention is the key to assignment.[1] The passage of title by operation of law is not an assignment.[2] An assignor must show an intention to divest himself of a property interest and to vest indefeasible title to that property interest in an assignee.[3] An assignment can be made orally and does not have to be supported by consideration.[4] There are no particular or prescribed formalities for assignment.[5]

Despite regular attempts to treat checks as assignments of funds, the law is clear that a check drawn on a demand account is not, by itself, an assignment.[6] Further, a blanket endorsement of a check is not an assignment by the endorser to the endorsee, although the endorsee may be a holder in due course.[7] In one case, for example, a subcontractor on a public construction project carried a labor and material payment bond as required by law. Employees of the subcontractor often took their paychecks to the Tara Pub where the owner would cash them as a service to his customers. The pub owner was left holding the bag when the bank dishonored more than $23,000 in paychecks for insufficient funds and the pub owner wanted to collect against the bond as an assignee.

> [A]t the time of the transfer of the checks, there was no objective manifestation by the [subcontractor's] employees … that the employees were assigning … any rights they may have possessed in the payment bond … we have found no authority that persuades us that the endorsement and delivery of a check transfers, as a matter of law, anything other than a right to payment from the drawer of the instrument and certain rights against the endorser.[8]

An assignor can manifest the assignment in any reasonable way.[9] An oral assignment is good and is not unusual when the subject of the assignment is an oral contract.[10] If the contract being assigned is in writing, the assignment should be in writing as well, if for no other reason than to avoid subsequent disputes about unrecorded conversations. If the statute of frauds governs the transaction, the assignment must be in writing.

Intention to assign and actual assignment may be determined by the context of a situation notwithstanding the absence of specific words to that effect. The Appellate Court of Illinois found that a purchaser of property through a foreclosure sale could develop the property as assignee of a declarant of a planned unit development even though there was not a written assignment of rights.[11]

Once the assignment is made, the assignee stands in the shoes of the assignor and may assert rights under the contract the same as the assignor.[12] The assignor no longer has the right or power to enforce the assigned interest.[13] The rules are slightly different if the assignment is of a security interest. Such an assignment does not extinguish the assignor's interest in the subject of the assignment because the purpose of the assignment is limited to security against a default in the principal contract.[14] On

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the other side of the creditor/debtor relationship, the general rule is that assignment of a debt carries with it assignment (at least equitably) of the security for the debt. [15]

Westlaw. © 2020 Thomson Reuters. No Claim to Orig. U.S. Govt. Works.

Footnotes

1 See McHenry Hosp. v. Metropolitan Life Ins. Co., 578 F. Supp. 122 (N.D. Ill. 1983); Brager v. Blum, 49 B.R. 626 (E.D. Pa. 1985). Getting the assignee's name right is an important aspect of "intention" especially if there is another entity or person with the same, or almost the same, name. Frontier Communications Northwest, Inc. v. D.R. Horton, Inc., 2014 WL 7473764 (Tex. App. Fort Worth 2014).

2 Johnson v. General Motors Corp., 349 Pa. Super. 147, 502 A.2d 1317, 42 U.C.C. Rep. Serv. 851 (1986) (overruled on other grounds by, REM Coal Co., Inc. v. Clark Equipment Co., 386 Pa. Super. 401, 563 A.2d 128, Prod. Liab. Rep. (CCH) ¶ 12252, 9 U.C.C. Rep. Serv. 2d 916 (1989)) (widow who received title to husband's car through his estate was not an assignee).

3 Kelly Health Care, Inc. v. Prudential Ins. Co. of America, Inc., 226 Va. 376, 309 S.E.2d 305 (1983).

4 Crystal Clear Development, LLC v. Devon Architects of New York, P.C., 127 A.D.3d 911, 7 N.Y.S.3d 361 (2d Dep't 2015).

5 Wells v. McMahon, 2019 WL 1779566 (D. Nev. 2019).

6 U.C.C. § 3-409(1); U.S. v. Four Million, Two Hundred Fifty-Five Thousand, 762 F.2d 895, 41 U.C.C. Rep. Serv. 859 (11th Cir. 1985).

7 Dysart Corp. v. Seaboard Sur. Co., 240 Conn. 10, 688 A.2d 306 (1997).

8 Dysart Corp. v. Seaboard Sur. Co., 240 Conn. 10, 688 A.2d 306, 310 (1997).

9 Farnsworth, Contracts, § 11.3, at 754.

10 See McDonald v. Welding Specialty, Inc., 144 Ga. App. 303, 241 S.E.2d 18 (1977).

11 Board of Managers of Medinah on Lake Homeowners Ass'n v. Bank of Ravenswood, 295 Ill. App. 3d 131, 229 Ill. Dec. 629, 692 N.E.2d 402 (3d Dist. 1998).

12 BSC Associates, LLC v. Leidos, Inc., 91 F. Supp. 3d 319 (N.D. N.Y. 2015). For example, the assignment of a contract that includes an arbitration clause includes the assignment of that clause and the assignee is subject to arbitration the same as the assignor. Williams-Hopkins v. LVNV Funding, LLC, 2019 WL 1873155 (N.J. Super. Ct. App. Div. 2019). If the clause itself delegates the determination of arbitrability to the arbitrator, the assignee is bound the same as the assignor would have been. See, Henry Schein, Inc. v. Archer and White Sales, Inc., 139 S. Ct. 524, 202 L. Ed. 2d 480, 169 Lab. Cas. (CCH) ¶ 11141, 2019-1 Trade Cas. (CCH) ¶ 80627 (2019). But see for a slightly differing view, Toll Dallas TX, LLC v. Dusing, 2019 WL 2127885 (Tex. App. Austin 2019).

13 One Call Property Services Inc. v. Security First Ins. Co., 165 So. 3d 749 (Fla. 4th DCA 2015).

14 In re Pihl, Inc., 529 B.R. 414 (Bankr. D. Mass. 2015).

15 A.J. Properties, LLC v. Stanley Black and Decker, Inc., 469 Mass. 581, 15 N.E.3d 198 (2014).

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-22

KeyCite Yellow Flag - Negative Treatment
Distinguished by Southwest Pet Products, Inc. v. Koch Industries, Inc., D.Ariz., June 12, 2000

205 F.3d 1351
Unpublished Disposition
NOTICE: THIS IS AN UNPUBLISHED OPINION.
(The Court's decision is referenced in a "Table of Decisions Without Reported Opinions" appearing in the Federal Reporter. Use FI CTA9 Rule 36-3 for rules regarding the citation of unpublished opinions.)
United States Court of Appeals, Ninth Circuit.

MRO COMMUNICATIONS, INC., Plaintiff-Appellant,
v.
AMERICAN TELEPHONE & TELEGRAPH COMPANY, now AT & T Corp., Defendant-Appellee.

No. 98-16716.
|
D.C. No. CV-95-00503-PMP.
|
Argued and Submitted Nov. 2, 1999.
|
Decided Dec. 13, 1999.

Appeal from the United States District Court for the District of Nevada, Philip M. Pro, District Judge, Presiding.

Before CHOY, SCHROEDER, and ALARCÓN, Circuit Judges.

MEMORANDUM [1]

***1** MRO Communications, Inc. ("MRO"), appeals from the order granting judgment on the pleadings to American Telephone & Telegraph Company ("AT & T") on MRO's antitrust claims, the order of partial summary judgment in favor of AT & T on a number of other issues and claims, and the grant of judgment as a matter of law for AT & T on MRO's remaining claims after a jury trial. Because MRO failed to present facts sufficient to support any of its claims, we affirm. Because the parties are familiar with historical and procedural background of this dispute, we will not rehearse them here.

I

MRO contends that the allegations in its complaint were sufficient to withstand AT & T's motion for judgment on the pleadings on MRO's claims under 15 U.S.C. §§ 1 and 2. We review de novo the entry of a judgment on the pleadings pursuant to Federal Rule of Civil Procedure 12(c). *Arnett v. California Pub. Employees Retirement Sys.,* 179 F.3d 690, 694 (9th Cir.1999). Judgment for AT & T was properly granted because, taking all the allegations in the pleadings as true, AT & T was entitled to judgment as a matter of law. *See Nelson v. City of Irvine,* 143 F.3d 1196, 1200 (9th Cir.), *cert. denied,* ____ U.S. ____, 119 S.Ct. 444 (1998).

A

To make out a claim of monopolization in violation of 15 U.S.C. § 2, MRO had to allege: (1) AT & T's possession of monopoly power in the relevant market; (2) AT & T's willful acquisition or maintenance of that power through exclusionary conduct; and (3) causal antitrust injury. *American Prof'l Testing Serv., Inc. v. Harcourt Brace Jovanovich Legal and Prof'l Publications, Inc.,* 108 F.3d 1147, 1151 (9th Cir.1997).

The one fact that MRO averred to support a finding of monopoly power was that AT & T had approximately a 50% share of the billing services and transport services markets. A high market share may raise an inference of monopoly power. *Oahu Gas Serv., Inc. v. Pacific Resources, Inc.,* 838 F.2d 360, 366 (9th Cir.1988). It is unlikely, however, that a 50% share of market, without more, can support a finding of monopoly power. *See Rebel Oil Co., Inc. v.. Atlantic Richfield Co.,* 51 F.3d 1421, 1438 (9th Cir.1995) ("[N]umerous cases hold that a market share of less than 50 percent is presumptively insufficient to establish market power.... [A] market share of 44 percent is sufficient as a matter of law to support a finding of market power, if entry barriers are high and competitors are unable to expand their output in response to supracompetitive pricing."); *Twin City Sportserv. Inc. v. Charles O. Finley & Co.,* 512 F.2d 1264, 1274 (9th Cir.1975) ("[O]n several occasions courts have considered a 50% share of the market as inadequate to establish a proscribed monopoly.").

More importantly, an inference of monopoly power from a high market share is inappropriate where there is evidence of the defendant's inability to control prices or exclude

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

competitors. *Oahu Gas,* 838 F.2d at 366. MRO's concession in its complaint that both MCI and Sprint offered billing and transport services and submitted viable bids to MRO is compelling evidence of AT & T's inability to exclude competitors. MRO failed to allege facts demonstrating that AT & T possessed monopoly power as required to sustain a claim of monopolization under 15 U.S.C. § 2.

B

***2** To make out a claim of attempted monopolization in violation of 15 U.S.C. § 2, MRO had to allege: (1) AT & T's specific intent to control prices or destroy competition; (2) predatory or anti-competitive conduct directed at accomplishing that purpose; (3) a dangerous probability of AT & T achieving monopoly power; and (4) causal antitrust injury. *Rebel Oil Co.,* 51 F.3d at 1432-33.

Neither monopoly power nor a dangerous probability of achieving monopoly power can exist absent barriers to new entry or expansion. *American Prof'l Testing,* 108 F.3d at 1154; *Rebel Oil,* 51 F.3d at 1439. The main sources of entry barriers are: (1) legal license requirements; (2) control of an essential or superior resource; (3) entrenched buyer preference for established brands; (4) capital market evaluations imposing higher capital costs on new entrants; and, in some situations, (5) economies of scale. *American Prof'l Testing,* 108 F.3d at 1154. We have rejected the theory that the good reputation of one vendor for providing high quality service constitutes an entry barrier to other vendors. *Id.*

In its complaint, MRO did not allege any barriers to entry or expansion in the billing or transport services markets. Furthermore, MRO did not allege that AT & T had a specific intent to control prices or destroy competition and that AT & T engaged in predatory or anti-competitive conduct directed at accomplishing that purpose. MRO alleged only that the BSA provisions had the "effect" of preventing AT & T customers from switching to a new billing services provider. The facts alleged do not support MRO's attempted monopolization claim.

C

To make out a claim of tying in violation of 15 U.S.C. § 1, MRO had to allege: (1) a tie-in between two products or services sold in different markets; (2) market power in the tying product market; and (3) an effect on a not insubstantial volume of commerce. *Datagate, Inc. v. Hewlett-Packard Co.,* 60 F.3d 1421, 1423-24 (9th Cir.1995). To plead the element of market power, MRO had to allege that AT & T had sufficient economic power in one product market to "coerce" MRO to purchase a second product. *Id.* at 1426.

By its own account, MRO could have contracted with either MCI or Sprint for billing and transport services but chose to contract with AT & T. MRO's allegation that it chose to contract with AT & T because it believed AT & T would deliver better service is not enough to support an inference of market power. *See American Prof'l Testing,* 108 F.3d at 1154 (rejecting the theory that a good reputation for providing high quality service, without more, confers market power) (citing *United States v. Syufy Enters.,* 903 F.2d 659, 668-69 (9th Cir.1990)).

MRO contends that AT & T's practice of assigning new 900 numbers to existing customers was a form of unlawful tying. As alleged in MRO's complaint, AT & T was able to discourage billing and transport customers from switching to a new billing services provider because of the equity the customers develop in their specific 900 numbers. We have already considered and rejected the theory that a practice like AT & T's is an exploitation of market power.

***3** In *Mozart Co. v. Mercedes-Benz of North America, Inc.,* a Mercedes-Benz franchisee was obligated under the franchise contract to use only parts approved by the franchisor. 833 F.2d 1342, 1343-44 (9th Cir.1987). The crux of the franchisee's tying claim was that he had to buy the parts the franchisor required or else he would lose the investment he had made in his franchise. *Id.* at 1346. We rejected the theory that the franchisor's policy was unlawful tying:

> Obviously there are costs to surrendering one franchise and acquiring another, but these costs are unrelated to the "market power" of the [franchisor's product]. These costs will enable the [franchisor] to extract concessions from the [franchisee], but this power is related to the franchise method of doing business, not to the possible uniqueness of the [product].

Id. at 1346-47.

As in *Mozart,* the advantage AT & T acquires over its 900 number customers is unrelated to market power and instead arises out of the nature of the business relationship. A service provider with a tiny share of the billing and transport services markets would acquire this same advantage over its customers. The district court did not err in denying MRO's tying claim.

D

MRO asserts that the district court should have granted MRO leave to amend instead of entering judgment on the pleadings for AT & T. We review the denial of leave to amend for abuse of discretion. *Swanson v. United States Forest Serv.,* 87 F.3d 339, 343 (9th Cir.1996). Because MRO failed to move properly for leave to amend, the district court's failure to grant such leave was not an abuse of discretion.

Under the Local Rules of Practice for the District of Nevada, "[t]he original proposed amended pleading shall be signed and attached to any motion to amend a pleading." D. Nev. R. 15-1(a). MRO's "motion" for leave to amend consisted of requests made in its opposition to AT & T's motion for judgment on the pleadings and in MRO's filed objections to the magistrate judge's report to the district court. MRO did not submit a proposed amended pleading to the court.

Valid local rules have the force of law. *Marshall v. Gates,* 44 F.3d 722, 724 (9th Cir.1995). A local rule is valid if it is "not inconsistent" with the Federal Rules of Civil Procedure. *Id* . (citing Fed.R.Civ.P. 83). The pertinent Federal Rule provides that, after a responsive pleading has been served, a party may amend its pleading by "leave of court." Fed.R.Civ.P. 15(a). Nevada's Local Rule 15-1(a) merely prescribes the procedure by which a party can secure the requisite leave of court and therefore is "not inconsistent" with Rule 15(a). Because MRO did not present a proper motion for leave to amend, the district court's failure to afford such leave sua sponte was not an abuse of discretion. *See Miranda v. Southern Pac. Transp. Co.,* 710 F.2d 516, 521 (9th Cir.1983) ("District courts have broad discretion in interpreting and applying their local rules.").

II

A

***4** MRO maintains that the district court erred in granting summary judgment to AT & T with respect to the enforceability of the BSA damages disclaimer and in excluding MRO's evidence of alleged "lost revenues."

1

We review a grant of summary judgment de novo. *Burrell v. Star Nursery, Inc.,* 170 F.3d 951, 954 (9th Cir.1999). The BSA included a New Jersey choice of law provision. New Jersey courts generally will enforce limitations of liability in private contracts like the BSA. *Marbro, Inc. v. Borough of Tinton Falls,* 688 A.2d 159, 162 (N.J.Super.Ct.L.Div.1996). Under New Jersey law, MRO and AT & T could agree to limit their liability so long as the limitation was not unconscionable or otherwise in contravention of public policy. *Id.* As the party challenging the contractual limitation of liability, MRO had the burden of proving its unconscionability. *See id.* at 163-64; *see also Wasserman's Inc. v. Township of Middletown,* 645 A.2d 100, 108 (N.J.1994) (expressly holding that the party challenging a contractual liquidated damages clause has the burden of proving unreasonableness).

The reasonableness of a contractual limitation of liability is a question of law. *Marbro,* 688 A.2d at 164. A New Jersey court may find a limitation on liability is unconscionable if the party challenging the clause shows that it was disadvantaged in the bargaining process, was powerless to negotiate the terms of the contract, or had a justified expectation that the limitation of liability clause would not be enforced. *Id.* at 163. Additionally, if the party relying on the contractual limitation of liability engaged in "willful and wanton misconduct," it cannot use the contractual provision to shield itself. *Tessler and Son, Inc. v. Sonitrol Sec. Sys., Inc.,* 497 A.2d 530, 533 (N.J.Super.Ct.App.Div.1985). "Willful and wanton misconduct" is a tortious act performed intentionally or with reckless disregard of the consequences. *Id.*

In opposition to the motion for summary judgment, MRO submitted three declarations. The declaration of Michael Olsen is the only one of the three that contains allegations pertinent to the enforceability of the disclaimer. Olsen alleged that the BSA was a "take it or leave it" form contract drafted by AT & T and that MRO was less than a year old and had less than $100,000 in assets when it signed the BSA. These

allegations are not enough to make the contractual limitation of liability unenforceable. Without more, the mere fact that the BSA was a "take it or leave it" form contract does not make it unconscionable. *Rudbart v. North Jersey Dist. Water Supply Comm'n,* 605 A.2d 681, 687 (N.J.1992). Moreover, the fact that MRO was a start-up company at the time of entering into the BSA does not equate to being powerless or disadvantaged in the bargaining process. *See, e.g., Shell Oil Co. v. Marinello,* 307 A.2d 598, 601 (N.J.1973) (finding buyer was disadvantaged because the seller "[f]or all practical purposes [could] dictate its own terms"); *Henningsen v. Bloomfield Motors, Inc.,* 161 A.2d 69, 95 (N.J.1960) (finding buyer was disadvantaged in the bargaining process because it had "no real freedom of choice"). Indeed, any assertion that MRO was powerless in the bargaining process is belied by MRO's concession that MCI and Sprint had also submitted bids for MRO's business.

***5** Lastly, the alleged "willful" breaches of contract by AT & T do not rise to the level of the tort of "wanton and willful misconduct ." *Tessler and Sons, Inc.,* 497 A.2d at 533-34. A simple failure to perform under a contract is generally not a tort. *See Noye v. Hoffman-La Roche Inc.,* 570 A.2d 12, 19 (N.J.Super.Ct.App.Div.1990). MRO pointed to nothing that would make AT & T's conduct anything more than a simple failure to perform its contractual duties. Summary judgment was therefore properly granted on the issue of the enforceability of the contractual damages disclaimer.

2

MRO contends that the district court erred when, pursuant to the disclaimer, it excluded a damages calculation showing MRO's alleged "lost revenues" and the supporting expert testimony of David Kahn and three other experts. We review de novo the district court's interpretation of the contractual damages disclaimer. *Simula, Inc. v. Autoliv, Inc.,* 175 F.3d 716, 719 (9th Cir.1999). We review the district court's exclusion of MRO's evidence for abuse of discretion. *EEOC v. Pape Lift, Inc.,* 115 F.3d 676, 680 (9th Cir.1997).

In Kahn's declaration, he described the methodology used in preparing the damages calculation. Kahn stated that "MRO's damage calculations reasonably estimate the incremental revenue that the MRO 900 numbers would have made, but for AT & T's improper termination of those numbers in 1991 and 1992 and other improper actions and/or inactions by AT & T as set forth in MRO's First Amended and Supplemental Complaint." He also provided a detailed description of the methodology used to calculate MRO's "lost revenues."

The damages MRO sought to prove with the excluded evidence fall squarely within the textbook definition of consequential damages. In *Law of Remedies,* Dan B. Dobbs describes the difference in general and consequential breach of contract damages:

> Expectancy damages are sometimes measured by "general damages" or market measures. Such measures use the market value of the very thing promised, at the time of performance, as a basis for calculation.... "Special damages" (consequential damages) are measured, not by the value of the promised performance alone but by the gains such performance could produce for collateral reasons, or the loss that is produced by the absence of such performance.

Dan B. Dobbs, *Law of Remedies* § 12.1(1) (2d ed.1993); *see also Perth Amboy Iron Works, Inc. v. American Home Assurance Co.,* 543 A.2d 1020, 1033 (N.J.Super.Ct.App.Div.1988), *aff'd mem.,* 571 A.2d 294 (N.J.1990) (discussing a similar definition of consequential damages in N.J. Stat. Ann. § 12A:2-715). MRO's alleged "lost revenues" are a "loss that is produced by the absence of [AT & T's] performance." Dobbs, *supra.* The district court therefore did not err in concluding that MRO's "lost revenues" were consequential damages disclaimed in the BSA. The district court properly excluded the evidence as irrelevant. Fed.R.Evid. 401-402.

B

***6** MRO also challenges the exclusion from trial of evidence of an alleged $1,476,206 in chargeback damages as a discovery sanction for untimely disclosure. MRO contends that the evidence should have been admitted as a timely supplement to an earlier expert witness disclosure. We review for abuse of discretion the district court's exclusion of

evidence as a discovery sanction. *Payne v. Exxon Corp .,* 121 F.3d 503, 507 (9th Cir.1997).

The district court set November 29, 1995, as the date by which all of MRO's expert witness disclosures and reports required by Federal Rule of Civil Procedure 26 were to be furnished to AT & T. In the timely disclosure of David Lahaderne, he stated that he had prepared the "AT & T Chargebacks and Erroneous Chargebacks Report" ("Report"). Attached to his declaration was a thirty-page spreadsheet that was the Report and a document detailing the methodology used in its preparation. As described in that document, the Report was designed to tabulate all "duplicate" and "bogus" chargebacks. "Duplicate" chargebacks occurred when AT & T deducted the cost of the same telephone call from MRO's revenues more than once. "Bogus" chargebacks were those "chargebacks for which MRO never received payment from AT & T for the original call."

In November 1997, two years after the court's deadline, MRO furnished AT & T with an exhibit entitled "Chargebacks by Month Greater Than 90 Days From Billing Month," which purported to show $1,476,206 in chargeback damages. Lahaderne was to provide supporting expert testimony. Federal Rule of Civil Procedure 37 provides that "[a] party that without substantial justification fails to disclose information required by Rule 26(a) or 26(e)(1) shall not, unless such failure is harmless, be permitted to use as evidence at a trial, at a hearing, or on a motion any witness or information not so disclosed." Fed.R.Civ.P. 37(c)(1). It was reasonable for the district court to infer that a two year delay in disclosing evidence interfered with AT & T's ability to prepare for trial. The district court therefore did not abuse its discretion in excluding Lahaderne's additional expert testimony and the related exhibit.

MRO contends that the untimely evidence should have been admitted pursuant to Federal Rule of Civil Procedure 26(e)(1). MRO invites this court to find that Rule 26(e)(1) creates a loophole through which a party who submits partial expert witness disclosures can add to them to its advantage after the court's deadline for doing so has passed. The language and spirit of Rule 26(e)(1) weigh against this reading of the rule. The rule creates a "duty to supplement," not a right. Fed.R.Civ.P. 26(e)(1); *see also Keener v. United States,* 181 F.R.D. 639, 640 (D.Mont.1998) ("Supplementation under the Rules means correcting inaccuracies, or filling the interstices of an incomplete report based on information that was not available at the time of the initial disclosure.").

***7** The exhibit and additional expert testimony of Lahaderne do not correct, clarify, or fill in a gap in the original Lahaderne disclosure. Instead, the new exhibit establishes a new category of chargeback damages. MRO does not contend that the information on which the new exhibit was based was unavailable at the time of the original Lahaderne disclosure. The district court did not err in concluding that the additional evidence was not admissible under Rule 26(e)(1). *See Keener,* 181 F.R.D. at 641-42 (excluding, on similar facts, the untimely portion of an expert's testimony that was styled as a supplement to the original disclosure).

III

A

MRO argues that the magistrate judge erred in concluding that MRO's FCA claim did not relate back to the original complaint. We review de novo a district court's determination that a claim does not relate back. *Martell v. Trilogy Ltd.,* 872 F.2d 322, 325 (9th Cir.1989).

In determining whether MRO's claim under the FCA relates back to the original complaint, the appropriate inquiry is whether the FCA claim and MRO's original complaint " 'share a common core of operative facts sufficient to impart fair notice of the transaction, occurrence, or conduct called into question." ' *FDIC v. Jackson,* 133 F.3d 694, 702 (9th Cir.1998) (quoting *Martell,* 872 F.2d at 327). In the original complaint, MRO alleged the following conduct by AT & T:

1. Failing and refusing to properly bill and collect from end users and forward those amounts to MRO.

2. Failing and refusing to credit MRO for calls for which end users never paid.

3. Failing to allow MRO to add or terminate 900 lines in order to satisfy the volume requirements under the BSA to obtain certain discounts.

4. Failing to credit MRO for MRO's monthly payments.

5. Withholding funds owed to MRO.

In the amended complaint, MRO identified the following conduct by AT & T as the basis of its FCA claim:

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

1. Refusing to change the termination point of MRO's transport services from Las Vegas to Reno or anywhere else in the United States.

2. Terminating transport services on MRO's particular 900 numbers, billing and collection services on MRO's 900 numbers, and terminating the 900 numbers of MRO and MRO's customers.

3. Refusing to permit other AT & T customers to terminate their 900 telephone numbers at MRO's facility.

The conduct alleged in support of the FCA claim does not overlap at all with the factual allegations in the original complaint. MRO's FCA claim and its original complaint therefore do not “share a common core of operative facts sufficient to impart fair notice [to AT & T] of the transaction, occurrence, or conduct called into question.” *FDIC,* 133 F.3d at 702. The district court therefore properly concluded that the FCA claim did not relate back to the original complaint. *See Murray v. Laborers Union Local No. 324,* 55 F.3d 1445, 1454 (9th Cir.1995). The district court also correctly concluded that the FCA statute of limitations barred MRO's claim to the extent that it challenged conduct occurring before February 8, 1993. 47 U.S.C. § 415(b).

***8** MRO urges this court to find that MRO's FCA claim did relate back to MRO's original complaint because similar FCA claims were raised in an action against AT & T filed August 21, 1991, by a different plaintiff in a different district. Our research revealed no authority to support this position. The case MRO cited to support its position did not consider whether factual allegations in a separate action could augment the factual allegations of an original complaint for purposes of determining whether a new claim related back to the original complaint. *See Woods Exploration and Producing Co. v. Aluminum Co. of America,* 438 F.2d 1286, 1299-1300 (5th Cir.1971).

B

On appeal, MRO challenges two conclusions of law that supported the district court's entry of partial summary judgment for AT & T on the FCA claim. The district court's interpretation of the FCA is reviewed de novo. *Bay Area Addiction Research and Treatment, Inc. v. City of Antioch,* 179 F.3d 725, 730 (9th Cir.1999). The district court's interpretation of the BSA is reviewed de novo. *Simula, Inc. v. Autoliv, Inc.,* 175 F.3d 716, 719 (9th Cir.1999).

First, MRO challenges the district court's conclusion that any alleged breaches of the BSA could not constitute violations of the FCA because the FCA does not regulate such agreements. MRO argues that AT & T's practice of assigning new 900 numbers on termination of billing services “ties” those services to the FCA regulated transport services and therefore subjects the billing services to FCA regulation. The district court's conclusion was supported by an FCC opinion relating to the same issue. *See In re AT & T 900 Dial-It Servs. and Third Party Billing and Collection Servs.,* 4 F.C.C.R. 3429 (1989). In the opinion, the FCC decided that AT & T's billing services were properly offered by AT & T on a non-tariffed basis and that the services should not be regulated by the FCA. *Id* . at 3433-34. In arriving at this decision, the FCC had before it a sample AT & T billing services contract. *Id.* at 3435 n. 53. MRO's argument is unpersuasive in the face of the FCC's opinion explicitly stating that it was “not convinced that any connection between the [billing services and transport services] is so significant” to warrant regulation of the billing services pursuant to the FCA. *Id* . at 3433. “Deference is due to the expressed opinions of the FCC on matters within their jurisdiction.” *California Satellite Sys. v. Seimon,* 767 F.2d 1364, 1367 (9th Cir.1985).

Second, MRO challenges the conclusion that the BSA and the Tariff expressly foreclosed any claim by MRO to a proprietary interest in its particular 900 numbers. BSA provisions 8 and 9 and Tariff provision E unambiguously establish that an AT & T customer has no proprietary right to his unique 900 numbers. A common sense reading of the BSA provisions further establishes AT & T's broad contractual right to assign new 900 numbers as AT & T sees fit to carry out its billing services or upon the termination of billing services by either party. *See Klamath Water Users Protective Ass'n v. Patterson,* 191 F.3d 1115, 1120 (9th Cir.1999) (noting that a contract “is only ambiguous if reasonable people could find its terms susceptible to more than one interpretation”).

***9** A remaining question is whether Tariff provision E made AT & T's practice of assigning new 900 numbers to existing customers permissible as a matter of law under the FCA. As discussed above, however, the last time AT & T changed MRO's 900 numbers was in October 1992, more than two years before MRO filed its amended complaint. We do not reach the question of whether AT & T's practice violated the FCA because the claim is time-barred. 47 U.S.C. § 415(b).

C

MRO also contends that the district court erred in excluding the testimony of Edward Kinsley. MRO sought to introduce Kinsley's testimony in support of its FCA claim of discrimination. To sustain its discrimination claim, MRO had to establish not only that AT & T treated MRO unlike other customers but also that the differences in treatment were unjust or unreasonable. 47 U.S.C. § 202(a). The district court excluded Kinsley's testimony as irrelevant. This evidentiary ruling is reviewed for abuse of discretion. *EEOC v. Pape Lift, Inc.,* 115 F.3d 676, 680 (9th Cir.1997).

The reason AT & T gave when it refused to make the termination point transfer MRO had requested was that MRO was in bankruptcy and the accounts of AT & T customers in bankruptcy were “frozen.” If allowed to testify, Kinsley would have testified that AT & T made just such a transfer for another customer. Kinsley and MRO conceded, however, that the other customer was not in bankruptcy. The district court may reasonably have concluded that Kinsley's testimony related only to AT & T's treatment of customers that it had a neutral, rational basis for treating differently from MRO and was therefore not probative of whether AT & T unjustly or unreasonably discriminated against MRO. The district court did not abuse its discretion in excluding Kinsley's testimony as irrelevant. Fed.R.Evid. 401-402. Because MRO offered no other evidence in support of its discrimination claim, we affirm the grant of judgment as a matter of law for AT & T on MRO's discrimination claim. Fed.R.Civ.P. 50(a).

AFFIRMED.

All Citations

205 F.3d 1351 (Table), 1999 WL 1178964, 2000-1 Trade Cases P 72,751

Footnotes

1 This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as may be provided by 9th Cir. R. 36-3.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-23

919 F.Supp.2d 345
United States District Court,
S.D. New York.

NEUROAXIS NEUROSURGICAL ASSOCIATES, PC, Plaintiff,
v.
COSTCO WHOLESALE COMPANY, Defendant.
Neuroaxis Neurosurgical Associates, PC, Plaintiff,
v.
Sprint Nextel Corporation, Defendant.
Neuroaxis Neurosurgical Associates, PC, Plaintiff,
v.
Aetna Health, Inc. and Aetna Health Insurance Company of New York, Defendants.

Nos. 11 Civ. 8350(DLC), 11 Civ. 8516(DLC), 11 Civ. 8756(DLC).
|
Jan. 23, 2013.

Synopsis
Background: In three coordinated actions, health care provider sought payment from Employee Retirement Income Security Act (ERISA) and non-ERISA welfare benefit plans for close to 200 surgical procedures performed on plan members. Plans moved to dismiss the claims.

Holdings: The District Court, Denise Cote, J., held that:

personal rights clauses in ERISA plans prohibiting the plan participant from assigning her rights to the healthcare provider rendered any purported assignment of participant's ERISA claim to healthcare provider void;

plan was not estopped from relying on the anti-assignment provisions in the plan; and

settlement agreement did not bar plan from relying on plan's anti-assignment clause to defend health care provider's ERISA claims.

Motions granted in part and denied in part.

Procedural Posture(s): Motion to Dismiss.

Attorneys and Law Firms

***347** Mario David Commetti, Timothy F. Butler, Tibbetts, Keating & Butler, LLC, New York, NY, for Plaintiff.

Jodie L. Ousley, Kimberly A. O'Toole, d'Arcambal Ousley & Cuyler Burk, LLP, New York, NY, for Defendants.

***348** *OPINION AND ORDER*

DENISE COTE, District Judge:

In these three coordinated actions, neurosurgeons associated with the plaintiff Neuroaxis Neurosurgical Associates, PC ("Neuroaxis") seek payment from welfare benefit plans for close to 200 surgical procedures performed on plan members. Neuroaxis has sued Sprint Nextel Corporation ("Sprint") and Costco Wholesale Company ("Costco"), private sector welfare plan sponsors, as well as Aetna Health Insurance Company of New York ("Aetna"), the plans' administrator. The defendants have moved to dismiss the plaintiff's claims on several grounds, three of which are addressed in this Opinion. As described below, in many instances Neuroaxis will be unable to recover against the plans because the benefit plans bar the assignment of claims by plan participants. On the other hand, two of the other issues raised by the defendants do not preclude the plaintiff's claims. Specifically, these suits are not barred by a 2003 settlement agreement ("2003 Settlement Agreement"), and upon proper application of the parties' tolling agreement, a number of the plaintiff's claims are timely under the plans' timing provisions. With the guidance given in this Opinion, the parties will be invited to identify which remaining issues require discovery or are ripe for further motion practice.

BACKGROUND
Aetna is an insurance company that administers the welfare benefits plans at issue here ("Plans"), including plans sponsored by Sprint and Costco. The majority of the Plans are sponsored by private sector employers like Sprint and Costco and as a result are governed by the Employee Retirement Income Security Act, 29 U.S.C. § 1001 *et seq.* ("ERISA"). The remainder of the Plans are administered by Aetna for government agencies and are not governed by ERISA. The Neuroaxis physicians performed approximately 182 surgeries after June 1, 2004, as out-of-network healthcare providers to patients covered by the Plans. Of these 182 surgeries, 105

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

were performed during the period covered by the Amended Complaints, that is, before December 31, 2007.

Neuroaxis contends that the Plans obligate the defendants to pay the doctors for the healthcare services at a "reasonable and customary rate," calculated on the basis of "the type of service provided, and the fee most commonly charged for that service" in the relevant geographic area. Neuroaxis further contends that the defendants improperly used other measures in calculating repayment rates, thereby unreasonably reducing the payments to the doctors. For instance, its complaint against Aetna asserts that Aetna ignored the "reasonable and customary" standard and used other factors to calculate payments such as "charges received by Aetna for the same service." Between the three complaints, the plaintiff claims to be owed approximately $8,481,753.

PROCEDURAL HISTORY

This litigation began on December 20, 2010, when Neuroaxis commenced an action against Aetna seeking recovery for health services provided by it from June 1, 2004 through December 31, 2007 to patients covered by employer-sponsored benefit plans administered by Aetna. The suit was filed in state court and was removed to federal court by Aetna. The parties then entered into a tolling agreement (the "Tolling Agreement"), agreed to engage in settlement negotiations, and dismissed the action. The Tolling Agreement provided that, should negotiations fail, "the Parties shall have the right to file and pursue any and all Claims in Federal Court."

***349** The Tolling Agreement also provided that "the Timing Defenses applicable to the Claims shall be tolled during the Tolling Period," but that the Tolling Agreement would "have no effect on any Timing Defenses that may be available to Aetna or Neuroaxis" either prior to or after the expiration of the Tolling Period. The Tolling period ran from December 20, 2010 to September 16, 2011.

On October 20, 2011, Neuroaxis initiated the instant action against Aetna and on October 27, 2011, Neuroaxis filed two lawsuits against Costco and Sprint. [1] Neuroaxis filed each action in state court, and the defendants removed the actions to this Court. At a conference held on March 9, 2012, the plaintiff's motions to remand were denied since the plaintiff's claims were preempted by ERISA and properly removed.

In *Montefiore Med. Center v. Teamsters Local 272,* 642 F.3d 321, 328 (2d Cir.2011), the Second Circuit outlined a three step test, derived from *Aetna Health Inc. v. Davila,* 542 U.S. 200, 124 S.Ct. 2488, 159 L.Ed.2d 312 (2004), for determining when a plaintiff's state law claims are completely preempted by ERISA. Applying this framework, this Court determined that Neuroaxis's state law claims were completely preempted by ERISA. Following the conference, Neuroaxis was given an opportunity to amend all of its complaints to plead ERISA causes of action.

Neuroaxis filed amended complaints that included ERISA claims in the Aetna and Costco matters on April 6, 2012. No amended complaint has been filed in the Sprint matter. [2] The amended complaints against Aetna and Costco assert five causes of action: 1) Failure to Abide by the Terms of ERISA-governed benefits plans in violation of 29 U.S.C. § 1104(a)(1)(D); 2) Breach of Contract; 3) Third Party Beneficiary Rights; 4) Unjust Enrichment; 5) Quantum Meruit. Neuroaxis also asserts that Aetna breached its fiduciary duties under 29 U.S.C. §§ 1022, 1104(a)(1)(A)(i), and 1106. The complaint against Sprint asserts only the four state law causes of action.

In a series of conferences, Aetna described several legal defenses that it contends bar most if not all of the claims in these actions. Since decisions on these issues will impact the scope of discovery, the Court ordered the defendants to file a motion addressed to those defenses.

Following limited discovery on threshold issues, on August 3, 2012, the defendants filed motions to dismiss in all three of these actions. The motions to dismiss address four threshold issues: 1) Whether the plaintiff has standing to sue under ERISA; 2) Whether the plaintiff's claims are barred by the timing provisions of the Plans; 3) Whether the plaintiff's claims were released under the 2003 Settlement Agreement; and 4) Whether the plaintiff has exhausted administrative remedies. The parties have attached numerous affidavits and exhibits to their motion papers. Neuroaxis filed its opposition to the motions on September 24, 2012. Briefing on the motions to dismiss was fully submitted on October 9, 2012. This Opinion addresses only the first three issues raised by the motions to dismiss.

DISCUSSION

When presented with a motion to dismiss, the court may not consider matters ***350** outside of the pleadings without converting the motion into a motion for summary judgment. *Friedl v. City of New York,* 210 F.3d 79, 83–84 (2d Cir.2000). A district court must ordinarily give notice to the parties

before converting a motion to dismiss to a motion for summary judgment, but a party "is deemed to have notice that a motion may be converted ... if that party should reasonably have recognized the possibility that such a conversion would occur." *Sira v. Morton,* 380 F.3d 57, 68 (2d Cir.2004) (citation omitted); *see also Hernandez v. Coffey,* 582 F.3d 303, 307 (2d Cir.2009); *see also Aetna Cas. & Sur. Co. v. Aniero Concrete Co., Inc.,* 404 F.3d 566, 573 (2d Cir.2005). Where represented parties attach to a motion to dismiss or to the opposition thereto "extensive materials that were not included in the pleadings," they "plainly should [be] aware of the likelihood of" conversion, and "cannot complain that they were deprived of an adequate opportunity to provide the materials they deemed necessary to support their" position. *Sira,* 380 F.3d at 68; *see also Aetna Cas. & Sur. Co.,* 404 F.3d at 573. In light of the parties' extensive factual submissions, it is appropriate to convert the defendants' motions to dismiss to motions for summary judgment.

Summary judgment may not be granted unless all of the submissions taken together "show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed.R.Civ.P. 56(c). The moving party bears the burden of demonstrating the absence of a material factual question, and in making this determination, the court must view all facts in the light most favorable to the non-moving party. *Celotex Corp. v. Catrett,* 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986); *Sista v. CDC Ixis N. Am., Inc.,* 445 F.3d 161, 169 (2d Cir.2006). When the moving party has asserted facts showing that the non-movant's claims cannot be sustained, the non-movant must "set forth specific facts showing that there is a genuine issue for trial," and cannot rest on the "mere allegations or denials" of the movant's pleadings. Fed.R.Civ.P. 56(e); *accord Sista,* 445 F.3d at 169. Only disputes over material facts, facts that might affect the outcome of the suit under the governing law, will properly preclude the entry of summary judgment. *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986).

1. Standing to Sue under ERISA

The defendants argue that, with respect to most of the claims at issue, Neuroaxis lacks standing to sue under ERISA. More specifically, the defendants contend that most of the Plans at issue bar or' limit assignments by Plan members to healthcare providers, and since the plaintiff's standing is ostensibly based exclusively on its status as an assignee, the plaintiff lacks standing to sue.

Pursuant to ERISA Section 502(a)(1)(B), health plan participants and beneficiaries are authorized to bring civil enforcement actions to recover plan benefits. *See Simon v. General Elec. Co.,* 263 F.3d 176, 177 (2d Cir.2001); 29 U.S.C. § 1132. The terms "participant" and "beneficiary" are defined by statute. A "participant" is "any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers employees of such employer or members of such organization, or whose beneficiaries may be eligible to receive any such benefit." 29 U.S.C. § 1002(2)(B)(7); *see also Simon,* 263 F.3d at 177. A "beneficiary" is "a person designated by a participant, or by ***351** the terms of an employee benefit plan, who is or may become entitled to a benefit thereunder." 29 U.S.C. § 1002(2)(B)(8); *see also Simon,* 263 F.3d at 177. A person seeking to recover under ERISA qualifies as a participant or beneficiary with standing to sue as long as they have a "colorable claim to vested benefits." *Firestone Tire & Rubber Co. v. Bruch,* 489 U.S. 101, 117, 109 S.Ct. 948, 103 L.Ed.2d 80 (1989) (citation omitted); *see also Coan v. Kaufman,* 457 F.3d 250, 256 (2d Cir.2006).

In *Franchise Tax Bd. v. Construction Laborers Vacation Trust for S. Cal.,* 463 U.S. 1, 103 S.Ct. 2841, 77 L.Ed.2d 420 (1983), the Supreme Court held that Section 502 permits only the parties specifically enumerated in the statute to sue for relief. *Id.* at 27, 103 S.Ct. 2841; *see also Montefiore Med. Center,* 642 F.3d at 329; *Simon,* 263 F.3d at 177. The Second Circuit, however, has carved out a "narrow exception" to this rule, holding that "healthcare providers to whom a beneficiary has assigned his claim in exchange for health care" have ERISA standing. *Montefiore Med. Center,* 642 F.3d at 329 (citation omitted); *see also I.V. Services of America Inc. v. Trustees of the American Consulting Engineers Council,* 136 F.3d 114, 117 n. 2 (2d Cir.1998). Thus, a provider who asserts a claim as an assignee of a participant or beneficiary to an ERISA plan has standing to sue as long as the litigant has a colorable claim to that status. *Kennedy v. Connecticut Gen. Life Ins. Co.,* 924 F.2d 698, 700 (7th Cir.1991).

In order for an assignee to prevail on an ERISA claim, however, the assignee must establish the existence of a valid assignment that comports with the terms of the welfare benefits plan. As explained in *Kennedy,* a plaintiff may bring suit under Section 502(a) when he asserts a colorable claim to beneficiary status, but "[b]ecause ERISA instructs courts to enforce strictly the terms of plans, an assignee cannot *collect*

unless he establishes that the assignment comports with the plan." *Id.* at 700 (citation omitted); *see also Physicians Multispecialty Group v. Health Care Plan of Horton Homes, Inc.,* 371 F.3d 1291, 1293 (11th Cir.2004); *City of Hope Nat. Med. Center v. HealthPlus, Inc.,* 156 F.3d 223, 228 (1st Cir.1998).

Assuming a plan does not dictate the form of a valid assignment or bar assignment altogether, a court may draw upon federal common law in assessing whether any purported assignment was effective. *See I.V. Servs. Of Am. Inc.,* 136 F.3d at 117 n. 2. In discerning the content of federal common law, courts draw inspiration from state law to the extent that state law is not inconsistent with the federal policies underlying ERISA. *Critchlow v. First UNUM Life Ins. Co. of Am.,* 378 F.3d 246, 256 (2d Cir.2004). Valid assignments may take a variety of forms. *Montefiore Med. Center,* 642 F.3d at 329 n. 8. At common law, an assignment can be made "either orally or by writing" unless a statute or contract provides otherwise. Restatement (Second) of Contracts § 324. Under New York law "[n]o particular words are necessary to effect an assignment; it is only required that there be a perfected transaction between the assignor and assignee, intended by those parties to vest in the assignee a present right in the things assigned." *Leon v. Martinez,* 84 N.Y.2d 83, 88, 614 N.Y.S.2d 972, 638 N.E.2d 511 (1994). *But see Hobbs v. Blue Cross Blue Shield of Alabama,* 276 F.3d 1236, 1241 (11th Cir.2001) (requiring written assignment).

As noted, however, where plan language unambiguously prohibits assignment, an attempted assignment will be ineffectual. *See Physicians Multispecialty Group,* 371 F.3d at 1295; *LeTourneau Lifelike Orthotics & Prosthetics, Inc. v.* ***352** *Wal–Mart Stores, Inc.,* 298 F.3d 348, 352 (5th Cir.2002); *City of Hope,* 156 F.3d at 229; *Davidowitz v. Delta Dental Plan of Calif., Inc.,* 946 F.2d 1476, 1481 (9th Cir.1991). Thus, a healthcare provider who has attempted to obtain an assignment in contravention of a plan's terms is not entitled to recover under ERISA.

In determining whether contract language prohibits assignment to a healthcare provider, courts apply traditional principles of contract interpretation. *See LeTourneau* 298 F.3d at 352; *cf. Critchlow,* 378 F.3d at 256; *City of Hope,* 156 F.3d at 229. The Second Circuit "interpret[s] ERISA plans in an ordinary and popular sense as would a person of average intelligence and experience." *Critchlow,* 378 F.3d at 256. Furthermore, because the Second Circuit applies "rules of contract law to ERISA plans, a court must not rewrite, under the guise of interpretation, a term of the contract when the term is clear and unambiguous." *Burke v. PriceWaterHouseCoopers LLP Term Disability Plan,* 572 F.3d 76, 81 (2d Cir.2009) (citation omitted).

As mentioned above, some of the Plans are governmental plans, and therefore are not governed by ERISA. 29 U.S.C. § 1003(b)(1). Some of the governmental welfare benefits plans may be governed by state law. While no party expressly addresses the law that applies to the non-ERISA Plans, the defendants have relied upon New York law, and the plaintiff has not taken issue with that choice nor relied on the law of any other jurisdiction. [3] Under New York law, unambiguous contract provisions that limit a party's ability to assign its rights under the contract render any purported assignment void. *Allhusen v. Caristo Const. Corp.,* 303 N.Y. 446, 452, 103 N.E.2d 891 (1952); *see also Spinex Laboratories Inc. v. Empire Blue Cross and Blue Shield,* 212 A.D.2d 906, 906–07, 622 N.Y.S.2d 154, 155 (N.Y.App.Div. 3d Dept.1995); *Cole v. Metro. Life Ins.,* 273 A.D.2d 832, 833, 708 N.Y.S.2d 789 (N.Y.App.Div. 4th Dept.2000).

The plaintiff has alleged a colorable claim to assignee status and is thus entitled to sue under ERISA. Specifically, the plaintiff contends that it should be permitted to prove the existence of valid assignments by means of 1) written assignments to Neuroaxis surgeons; 2) written assignments to a hospital where Neuroaxis surgeons rendered care; 3) patient intake forms; 4) oral assignments; or 5) requests for payment forms submitted by Neuroaxis to Aetna. The plaintiff has submitted no proof of any assignment, however, for 111 of its claims. Following the guidance given in this Opinion, the plaintiff will be permitted a further opportunity to show a valid assignment of claims for reimbursement arising under Plans that permit assignments. Without further factual development it cannot be determined whether each of these purported forms of assignment was effective.

Turning to the merits, at least 75 of the claims at issue arise from Plans that contain some version of an anti-assignment clause. These clauses limit the right to assign a claim in one or more of the following four ways and may prevent recovery by the plaintiff. One type of clause provides that coverage, or rights to Plan benefits, can only be assigned by a Plan member or covered person with the consent of ***353** Aetna. ("Consent Clause"). For instance, the GE Healthcare Preferred Plan, states that:

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> A covered person may assign his or her right to receive plan benefits to a health care provider *only with the consent of the benefits administrator,* in its sole discretion, except as may be required by applicable law. Assignments must be in writing. If benefits are assigned in accordance and a health care provider submits claims on behalf of a covered person, benefits will be paid to that health care provider. [4]

(Emphasis supplied.)

Another category of non-assignment clause states that rights under the Plans are personal to the member and categorically may not be assigned ("Personal Rights Clause"). For instance, the Rubies Costume Company Plan provides that:

> All rights of the member to receive benefits hereunder are personal to the member and may not be assigned.

A third category of non-assignment clause prohibits assignment except in limited circumstances or when otherwise permitted by the Plan ("Limited Circumstances Clause"). For example, the Sprint Plan provides that:

> Except under limited circumstances, your benefits cannot be assigned and transferred to another person or organization.

Lastly, some of the non-assignment clauses provide that the contract-holder or policy-holder may not assign coverage or benefits without the consent of the Plan administrator ("Contract–Holder Clause"). For example, the Bank of Tokyo—Mitsubishi Plan provides that:

> No rights or benefits under this group agreement are assignable by contract holder to any other party unless approved by HMO. [5]

Two of these four categories of clauses bar the claims asserted by Neuroaxis on ***354** behalf of participants in Plans that contain these clauses. In those two instances, Neuroaxis has failed to show that Plans containing these clauses have permitted them to pursue these claims on the basis of a valid assignment of rights.

The plain meaning of the Consent Clauses is that assignments are prohibited without the consent of the administrator, here, Aetna. The defendants have presented evidence that consent to assignments was never requested from Aetna and that consent was never given for any assignment. The plaintiff has offered no evidence that consent was requested or received for any assignment, but seeks to take discovery of Aetna and Plan members to develop such evidence. Accordingly, Neuroaxis will be given an opportunity to take targeted discovery to show that Aetna provided consent for Neuroaxis to obtain assignments of claims from Plan members under Plans containing Consent Clauses.

The Personal Rights Clauses are more categorical. The Personal Rights Clauses in the Plans are identical or nearly identical to the clause interpreted in *City of Hope.* In *City of Hope,* the welfare benefits plans provided that "All entitlements of a member to receive covered rights are personal and may not be assigned." *City of Hope,* 156 F.3d at 229. The First Circuit held that this language prohibited the plan participant from assigning her rights to the healthcare provider and, as a result, the defendant insurance carrier was entitled to judgment as a matter of law. *Id.* As a result, Plans with Personal Rights Clauses render any purported assignment void.

The Limited Circumstances Clauses are less categorical than the Personal Rights Clauses, but in this case, the difference is not significant. These clauses provide that, except in limited circumstances or as specifically provided by the Plans, benefits may not be assigned to another person or organization. The plaintiff has not argued that the assignments they purportedly received fall within the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

limited circumstances in which assignments are permissible. Accordingly, the purported assignments of claims accruing under Plans with Limited Circumstances Clauses are also invalid.

The final category of non-assignment language—the Contract–Holder Clauses—requires a more extended discussion. As mentioned, these clauses prohibit the contract-holder or policy-holder from assigning rights and benefits under the Plans. The plaintiff argues that this language does not prohibit Plan members from assigning their rights and benefits to healthcare providers because the Plans define the contract-holder or policy-holder as the employer or the company sponsoring the Plan. For example, claim 150 is asserted under a Plan that contains a Contract–Holder Clause. The Group Agreement that covers this claim defines the contract-holder as “Astoria Federal Savings.” By the plain terms of the Group Agreement, the contract-holder is not a Plan member and this language does not prohibit Plan members from assigning their rights to healthcare providers. Thus, to the extent that Plans containing Contract–Holder Clauses define the contract-holder or policy-holder as the employer or Plan sponsor, those clauses would not bar Plan members from granting assignments to healthcare providers.

To be clear, while the Contract–Holder Clauses do not prohibit Plan members from granting assignments to healthcare providers, to the extent the Plans contain other non-assignment clauses, those other clauses may bar the members from granting assignments. For example, claims 101 and 102 are asserted under Plans that contain Contract–Holder Clauses as well as Personal Rights Clauses. Thus, while ***355** the Contract–Holder Clauses in those Plans do not affect the Plan members' ability to grant assignments, the Personal Rights Clauses do.

The plaintiff makes principally five arguments against construing the anti-assignment clauses to invalidate its purported assignments of rights. First, the plaintiff argues that the Personal Rights Clauses should be interpreted to bar only those assignments that are made to other creditors of a Plan participant, rather than to healthcare providers. In support of its argument, Neuroaxis relies on *Hermann Hospital v. MEBA Medical & Benefits Plan,* 959 F.2d 569 (5th Cir.1992). In *Hermann Hospital* the relevant non-assignment language read as follows:

> No employee, dependent or beneficiary shall have the right to assign, alienate, transfer, sell, hypothecate, mortgage, encumber, pledge, commute, or anticipate any benefit payment hereunder, and any such payment shall not be subject to any legal process to levy executing upon or attachment or garnishment proceedings against for the payment of any claims.

Id. at 574. The Fifth Circuit interpreted

> the anti-assignment clause as applying only to unrelated, third-party assignees —other than the health care provider of assigned benefits—such as creditors who might attempt to obtain voluntary assignments to cover debts having no nexus with the Plan or its benefits, or even involuntary alienations such as attempting to garnish payments for plan benefits.

Id. at 575. In support of this determination, the Fifth Circuit emphasized “the typical ‘spendthrift’ language of the clause.” *Id.*

The Personal Rights Clause described above, however, does not contain “typical spendthrift” language. Instead, it is either identical or very nearly identical to the anti-assignment clause construed in *City of Hope,* where the First Circuit held that the clause barred the attempted assignment to the healthcare provider. *City of Hope,* 156 F.3d at 229. The Personal Rights Clauses are general and broad. They do not take the form of traditional spendthrift clauses and there is no basis to find that they were meant to apply only to third-party creditors other than healthcare providers.

Next, Neuroaxis argues that in a number of the Plans Aetna reserved discretion to make payments directly to out-of-network healthcare providers. This reservation, Neuroaxis argues, demonstrates that the Plans are not meant to prohibit

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

assignments by Plan members to healthcare providers. But, the fact that Aetna has reserved for itself the right to make direct payments to healthcare providers does not suggest that the Plan members also have the right to unilaterally assign rights to healthcare providers.

A related argument made by Neuroaxis is that because Aetna accepted direct billing from Neuroaxis and made direct reimbursement payments to Neuroaxis on each claim, Aetna is estopped from relying on the anti-assignment provisions in the Plans. Principles of estoppel can be applied in the ERISA context in "extraordinary" circumstances. *Schonholz v. Long Island Jewish Med. Center,* 87 F.3d 72, 78 (2d Cir.1996). Estoppel in ERISA cases, as in other cases, has three elements: (1) material representation, (2) reliance and (3) damage. *Lee v. Burkhart,* 991 F.2d 1004, 1009 (2d Cir.1993). Prior payments to healthcare providers do not create a "viable estoppel claim," however, where ERISA plans unambiguously prohibit assignments. ***356** *Riverview Health Institute LLC v. Med. Mutual of Ohio,* 601 F.3d 505, 523 (6th Cir.2010). The Sixth Circuit explained the reasoning behind this conclusion as follows:

> Principles of estoppel cannot be applied to vary the terms of unambiguous plan documents; estoppel can only be invoked in the context of ambiguous plan provisions. There are at least two reasons for this. First, as we have seen, estoppel requires reasonable or justifiable reliance by the party asserting the estoppel. That party's reliance can seldom, if ever, be reasonable or justifiable if it is inconsistent with the clear and unambiguous terms of plan documents available to or furnished to the party. Second, to allow estoppel to override the clear terms of plan documents would be to enforce something other than the plan documents themselves. That would not be consistent with ERISA.

Riverview Health Institute LLC, 601 F.3d at 521 (citation omitted).

The Personal Rights and Limited Circumstances Clauses unambiguously prohibit assignments, as does the Consent Clause in the absence of consent from Aetna. Thus, the defendants are not estopped from relying on the Plans' anti-assignment provisions as a defense to the plaintiff's claims.

Next, Neuroaxis argues that the breach of anti-assignment clauses by the Plan members entitles the defendants to damages from the Plan members, but does not affect the validity of the assignments to Neuroaxis. It relies on the principle under New York law that "covenants not to assign [are treated] as personal covenants whose breach justifies only an award of damages, unless the language of the covenant clearly indicates a stronger intent." *Citibank, N.A. v. Tele/Resources, Inc.,* 724 F.2d 266, 268 (2d Cir.1983); *see also* Restatement (Second) of Contracts § 322.

As explained above, however, New York considers an assignment "void" when contracts unambiguously prohibit assignments. *Allhusen,* 303 N.Y. at 452, 103 N.E.2d 891. Moreover, federal courts routinely enforce anti-assignment clauses in ERISA-governed welfare plans. *See, e.g., Physicians Multispecialty Group,* 371 F.3d at 1295 (11th Cir.2004); *LeTourneau Lifelike Orthotics & Prosthetics, Inc.,* 298 F.3d at 352; *City of Hope,* 156 F.3d at 229; *Davidowitz,* 946 F.2d at 1481. Similarly, unambiguous anti-assignment clauses in government welfare benefit plans have also been enforced. *See, e.g., Cole,* 273 A.D.2d at 832–33, 708 N.Y.S.2d at 790.

Lastly, the plaintiff argues that Aetna is barred from relying on any Plan's anti-assignment clause because § 7.13 of the 2003 Settlement Agreement, discussed at greater length below, binds Aetna. Section 7.13 states that

> [Aetna] shall recognize all valid assignments by Plan Members of Plan benefits to Physicians; provided that [Aetna] shall not be obligated to recognize such assignments in any market in which a competitor with substantial market share declines to recognize similar benefits assignments.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Section 12.1(a) of the 2003 Settlement Agreement dictates the exclusive forum for enforcement of this settlement term. It states that

> All Compliance Disputes shall be directed not to the Court nor to any other state court, federal court, arbitration panel or any other binding or non-binding dispute resolution mechanism but to the Compliance Dispute Facilitator to be designated by Class Counsel. [Aetna] shall publish on the Public Website the name and address of the Compliance Dispute Facilitator. The proposed Order and Final Judgment shall provide that no state or federal court or dispute ***357** resolution body of any kind shall have jurisdiction over any enforcement of § 7 of this Agreement at any time, including without limitation through any form of review or appeal, except to the extent otherwise provided in this Agreement.

Accordingly, Neuroaxis must raise Aetna's purported failure to comply with § 7.13 of the 2003 Settlement Agreement with the "Compliance Dispute Facilitator," and may not rely on § 7.13 in litigation before this Court.

2. Release by Settlement Agreement

Aetna next asserts that the plaintiff's claims are barred by the terms of a settlement entered in 2003 in a multi-district class action law suit. The settlement, which binds Neuroaxis, does not prevent it from pursuing these post-settlement claims.

On October 24, 2003, the Southern District of Florida entered an Order approving a settlement agreement that arose out of the *In re Managed Care Litigation,* Case. No. 1:00–MDL–1334 ("MDL 1334") ("the 2003 Settlement"). In MDL 1334, healthcare providers alleged that Aetna systematically undercompensated in-network and out-of-network providers. The parties do not dispute that Aetna was a released party under the 2003 Settlement and that Neuroaxis, as a class member that did not opt-out, is bound by it. The 2003 Settlement Agreement provides that Aetna

> shall be released ... [by] all Class Members who have not validly and timely requested to Opt–Out of this Agreement ... from any and all causes of action, judgments, liens, indebtedness, costs, damages, obligations, attorneys' fees, losses, *claims,* liabilities and demands of whatever kind or character, *arising on or before the Preliminary Approval Date,* that are, were or could have been asserted against any of the Released Parties based on or arising from the factual allegations of the Complaint.

(Emphasis supplied.) The complaint to which this provision refers is the Provider Plaintiffs' Second Amended Consolidated Class Action Complaint ("the 1334 Complaint"). The Preliminary Approval Date is May 30, 2003.

The parties do not agree on which jurisdiction's law should be applied to the 2003 Settlement Agreement. The defendants rely primarily on New York law, while the plaintiff cites cases from the Eleventh Circuit. The 2003 Settlement Agreement itself provides that

> [Aetna] and the Signatory Medical Societies agree that, with respect to disputes arising between and among such Persons, this Agreement shall be governed by and construed in accordance with the *laws of the State of Florida,* without regard to the conflicts of law rules of such state.

(Emphasis supplied.) The 2003 Settlement Agreement, over which the federal court continues to exercise jurisdiction, thus adopted Florida law for the construction of its terms. The 2003 Settlement Agreement's choice of Florida law will be honored here.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Under Florida law, settlement agreements are interpreted in accordance with traditional contract principles. *Comm. Capital Resources LLC v. Giovannetti,* 955 So.2d 1151, 1153 (Fla.Dist.Ct.App.2007). Terms of a settlement agreement "are to be given their plain and ordinary meaning, and it is not for the court to add or subtract any language from the face of a clearly worded agreement." *Schwartz v. Florida Bd. of Regents,* 807 F.2d 901, 905 (11th Cir.1987) (applying Florida law). It is a deeply rooted principle of Florida law, that "the intent of the ***358** parties controls interpretations of their releases." *Wachovia Ins. Servs. Inc. v. Toomey,* 994 So.2d 980, 986 (Fla.2008) (citation omitted). Accordingly, "[i]n construing a release agreement, the court must look first to the intent of the parties as expressed in the document itself." *Weingart v. Allen & O'Hara, Inc.,* 654 F.2d 1096, 1103 (5th Cir.1981) (applying Florida law). If the language of the release is clear and unambiguous, a court will "not entertain evidence contrary to its plain meaning." *Cerniglia v. Cerniglia,* 679 So.2d 1160, 1164 (Fla.1996).

The parties dispute whether the claims made by the plaintiff here "aris [e] from the factual allegations of the [1334] Complaint" and were therefore released under the 2003 Settlement. It is unnecessary to resolve that dispute since the 2003 Settlement only bars claims that arose "on or before the Preliminary Approval Date," that is, May 30, 2003. The language of the release is clear and unambiguous. Therefore, the release does not bar the claims pressed here, the earliest of which arose in 2004. *See In re Managed Care Litigation,* 2010 WL 6532982, *12 (S.D. Fla. Aug. 15, 2010).

Aetna argues that claims arising after 2003 may nonetheless be barred by the 2003 Settlement since the 2003 Settlement Agreement contained a broad release and Aetna made changes to its business practices in reliance on that release. Aetna contends that Neuroaxis must pursue any complaint it might have that Aetna has failed to comply with the 2003 Settlement Agreement through the 2003 Settlement Agreement's enforcement mechanism. Finally, it points out that the Southern District of Florida recently relied on the 2003 Settlement to enjoin an action that was seemingly based on conduct occurring after 2003. *In re Managed Care Litigation,* No. 00 MDL 1334, 2011 WL 1522561 (S.D.Fla. Mar. 8, 2011) (adopting Magistrate Judge's report and recommendation).

Aetna's effort to bar all future claims that may be filed against it by healthcare providers who were class members in the MDL 1334 arising from reimbursement practices that may have existed prior to the Preliminary Approval Date of the 2003 Settlement, may be swiftly rejected. Aetna does not rely on the doctrine of either claim or issue preclusion to dismiss the Neuroaxis claims. As already explained, the terms of the release in the 2003 Settlement Agreement are unambiguous and cannot be construed to bar reimbursement claims for surgeries performed after May 30, 2003.

3. Time Limitations

The final issue to be addressed in this Opinion is whether the plaintiff has lost the right to benefit from the Tolling Agreement because it breached its terms. The defendants assert that 49 claims are time barred; the plaintiff asserts that many of those claims are timely if it may rely on the tolling period contained in the Tolling Agreement. [6]

On May 19, 2011, the parties entered a Tolling Agreement in which they agreed that "the Timing Defenses applicable to the Claims shall be tolled during the Tolling Period." The parties agree that the Tolling Agreement expired on September 16, 2011. The defendants argue that Neuroaxis may not take advantage of the Tolling Agreement because it breached its terms by reinitiating its law suits in state court rather than federal court.

***359** The Tolling Agreement did not prohibit the plaintiff from re-initiating suit in state court. Rather, the Tolling Agreement provides that "if a settlement of all issues is not reached between the parties, the Parties shall have the right to file and pursue any and all Claims in Federal Court and to seek any and all legal remedies that may be available." This language is permissive rather than mandatory. *Cf. Global Seafood Inc. v. Bantry Bay Mussels Ltd.,* 659 F.3d 221, 224–26 (2d Cir.2011) (forum selection clause); *Blanco v. Banco Indus. de Venezuela, S.A.,* 997 F.2d 974, 979–80 (2d Cir.1993) (same). Accordingly, the parties shall take the Tolling Agreement into account when calculating whether any of the plaintiff's claims are time barred.

CONCLUSION

The defendants' August 3, 2012 motions to dismiss are granted in part. In summary, the plaintiff has failed to demonstrate that it received valid assignments of rights with respect to claims arising under ERISA-governed welfare Plans containing Personal Rights Clauses or Limited Circumstances Clauses. Accordingly, the plaintiff's ERISA causes of action are dismissed with respect to those claims. Claims asserted against Aetna, however, are not barred by

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the 2003 Settlement. Lastly, the parties must take the Tolling Agreement into account when calculating whether any of the plaintiff's claims are time barred.

All Citations

919 F.Supp.2d 345

Footnotes

1 A related case, *Neuroaxis Neurosurgical Assocs., I.C. v. Hartford Fire Insur. Co. Employee Med. et. al.,* 12 Civ. 0522(DLC), was voluntarily dismissed by the parties on August 27, 2012.

2 By a separate Order, Neuroaxis will be required to amend its complaint to plead an ERISA action by February 6, 2013 or the action against Sprint will be dismissed.

3 The sponsors for the government Plans include federal and local government entities as well as the United Nations. The parties have not addressed which law applies to each of these entities and it appears that it is unnecessary to do so to resolve the issues reached in this Opinion.

4 Other language falling in the “Consent Clause” category includes the following four examples: 1) Coverage may be assigned only with the written consent of Aetna. To the extent allowed by law, Aetna will not accept an assignment to an out-of-network provider, provider or facility including but not limited to, an assignment of: a) The benefits due under this contract; b) The right to receive payments due under this contract; or c) Any claim you make for damages resulting from a breach or alleged breach, of the terms of this contract; 2) Coverage may be assigned only with written consent of Aetna; 3) Coverage may be assigned only with written consent of Aetna. Aetna will not accept an assignment to an out-of-network provider or facility an assignment of the benefits due under this contract, the right to receive payments due under this contract or any claim you make for damages resulting from a breach or alleged breach; and 4) Rights and benefits cannot be assigned to anyone except when allowed under the Plan. You may authorize the administrator to make payments directly to providers for covered services. However, the administrator reserves the right to make payments directly to you. You cannot assign your right to receive payment to anyone else without written consent of the Plan, except as required by a qualified medical child support order (QMCSO) or any applicable state law.

5 Other language falling in the “Contract–Holder Clause” category includes the following two examples: 1) No rights or benefits under this Policy are assignable by the Policyholder to any other party unless approved by Us[.] Coverage may be assigned only with the written consent of Aetna. To the extent allowed by law, Aetna will not accept an assignment to an out-of-network provider, including but not limited to, an assignment of: a) The benefits due under this group insurance policy; b) The right to receive payments due under this group insurance policy; or c) Any claim you make for damages resulting from a breach or alleged breach, of the terms of this group insurance policy; and 2) No rights or benefits under this policy are assignable by the policyholder to any other party unless approved by us.

6 For instance, the plaintiff contends that if Aetna's proposed accrual date is used to calculate the running of the Plan's time limitations, and if the Tolling Agreement is applied, claims 76, 77, 101, 102, 154, 155, and 156 are timely.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-24

KeyCite Yellow Flag - Negative Treatment
Distinguished by Restoration 1 of Port St. Lucie v. Ark Royal Insurance Company, Fla.App. 4 Dist., September 5, 2018

165 So.3d 749
District Court of Appeal of Florida,
Fourth District.

ONE CALL PROPERTY SERVICES INC. a/a/o William Hughes, Appellant,
v.
SECURITY FIRST INSURANCE COMPANY, Appellee.

No. 4D14–424.
|
May 20, 2015.

Synopsis
Background: Insured's alleged assignee brought action against homeowners insurer to recover for breach of contract by failing to adequately compensate assignee for emergency water removal. The Fifteenth Judicial Circuit Court, Palm Beach County, Joseph George Marx, J., dismissed complaint. Assignee appealed.

Holdings: The District Court of Appeal, Taylor, J., held that:

trial court could review policy that insurer had attached to the motion, and

the assignment was valid.

Reversed and remanded.

Procedural Posture(s): On Appeal; Motion to Dismiss.

Attorneys and Law Firms

***750** Susan W. Fox of Fox & Loquasto, P.A., Orlando, and Scott G. Millard of ***751** Cohen Battisti, Attorneys at Law, Winter Park, for appellant.

Andrew A. Labbe and David J. Salmon of Groelle & Salmon, P.A., Tampa, for appellee.

Maria Elena Abate and Matthew C. Scarfone of Colodny, Fass, Talenfeld, Karlinsky, Abate & Webb, P.A., Fort Lauderdale, for Amici Curiae–Florida Property & Casualty Association and Florida Insurance Council.

Opinion

TAYLOR, J.

One Call Property Services ("One Call") appeals a final order dismissing a complaint that it filed, as an alleged assignee of an insured on a homeowners' policy, against Security First Insurance for breach of contract. Because we conclude that the trial court erred in dismissing One Call's complaint based on the anti-assignment and loss payment provisions of the insurance policy, we reverse.

One Call, as an alleged assignee of an insured on a homeowners' insurance policy, brought a complaint for breach of contract against the insurer, Security First, alleging that One Call performed emergency water removal services for the insured following an August 2012 water event, that the insured had assigned his right to insurance proceeds as payment, and that Security First refused to reimburse it adequately for the services provided. In the alternative, the complaint alleged that One Call had an assignment in equity based on the services it rendered. Attached to the complaint was a copy of the assignment, which stated in relevant part:

> I, the Owner, hereby assign any and all insurance rights, benefits, and proceeds under any applicable insurance policies to One Call. I make this assignment in consideration of One Call's agreement to perform services and supply materials and otherwise perform its obligations under this contract, including One Call not requiring full payment at the time of service. I intend to transfer all insurance rights to One Call, including any causes of action which exist or may exist in the future.

One Call did not attach a copy of the policy to the complaint. Instead, One Call alleged that a copy of the policy would be obtained "through the discovery process" and would "be filed in support of this action at that time." One Call also alleged

compliance with all conditions precedent to recovery under the policy.

Security First moved to dismiss, arguing that One Call lacked standing to maintain the lawsuit and that the complaint failed to state a cause of action. Security First advanced multiple arguments in support of its position that the assignment was invalid under the terms of the policy and Florida law. Attached to the motion to dismiss was a certified copy of the policy.

One Call filed a written response to the motion to dismiss, arguing that the motion impermissibly went beyond the four corners of the complaint and asserting various reasons for upholding the validity of the assignment.

The trial court held a hearing on the motion to dismiss. At the hearing, counsel for One Call focused on the argument that "the nonassignment provision of the policy when read in conjunction with the loss payment provision of the policy precludes the plaintiff, as an assignee, from bringing a lawsuit to determine the amount of the loss or ... what is due under the policy." The trial court ultimately granted the motion to dismiss on the basis of this argument, noting that the same ruling had been made in a similar case and that the court was "going to stay consistent." The court later entered a final order dismissing the complaint with prejudice. One Call appealed the dismissal.

***752** "A trial court's order granting a motion to dismiss is reviewed de novo." *Edwards v. Landsman,* 51 So.3d 1208, 1213 (Fla. 4th DCA 2011).

In ruling on a motion to dismiss, a trial court is limited to the four corners of the complaint and its incorporated attachments. *U.S. Project Mgmt., Inc. v. Parc Royale E. Dev., Inc.,* 861 So.2d 74, 76 (Fla. 4th DCA 2003). But where the terms of a legal document are impliedly incorporated by reference into the complaint, the trial court may consider the contents of the document in ruling on a motion to dismiss. *See Veal v. Voyager Prop. & Cas. Ins. Co.,* 51 So.3d 1246, 1249 (Fla. 2d DCA 2011) (rejecting argument that the trial court erred by considering the contents of a settlement agreement that was attached to a motion to dismiss: "[I]n this case, the complaint refers to the settlement agreement, and in fact, Veal's standing to bring suit is premised on the terms of that agreement. Accordingly, since the complaint impliedly incorporates the terms of the agreement by reference, the trial court was entitled to review the terms of that agreement to determine the nature of the claim being alleged.").

Here, the trial court did not err in considering the contents of the insurance policy that was filed in connection with the insurer's motion to dismiss. The complaint refers to the policy, and One Call's standing to bring suit is premised on an assignment of the policy. Accordingly, because the complaint impliedly incorporates the policy by reference, the trial court was entitled to review the policy in ruling on the motion to dismiss. [1]

On the merits of the issue, One Call argues that the trial court erred as a matter of law in dismissing its complaint based on the anti-assignment and loss payment provisions of the policy. Stated succinctly, One Call maintains that: (1) post-loss assignments of insurance proceeds are valid under Florida law even if the policy contains an anti-assignment clause; (2) the right of payment accrues on the date of the loss; and (3) the loss payment provision does not preclude an assignment of benefits and has never been construed to have any bearing on the issue of assignments.

"All contractual rights are assignable unless the contract prohibits assignment, the contract involves obligations of a personal nature, or public policy dictates against assignment." *Kohl v. Blue Cross & Blue Shield of Fla., Inc.,* 988 So.2d 654, 658 (Fla. 4th DCA 2008). Once an assignment has been made, "the assignor no longer has a right to enforce the interest because the assignee has obtained all rights to the thing assigned." *Continental Cas. Co. v. Ryan Inc. E.,* 974 So.2d 368, 376 (Fla.2008) (citations and internal quotation marks omitted). By statute, an insurance policy "may be assignable, or not assignable, as provided by its terms." § 627.422, Fla. Stat. (2012).

A chose in action [2] arising out of contract is assignable and "may be sued upon and recovered by the assignee in his ***753** own name and right." *Spears v. W. Coast Builders' Supply Co.,* 101 Fla. 980, 983, 133 So. 97, 98 (1931). "A claim on an insurance policy is a chose in action and is assignable as such." *United Cos. Life Ins. Co. v. State Farm and Fire Cas. Co.,* 477 So.2d 645, 646 (Fla. 1st DCA 1985). Where there is no provision forbidding assignment, "an insurance policy may be assigned as any other chose in action." *Kohl v. Blue Cross & Blue Shield of Fla., Inc.,* 955 So.2d 1140, 1143 (Fla. 4th DCA 2007).

Even when an insurance policy contains a provision barring assignment of the policy, an insured may assign a post-loss claim. *See W. Fla. Grocery Co. v. Teutonia Fire Ins. Co.,*

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

74 Fla. 220, 224, 77 So. 209, 210–11 (1917) ("The policy was assigned after loss, and it is a well-settled rule that the provision in a policy relative to the consent of the insurer to the transfer of an interest therein does not apply to an assignment after loss."); *Lexington Ins. Co. v. Simkins Indus., Inc.,* 704 So.2d 1384, 1386 n. 3 (Fla.1998) ("[The insurer] concedes that an insured may assign insurance proceeds to a third party after a loss, even without the consent of the insurer."); *Accident Cleaners, Inc. v. Universal Ins. Co.,* 2015 WL 1609973, *2 (Fla. 5th DCA Apr.10, 2015) ("[The insurer's] argument ignores that the right to recover is freely assignable after loss and that an assignee has a common-law right to sue on a breach of contract claim. Dating back to 1917, the Florida Supreme Court recognized that provisions in insurance contracts requiring consent to assignment of the policy do not apply to assignment after loss."); *Citizens Prop. Ins. Corp. v. Ifergane,* 114 So.3d 190, 195 (Fla. 3d DCA 2012) ("Post-loss insurance claims are freely assignable without the consent of the insurer."); *Better Constr., Inc. v. Nat'l Union Fire Ins. Co.,* 651 So.2d 141, 142 (Fla. 3d DCA 1995) ("[A] provision against assignment of an insurance policy does not bar an insured's assignment of an after-loss claim."); *Gisela Invs., N.V. v. Liberty Mut. Ins. Co.,* 452 So.2d 1056, 1057 (Fla. 3d DCA 1984) ("A provision in a policy of insurance which prohibits assignment thereof except with consent of the insurer does not apply to prevent assignment of the claim or interest in the insurance money then due, after loss."); *see also NextGen Restor., Inc. v. Citizens Prop. Ins. Corp.,* 126 So.3d 1255, 1256–57 (Fla. 2d DCA 2013) (stating in dicta: "[The anti-assignment clause] does not appear to prevent an assignment of benefits or proceeds owing by virtue of a claim arising under the policy. We do not reach the validity of this specific assignment of insurance benefits, but we note that other cases seem to permit assignees to bring similar actions.").

Despite the well-settled case law allowing post-loss assignments of insurance claims, Security First argues the assignment is invalid pursuant to the policy's anti-assignment and loss payment provisions. Security First maintains that the assignment impermissibly sought to assign unaccrued rights under the policy. Essentially, Security First argues that, at the time the assignment was executed, the insured had nothing to assign because at that time there were no benefits due and owing to the insured under the policy.

Security First's argument is based upon the loss payment clause of the policy, which states:

Loss Payment. We will adjust all losses with you. We will pay you unless some other person is named in the policy or is legally entitled to receive payment. Loss will be paid upon the earliest of the following:

a. 20 days after:

(1) We receive your written proof of loss and reach a written, executed agreement or settlement with you according to the terms of the written agreement; or

***754** **b.** 60 days after we receive your written proof of loss and:

(1) There is an entry of a final judgment or, in the case of an appeal from such judgment, within 60 days from and after the affirmance of the same by the appellate court; or

(2) Written executed mediation settlement with you according to the terms of the written mediation settlement; or

c. Within 90 days after we receive notice of an initial claim "reopened claim" or "supplemental claim" from you, we will pay or deny such claim or a portion of the claim unless the failure to pay such claim or portion of claim is caused by factors beyond our control which reasonably prevent such payment.

The issue we confront is whether payment must be due under the loss payment provision before an insured may assign a post-loss claim under the policy. We find that the loss payment provision "falls far short of creating a contractual bar to assignment." *Cf. Kohl,* 988 So.2d at 658 (language stating that "[b]enefits will be paid directly to you" fell "far short of creating a contractual bar to assignment").

The Second District's opinion in *Curtis v. Tower Hill Prime Ins. Co.,* 154 So.3d 1193 (Fla. 2d DCA 2015), while not directly on point, provides useful guidance on this issue. There, the Second District rejected an insurer's argument that the insureds could not "maintain a breach-of-contract suit until the time for payment under the loss-payment provision has come and gone without payment." *Id.* at 1196. The Second District held that "[t]he loss-payment provision of the policy did not render the suit premature; indeed, that provision expressly contemplated that there might be a final judgment —presumably stemming from a lawsuit—before payment was due." *Id.*

Following the reasoning of *Curtis,* we hold that a standard loss payment provision in an insurance policy does not preclude an assignment of a post-loss claim, even when payment is not yet due. The loss payment clause merely addresses the timing of the payment and expressly contemplates that a lawsuit could occur before payment is due. We decline to interpret it as affecting the validity of a post-loss assignment.

We therefore conclude that an assignable right to benefits accrues on the date of the loss, even though payment is not yet due under the loss payment clause. *Cf. In re Surfside Resort & Suites, Inc.,* 344 B.R. 179, 189 (Bkrtcy.M.D.Fla.2006) ("Once the Hotel had sustained property damage, [the insurer] was already responsible for payment of whatever claim Debtor asserted. Hence, once the damage affected the property, [the insurer's] obligation to pay originated."); *Antal's Rest., Inc. v. Lumbermen's Mut. Cas. Co.,* 680 A.2d 1386, 1389 (D.C.1996) ("Before loss, the insured has only an inchoate or a contingent right to compensation, but after loss that right has 'become absolute' and transferable without consent, since the relationship of insured and insurer is now one of 'creditor and debtor' and the policy [is] no longer 'significant except as evidence of the existence and amount of the debt.' ") (citation and internal alteration omitted); *cf. also Levy v. Travelers Ins. Co.,* 580 So.2d 190, 191 (Fla. 4th DCA 1991) (stating that an insurer's obligation to pay first-party PIP benefits arose as the loss was incurred, but also stating that the insurer "owed no contractual obligation to pay first-party benefits" at the time of the accident and that the cause of action to recover unpaid benefits accrued when the payment was overdue).

Furthermore, even assuming an insured's right to benefits does not accrue ***755** until payment is due under the loss payment provision, there is no reason why an insured could not assign an unaccrued right to benefits under the policy, so long as the assignment took place after the loss. The fact that a right is unaccrued does not necessarily prevent its assignment before the right accrues. *See* Restatement (Second) of Contracts § 320 ("The fact that a right is ... conditional does not prevent its assignment before the condition occurs.").

Nor can the assignment be invalidated on the theory that it attempts to assign a contractual "duty to adjust" from the insured to a third party. In arguing that the insured owes a duty to adjust the loss, the insurers rely upon the language of the loss payment provision stating that "[w]e will adjust the loss with you." Grammatically, "we" is the subject of the sentence and refers to the insurer, while "you" is the indirect object of the sentence and refers to the insured. Although this language contemplates the insured's participation in the adjustment process, it does not impose a *duty* on the insured to adjust the loss. In fact, a "duty to adjust" is not among the insured's duties in the section of the policy listing the insured's Duties After Loss.

An insured is not an "adjuster" and does not "adjust" losses. To "adjust" means "[t]o determine the amount that an insurer will pay an insured to cover a loss." *Black's Law Dictionary* (9th ed. 2009). An insured does not determine the amount that the insurer will pay to cover the loss, nor does an insured fit within any commonly recognized definition of "adjuster."

In short, as long as the insured complies with all policy conditions, a third-party assignee may recover benefits on a covered loss. *Cf. Shaw v. State Farm Fire and Cas. Co.,* 37 So.3d 329, 332 (Fla. 5th DCA 2010) (stating that "[a]ssignment of a right to payment under a contract does not eliminate the duty of compliance with contract conditions, but a third-party assignee is not liable for performance of any duty under a contract"), *disapproved on other grounds by Nunez v. Geico Gen. Ins. Co.,* 117 So.3d 388 (Fla.2013).

Turning to the practical implications of this case, we note that this issue boils down to two competing public policy considerations. On the one side, the insurance industry argues that assignments of benefits allow contractors to unilaterally set the value of a claim and demand payment for fraudulent or inflated invoices. On the other side, contractors argue that assignments of benefits allow homeowners to hire contractors for emergency repairs immediately after a loss, particularly in situations where the homeowners cannot afford to pay the contractors up front.

Our court is not in a position, however, to evaluate these public policy arguments. There is simply insufficient evidence in the record in this case—or in any of the related cases—to decide whether assignments of benefits are significantly increasing the risk to insurers. If studies show that these assignments are inviting fraud and abuse, then the legislature is in the best position to investigate and undertake comprehensive reform.

For the foregoing reasons, we reverse the dismissal of the complaint and remand for further proceedings consistent with this opinion. We emphasize, however, that we decline to reach

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

any of Security First's other challenges to the assignment, including whether the assignment violates the public adjuster statute or the statute governing insurable interests,[3] or whether the assignment is a partial assignment that cannot be enforced against Security First without its consent. The trial court should ***756** address these issues in the first instance. *See Stark v. State Farm Fla. Ins. Co.,* 95 So.3d 285, 289 n. 4 (Fla. 4th DCA 2012) (declining to apply the tipsy coachman doctrine and explaining that an appellate court should not ordinarily decide issues not ruled on by the trial court in the first instance).

Reversed and Remanded.

DAMOORGIAN, C.J., and MAY, J., concur.

All Citations

165 So.3d 749, 40 Fla. L. Weekly D1196

Footnotes

1 While we agree that some of Security First's arguments against the validity of the assignment probably cannot be resolved on a motion to dismiss, we interpret the trial court's ruling as being based exclusively on Security First's argument concerning the anti-assignment and loss payment provisions of the insurance policy. Moreover, in this case, in contrast to *Nextgen Restoration Inc. v. Citizens Property Ins. Corp.,* 126 So.3d 1255 (Fla. 2d DCA 2013), the policy was placed in the record, and it was incorporated by reference in the complaint, so the trial court was permitted to consider it in ruling on the legal issue that formed the basis for the dismissal.

2 A “chose in action” is the “right to bring an action to recover a debt, money, or thing.” *Black's Law Dictionary* (9th ed. 2009).

3 For the trial court's benefit on remand, we note that the Fifth District recently held that a post-loss assignee is not required to have an insurable interest at the time of loss. *See Accident Cleaners, Inc. v. Universal Ins. Co.,* ––– So.3d ––––, 2015 WL 1609973 (Fla. 5th DCA 2015). The court explained that the legislature, in enacting section 627.405, Florida Statutes, “did not state that it was displacing well-settled common law of (1) the free assignability of contractual rights to recover or (2) the inability for insurers to restrict post-loss assignments.” *Id.* at ––––, 2015 WL 1609973, at *2.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-25

KeyCite Yellow Flag - Negative Treatment
Disagreed With by Collins v. International Dairy Queen, Inc., M.D.Ga., October 7, 1997

124 F.3d 430
United States Court of Appeals,
Third Circuit.

QUEEN CITY PIZZA, INC.; Thomas C. Bolger; Scale Pizza, Inc.; Baughans, Inc.; Charles F. Buck; F.M. Pizza, Inc.; Robert S. Bigelow; Blue Earth Enterprises, Inc.; Kevin Bores; Davis Pizza Enterprises, Inc.; Diane A. Davis; Fisher Pizza, Inc.; James B. Fisher, Jr.; SEPCO, Inc.; S & S Pizza Corp.; G & L Pizza Co.; Stephen D. Gallup; Lugent Pizza, Inc.; Joseph J. Lugent; Billio's Pizza, Inc.; William J. Murtha; Spring Garden Pizza, Inc; Brad L. Walker; JRW Pizza, Inc.; James R. Wood, Individually and as Class Representatives of a Class Consisting of All Present and Certain Former Domino's Franchisees in the United States; International Franchise Advisory Council, Inc.,
v.
DOMINO'S PIZZA, INC.; Queen City Pizza, Inc.; Thomas C. Bolger; Scale Pizza, Inc.; Baughans, Inc.; Charles F. Buck; F.M. Pizza, Inc.; Robert S. Bigelow; Blue Earth Enterprises, Inc.; Kevin Bores; Davis Pizza Enterprises, Inc.; Diane A. Davis; Fisher Pizza, Inc.; James B. Fisher, Jr.; SEPCO, Inc.; S & S Pizza, Inc.; G & L Pizza, Inc.; Stephen D. Gallup; Lugent Pizza, Inc.; Joseph J. Lugent; Billio's Pizza, Inc.; William J. Murtha; Spring Garden Pizza, Inc.; Brad L. Walker; JRW Pizza, Inc.; James R. Wood; and International Franchise Advisory Council, Inc., Appellants.

No. 96–1638.
|
Argued Feb. 28, 1997.
|
Decided Aug. 27, 1997.

Synopsis

Pizza franchisees and related corporation brought action against franchisor for antitrust violations, breach of contract, and tortious interference with contract. The United States District Court for the Eastern District of Pennsylvania, J. Curtis Joyner, J., 922 F.Supp. 1055, dismissed, and franchisees appealed. The Court of Appeals, Scirica, Circuit Judge, held that: (1) ingredients, supplies, and materials used by and in operation of pizza franchise stores did not qualify as relevant market for purposes of monopolization, attempted monopolization, and restraint of trade claims, and (2) franchisor-approved dough did not qualify as separate market for purposes of tying claim.

Affirmed.

Lay, Circuit Judge, sitting by designation, filed dissenting opinion.

Rehearing Denied Oct. 27, 1997.

Attorneys and Law Firms

***432** Sheryl G. Snyder, (Argued), Brown, Todd & Hayburn, Louisville, KY, for Appellants.

Daniel F. Kolb, (Argued), Thomas P. Ogden, Davis, Polk & Wardwell, New York City, Laurence Z. Shiekman, ***433** Pepper, Hamilton & Scheetz, Philadelphia, PA, for Appellee.

Before: SCIRICA, ALITO and LAY, [*] Circuit Judges.

SCIRICA, Circuit Judge.

OPINION OF THE COURT

In this appeal, we must decide whether certain franchise tying restrictions support a claim for violation of federal antitrust laws. Eleven franchisees of Domino's Pizza stores and the International Franchise Advisory Council, Inc. filed suit against Domino's Pizza, Inc., alleging violations of federal antitrust laws, breach of contract, and tortious interference with contract. The district court dismissed the antitrust claims under Fed.R.Civ.P. 12(b)(6) for failure to state a claim for which relief can be granted, because the plaintiffs failed to allege a valid relevant market. The district court declined to exercise supplemental jurisdiction over the plaintiffs' remaining common law claims. *Queen City Pizza, Inc. v. Domino's Pizza, Inc.,* 922 F.Supp. 1055 (E.D.Pa.1996). We will affirm.

I. Facts and Procedural History

A.

Domino's Pizza, Inc. is a fast-food service company that sells pizza through a national network of over 4200 stores. Domino's Pizza owns and operates approximately 700 of these stores. Independent franchisees own and operate the remaining 3500. Domino's Pizza, Inc. is the second largest pizza company in the United States, with revenues in excess of $1.8 billion per year.

A franchisee joins the Domino's system by executing a standard franchise agreement with Domino's Pizza, Inc. Under the franchise agreement, the franchisee receives the right to sell pizza under the “Domino's” name and format. In return, Domino's Pizza receives franchise fees and royalties.

The essence of a successful nationwide fast-food chain is product uniformity and consistency. Uniformity benefits franchisees because customers can purchase pizza from any Domino's store and be certain the pizza will taste exactly like the Domino's pizza with which they are familiar. This means that individual franchisees need not build up their own good will. Uniformity also benefits the franchisor. It ensures the brand name will continue to attract and hold customers, increasing franchise fees and royalties. [1]

For these reasons, section 12.2 of the Domino's Pizza standard franchise agreement requires that all pizza ingredients, beverages, and packaging materials used by a Domino's franchisee conform to the standards set by Domino's Pizza, Inc. Section 12.2 also provides that Domino's Pizza, Inc. “may in our sole discretion require that ingredients, supplies and materials used in the preparation, packaging, and delivery of pizza be purchased exclusively from us or from approved suppliers or distributors.” Domino's Pizza reserves the right “to impose reasonable limitations on the number of approved suppliers or distributors of any product.” To enforce these rights, Domino's Pizza, Inc. retains the power to inspect franchisee stores and to test materials and ingredients. Section 12.2 is subject to a reasonableness clause providing that Domino's Pizza, Inc. must “exercise reasonable judgment with respect to all determinations to be made by us under the terms of this Agreement.”

Under the standard franchise agreement, Domino's Pizza, Inc. sells approximately 90% of the $500 million in ingredients and supplies used by Domino's franchisees. [2] These sales, worth some $450 million per year, form a significant part of Domino's Pizza, Inc.'s profits. Franchisees purchase only 10% of their ingredients and supplies from outside sources. With the exception of fresh dough, Domino's Pizza, Inc. does not manufacture ***434** the products it sells to franchisees. Instead, it purchases these products from approved suppliers and then resells them to the franchisees at a markup.

B.

The plaintiffs in this case are eleven Domino's franchisees and the International Franchise Advisory Council, Inc. (“IFAC”), a Michigan corporation consisting of approximately 40% of the Domino's franchisees in the United States, formed to promote their common interests. [3] The plaintiffs contend that Domino's Pizza, Inc. has a monopoly in “the $500 million aftermarket for sales of supplies to Domino's franchisees” and has used its monopoly power to unreasonably restrain trade, limit competition, and extract supra-competitive profits. Plaintiffs point to several actions by Domino's Pizza, Inc. to support their claims.

First, plaintiffs allege that Domino's Pizza, Inc. has restricted their ability to purchase competitively priced dough. Most franchisees purchase all of their fresh dough from Domino's Pizza, Inc. Plaintiffs here attempted to lower costs by making fresh pizza dough on site. They contend that in response, Domino's Pizza, Inc. increased processing fees and altered quality standards and inspection practices for store-produced dough, which eliminated all potential savings and financial incentives to make their own dough. Plaintiffs also allege Domino's Pizza, Inc. prohibited stores that produce dough from selling their dough to other franchisees, even though the dough-producing stores were willing to sell dough at a price 25% to 40% below Domino's Pizza, Inc.'s price.

Next, plaintiffs object to efforts by Domino's Pizza, Inc. to block IFAC's attempt to buy less expensive ingredients and supplies from other sources. In June 1994, IFAC entered into a purchasing agreement with FoodService Purchasing Cooperative, Inc. (FPC). Under the agreement, FPC was appointed the purchasing agent for IFAC-member Domino's franchisees. FPC was charged with developing a cooperative purchasing plan under which participating franchisees could obtain supplies and ingredients at reduced cost from suppliers

other than Domino's Pizza, Inc. Plaintiffs contend that when Domino's Pizza, Inc. became aware of these efforts, it intentionally issued ingredient and supply specifications so vague that potential suppliers could not provide FPC with meaningful price quotations.

Plaintiffs also allege Domino's Pizza entered into exclusive dealing arrangements with several franchisees in order to deny FPC access to a pool of potential buyers sufficiently large to make the alternative purchasing scheme economically feasible. In addition, plaintiffs contend Domino's Pizza, Inc. commenced anti-competitive predatory pricing to shut FPC out of the market. For example, they maintain that Domino's Pizza, Inc. lowered prices on many ingredients and supplies to a level competitive with FPC's prices and then recouped lost profits by raising the price on fresh dough, which FPC could not supply. Further, plaintiffs contend Domino's Pizza, Inc. entered into exclusive dealing arrangements with the only approved suppliers of ready-made deep dish crusts and sauce. Under these agreements, the suppliers were obligated to deliver their entire output to Domino's Pizza, Inc. Plaintiffs allege the purpose of these agreements was to prevent FPC from purchasing these critical pizza components for resale to franchisees.

Finally, plaintiffs allege Domino's Pizza, Inc. refused to sell fresh dough to franchisees unless the franchisees purchased other ingredients and supplies from Domino's Pizza, Inc. As a result of these and other alleged practices, plaintiffs maintain that each franchisee store now pays between $3000 and $10,000 more per year for ingredients and supplies than it would in a competitive market. Plaintiffs allege these costs are passed on to consumers.

C.

As noted, eleven Domino's franchisees and IFAC filed an amended complaint in United ***435** States District Court for the Eastern District of Pennsylvania against Domino's Pizza, Inc. seeking declaratory, injunctive, and compensatory relief under §§ 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2. The plaintiffs also sought damages for breach of contract, breach of implied covenants of good faith and fair dealing, and tortious interference with contractual relations.[4]

Domino's Pizza, Inc. moved to dismiss the antitrust claims for failure to state a claim, contending the plaintiffs failed to allege a "relevant market," a basic pleading requirement for claims under both § 1 and § 2 of the Sherman antitrust act. They maintained that the relevant market defined in the complaint—the "market" in Domino's-approved ingredients and supplies used by Domino's Pizza franchisees—was invalid as a matter of law because the boundaries of the proposed relevant market were defined by contractual terms contained in the franchise agreement, and not measured by cross-elasticity of demand or product interchangeability.

The district court granted defendant's motion to dismiss with prejudice plaintiffs' federal antitrust claims. The district court observed that "in order to state a Sherman Act claim under either § 1 or § 2, a plaintiff must identify the relevant product and geographic markets and allege that the defendant exercises market power within those markets." *Queen City Pizza, Inc. v. Domino's Pizza, Inc.,* 922 F.Supp. 1055, 1060 (E.D.Pa.1996). Noting that plaintiffs did "not explicitly identify the relevant product and geographic markets in their amended complaint," the court said that "it is clear from the context, and confirmed in their memorandum in opposition to the instant motion, that Plaintiffs consider the relevant product market to be the market for ingredients and supplies among Domino's franchisees." *Id.* at 1061. Rejecting this concept of the relevant market, the court held that "antitrust claims predicated upon a 'relevant market' defined by the bounds of a franchise agreement are not cognizable." *Id.* at 1063. The court noted that Domino's Pizza, Inc.'s power to force plaintiffs to purchase ingredients and supplies from them stemmed "not from the unique nature of the product or from its market share in the fast food franchise business, but from the franchise agreement." *Id.* at 1062. For that reason, plaintiffs' claims "implicate principles of contract, and are not the concern of the antitrust laws." *Id.* The district court also held plaintiffs had failed adequately to allege harm to competition, "a bedrock premise of antitrust law." *Id.* at 1063. Because plaintiffs failed to assert a cognizable antitrust claim and there was neither diversity among the parties nor special circumstances justifying exercise of supplemental jurisdiction, the court dismissed without prejudice plaintiffs' common law claims for lack of subject matter jurisdiction. *Id.* at 1063–64.

The district court granted plaintiffs leave to file an amended complaint to cure the jurisdictional pleading deficiencies in their state law claims. Plaintiffs decided not to replead their state law claims. Instead, they sought to amend their complaint for a second time in an attempt to state a valid federal antitrust claim. The district court denied their motion, noting that though the plaintiffs' proposed second

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

amended complaint would cure the failure to plead harm to competition, it would not cure the failure to allege a valid relevant market. The court stated: "Plaintiffs do not and cannot purchase ingredients and supplies from alternative suppliers not because Domino's dominates the ingredient and supply market or because Defendant is the market's only supplier, but because the franchisee-plaintiffs are contractually bound to purchase only from suppliers approved by Defendant. It is economic power resulting from the franchise agreement, therefore, and not market power, that defines the 'relevant market' Plaintiffs allege in support of their antitrust claims." The district court rejected plaintiffs' argument that a different result was required under the Supreme Court's decision in *Eastman Kodak Co. v. Image Technical Services, Inc.,* 504 U.S. 451, 112 S.Ct. 2072, 119 L.Ed.2d 265 (1992). This appeal followed.

***436** II. Jurisdiction and Standard of Review

The district court had jurisdiction over the antitrust counts under 15 U.S.C. §§ 15 and 26 and 28 U.S.C. §§ 1331 and 1337. It declined to exercise supplemental jurisdiction over the common law counts. We have jurisdiction under 28 U.S.C. § 1291. Our review of the district court's dismissal under Fed.R.Civ.P. 12(b)(1) and 12(b)(6) is plenary. *Stehney v. Perry,* 101 F.3d 925 (3d Cir.1996).

III. Discussion

Plaintiffs assert six distinct antitrust claims on appeal. First, plaintiffs allege Domino's Pizza, Inc. has monopolized the market in pizza supplies and ingredients for use in Domino's stores, in violation of § 2 of the Sherman Act, 15 U.S.C. § 2. In support of this contention, plaintiffs allege Domino's Pizza, Inc. has sufficient market power to control prices and exclude competition in this market. Second, plaintiffs contend Domino's Pizza, Inc. has attempted to monopolize the market for Domino's pizza supplies and ingredients, in violation of § 2 of the Sherman Act. Third, plaintiffs allege Domino's Pizza, Inc.'s exclusive dealing arrangements have unreasonably restrained trade in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. Fourth, plaintiffs allege Domino's Pizza, Inc. imposed an unlawful tying arrangement [5] by requiring franchisees to buy ingredients and supplies from them as a condition of obtaining fresh dough, in violation of the Sherman Act § 1, 15 U.S.C. § 1. Fifth, plaintiffs allege Domino's Pizza, Inc. imposed an unlawful tying arrangement by requiring franchisees to buy ingredients and supplies "as a condition of their continued enjoyment of rights and services under their Standard Franchise Agreement," in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. Sixth, plaintiffs allege Domino's Pizza, Inc. has monopoly power in a relevant "market for reasonably interchangeable franchise opportunities facing prospective franchisees," in violation of § 2 of the Sherman Act, 15 U.S.C. § 2. This last claim was not raised before the district court.

As we have noted, the district court held that none of the plaintiffs' antitrust claims was cognizable under federal law. We will analyze each claim in turn.

A.

As a threshold matter, plaintiffs argue that "relevant market determinations are inherently fact intensive, and therefore are inappropriate for disposition on a Rule 12(b)(6) motion." (Appellant's brief at 16). It is true that in most cases, proper market definition can be determined only after a factual inquiry into the commercial realities faced by consumers. *See Eastman Kodak Co. v. Image Technical Services, Inc.,* 504 U.S. 451, 482, 112 S.Ct. 2072, 2090, 119 L.Ed.2d 265 (1992). Plaintiffs err, however, when they try to turn this general rule into a *per se* prohibition against dismissal of antitrust claims for failure to plead a relevant market under Fed.R.Civ.P. 12(b)(6).

Plaintiffs have the burden of defining the relevant market. *Pastore v. Bell Telephone Co. of Pennsylvania,* 24 F.3d 508, 512 (3d Cir.1994); *Tunis Bros. Co., Inc. v. Ford Motor Co.,* 952 F.2d 715, 726 (3d Cir.1991). "The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe Co. v. U.S.,* 370 U.S. 294, 325, 82 S.Ct. 1502, 1523, 8 L.Ed.2d 510 (1962); *Tunis Brothers,* 952 F.2d at 722 (same). Where the plaintiff fails to define its proposed relevant market with reference to the rule of reasonable interchangeability and cross-elasticity of demand, or alleges a proposed relevant market that clearly does not encompass all interchangeable substitute products even when all factual inferences are granted in plaintiff's favor, the relevant market is legally insufficient and a motion to dismiss may be granted. *See, e.g., TV Communications Network, Inc. v. Turner Network Television, Inc.,* 964 F.2d 1022, 1025 (10th Cir.1992) (affirming district ***437** court's dismissal

of claim for failure to plead a relevant market; proposed relevant market consisting of only one specific television channel defined too narrowly); *Tower Air, Inc. v. Federal Exp. Corp.,* 956 F.Supp. 270 (E.D.N.Y.1996) ("Because a relevant market includes all products that are reasonably interchangeable, plaintiff's failure to define its market by reference to the rule of reasonable interchangeability is, standing alone, valid grounds for dismissal."); *B.V. Optische Industrie De Oude Delft v. Hologic, Inc.,* 909 F.Supp. 162 (S.D.N.Y.1995) (dismissal for failure to plead a valid relevant market; plaintiffs failed to define market in terms of reasonable interchangeability or explain rationale underlying narrow proposed market definition); *Re–Alco Industries, Inc. v. Nat'l Center for Health Educ., Inc.,* 812 F.Supp. 387 (S.D.N.Y.1993) (dismissal for failure to plead a valid relevant market; plaintiff failed to allege that specific health education product was unique or explain why product was not part of the larger market for health education materials); *E. & G. Gabriel v. Gabriel Bros., Inc.,* No. 93 Civ. 0894, 1994 WL 369147 (S.D.N.Y.1994) (dismissal for failure to plead valid relevant market; proposed relevant market legally insufficient because it clearly contained varied items with no cross-elasticity of demand).

B.

Plaintiffs allege Domino's Pizza, Inc. has willfully acquired and maintained a monopoly in the market for ingredients, supplies, materials and distribution services used in the operation of Domino's stores, in violation of § 2 of the Sherman Act, 15 U.S.C. § 2. Section 2 sanctions those "who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations." "The offense of monopoly under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.,* 472 U.S. 585, 596 n. 19, 105 S.Ct. 2847, 2854 n. 19, 86 L.Ed.2d 467 (1985) (quoting *United States v. Grinnell Corp.,* 384 U.S. 563, 570–71, 86 S.Ct. 1698, 1703–04, 16 L.Ed.2d 778 (1966)). *See also Ideal Dairy Farms, Inc. v. John Labatt, Ltd.,* 90 F.3d 737, 749 (3d Cir.1996) (same); *Bonjorno v. Kaiser Aluminum & Chemical Corp.,* 752 F.2d 802, 808 (3d Cir.1984) (same).

The district court dismissed plaintiffs' § 2 monopoly claims for failure to plead a valid relevant market. Plaintiffs suggest the "ingredients, supplies, materials, and distribution services used by and in the operation of Domino's pizza stores" constitutes a relevant market for antitrust purposes. We disagree.

As we have noted, the outer boundaries of a relevant market are determined by reasonable interchangeability of use. *Eastman Kodak Co. v. Image Technical Services, Inc.,* 504 U.S. 451, 482, 112 S.Ct. 2072, 2090, 119 L.Ed.2d 265 (1992); *Brown Shoe Co. v. U.S.,* 370 U.S. 294, 325, 82 S.Ct. 1502, 1523, 8 L.Ed.2d 510 (1962); *Tunis Brothers Co., Inc. v. Ford Motor Co.,* 952 F.2d 715, 722 (3d Cir.1991). "Interchangeability implies that one product is roughly equivalent to another for the use to which it is put; while there may be some degree of preference for the one over the other, either would work effectively. A person needing transportation to work could accordingly buy a Ford or a Chevrolet automobile, or could elect to ride a horse or bicycle, assuming those options were feasible." *Allen–Myland, Inc. v. International Business Machines Corp.,* 33 F.3d 194, 206 (3d Cir.1994) (internal quotations omitted). When assessing reasonable interchangeability, "[f]actors to be considered include price, use, and qualities." *Tunis Brothers,* 952 F.2d at 722. Reasonable interchangeability is also indicated by "cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe Co. v. U.S.,* 370 U.S. 294, 325, 82 S.Ct. 1502, 1523, 8 L.Ed.2d 510 (1962). As we explained in *Tunis Brothers Co., Inc. v. Ford Motor Co.,* 952 F.2d 715, 722 (3d Cir.1991), "products in a relevant market [are] characterized by a cross-elasticity of demand, in other words, ***438** the rise in the price of a good within a relevant product market would tend to create a greater demand for other like goods in that market." *Tunis Brothers,* 952 F.2d at 722.[6]

Here, the dough, tomato sauce, and paper cups that meet Domino's Pizza, Inc. standards and are used by Domino's stores are interchangeable with dough, sauce and cups available from other suppliers and used by other pizza companies. Indeed, it is the availability of interchangeable ingredients of comparable quality from other suppliers, at lower cost, that motivates this lawsuit. Thus, the relevant market, which is defined to include all reasonably interchangeable products, cannot be restricted solely to those products currently approved by Domino's Pizza, Inc. for use by Domino's franchisees. For that reason, we must reject plaintiffs' proposed relevant market.

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Of course, Domino's-approved pizza ingredients and supplies differ from other available ingredients and supplies in one crucial manner. Only Domino's-approved products may be used by Domino's franchisees without violating section 12.2 of Domino's standard franchise agreement. Plaintiffs suggest that this difference is sufficient by itself to create a relevant market in approved products. We disagree. The test for a relevant market is not commodities reasonably interchangeable by a particular plaintiff, but "commodities reasonably interchangeable by consumers for the same purposes." *United States v. E.I. du Pont de Nemours & Co.,* 351 U.S. 377, 395, 76 S.Ct. 994, 1007, 100 L.Ed. 1264 (1956); *Tunis Brothers,* 952 F.2d at 722. A court making a relevant market determination looks not to the contractual restraints assumed by a particular plaintiff when determining whether a product is interchangeable, but to the uses to which the product is put by consumers in general. Thus, the relevant inquiry here is not whether a Domino's franchisee may reasonably use both approved or non-approved products interchangeably without triggering liability for breach of contract, but whether pizza makers in general might use such products interchangeably. Clearly, they could. Were we to adopt plaintiffs' position that contractual restraints render otherwise identical products non-interchangeable for purposes of relevant market definition, any exclusive dealing arrangement, output or requirement contract, or franchise tying agreement would support a claim for violation of antitrust laws. Perhaps for this reason, no court has defined a relevant product market with reference to the particular contractual restraints of the plaintiff. [7] Indeed, the only cases we have found involving similar claims rejected plaintiffs' position as a matter of law. *See United Farmers Agents Ass'n, Inc. v. Farmers Ins. Exchange,* 89 F.3d 233 (5th Cir.1996) ("Economic power derived from contractual arrangements such as franchises or in this case, the agents' contract with Farmers', has nothing to do with market power, ultimate consumers' welfare, or antitrust.") (internal citation and quotation omitted), *cert. denied,* 519 U.S. 1116, 117 S.Ct. 960, 136 L.Ed.2d 846 (1997); *Ajir v. Exxon Corp.,* No. C 93–20830, 1995 WL 429234, *3 (N.D.Ca.) ("Just because Exxon's direct serve dealers may contractually purchase gasoline from only one source—Exxon—does not mean that the relevant market is Exxon gasoline"; the correct relevant market is all gasoline). *See also Seagood Trading Corp. v. Jerrico, Inc.,* 924 F.2d 1555, 1570 n. 39 (11th Cir.1991) ***439** (declining to reach issue but noting the district court rejected plaintiffs' claim that proposed market for sales of supplies to Long John Silver's fast food stores was a relevant market for antitrust purposes).

Plaintiffs argue that the Supreme Court's decision defining relevant markets in *Eastman Kodak Co. v. Image Technical Services, Inc.,* 504 U.S. 451, 112 S.Ct. 2072, 119 L.Ed.2d 265 (1992) requires a different outcome. We disagree.

In *Kodak,* the Supreme Court observed that a market is defined with reference to reasonable interchangeability. *Kodak,* 504 U.S. at 482, 112 S.Ct. at 2090. The Court held that the market for repair parts and services for Kodak photocopiers was a valid relevant market because repair parts and services for Kodak machines are not interchangeable with the service and parts used to fix other copiers. *Id.* Plaintiffs suggest that *Kodak* supports its proposed relevant market because it indicates that in some circumstances, a single brand of a product or service may constitute a relevant market. This is correct where the commodity is unique, and therefore not interchangeable with other products. But here, it is uncontested that contractual restraints aside, the sauce, dough, and other products and ingredients approved for use by Domino's franchisees are interchangeable with other items available on the market.

Plaintiffs contend that they face information and switching costs that "lock them in" to their position as Domino's franchisees, making it economically impracticable for them to abandon the Domino's system and enter a different line of business. They argue that under *Kodak,* the fact that they are "locked in" supports their claim that an "aftermarket" for Domino's-approved supplies is a relevant market for antitrust purposes. We believe plaintiffs misread *Kodak.*

The defendants in *Kodak* argued that there was no relevant market in Kodak repair parts, even if they were unique and non-interchangeable with other repair parts, because of cross-elasticity of demand between parts prices and copier sales. If the price of parts were raised too high, defendants contended, it would decrease demand for copiers. [8] The Court held that whether there was cross-elasticity of demand between parts and copiers was, in this case, a factual question that could not be determined as a matter of law. The Court reached this conclusion because switching and information costs arise when one purchases an expensive piece of equipment like a copier. In some circumstances, these costs might create an economic lock-in that could reduce or eliminate the cross-elasticity of demand between copiers and the repair parts for those copiers.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Kodak, we believe, held that a plaintiff's proposed relevant market in a unique and non-interchangeable derivative product or service cannot be defeated on summary judgment by a defendant's assertion that the proposed derivative market is cross-elastic with the primary market, if there is a reasonable possibility that the defendant's assertion about cross-elasticity is factually incorrect. But *Kodak* does not hold that the existence of information and switching costs alone, such as those faced by the Domino's franchisees, [9] renders an otherwise invalid relevant market valid. [10] In *Kodak,* the repair parts ***440** and service were unique and there was a question of fact about cross-elasticity. Judgment as a matter of law was therefore inappropriate. Here, it is uncontroverted that Domino's approved supplies and ingredients are fully interchangeable in all relevant respects with other pizza supplies outside the proposed relevant market. For this reason, dismissal of the plaintiffs' claim as a matter of law is appropriate.

Kodak is distinguishable from the present appeal in other important respects. The *Kodak* case arose out of concerns about unilateral changes in Kodak's parts and repairs policies. When the copiers were first sold, Kodak relied on purchasers to obtain service from independent service providers. Later, it chose to use its power over the market in unique replacement parts to squeeze the independent service providers out of the repair market and to force copier purchasers to obtain service directly from Kodak, at higher cost. Because this change in policy was not foreseen at the time of sale, buyers had no ability to calculate these higher costs at the time of purchase and incorporate them into their purchase decision. In contrast, plaintiffs here knew that Domino's Pizza retained significant power over their ability to purchase cheaper supplies from alternative sources because that authority was spelled out in detail in section 12.2 of the standard franchise agreement. Unlike the plaintiffs in *Kodak,* the Domino's franchisees could assess the potential costs and economic risks at the time they signed the franchise agreement. The franchise transaction between Domino's Pizza, Inc. and plaintiffs was subjected to competition at the pre-contract stage. That cannot be said of the conduct challenged in *Kodak* because it was not authorized by contract terms disclosed at the time of the original transaction. Kodak's sale of its product involved no contractual framework for continuing relations with the purchaser. But a franchise agreement regulating supplies, inspections, and quality standards structures an ongoing relationship between franchisor and franchisee designed to maintain good will. These differences between the *Kodak* transaction and franchise transactions are compelling. [11]

Plaintiffs also contend that *Virtual Maintenance, Inc. v. Prime Computer, Inc.,* 11 F.3d 660 (6th Cir.1993), supports their claim that the boundaries of a relevant market may be defined by contract. In *Virtual Maintenance,* Ford Motor Co. granted Prime Computer an exclusive right to market Ford designed software and software revisions that automobile design companies must use to design cars for Ford. Prime Computer sold the software revisions only in a package with uncompetitive hardware maintenance services. The Court of Appeals for the Sixth Circuit held that Prime could not legally exercise its monopoly power over software revisions to force customers to buy unwanted hardware maintenance contracts. Plaintiffs note that Prime's *de facto* monopoly power over software stemmed from a contract with Ford, which they argue implies that the boundaries of a market may be defined by contract. But Prime had a monopoly because it possessed a unique product that no one else sold. Since the product was unique, and not interchangeable with any other products, it constituted its own relevant market for antitrust purposes. By contrast, Domino's does not sell a unique product or service. Franchisees must buy Domino's-approved supplies and ingredients not because they are unique, but because they are obligated by contract to do so.

Were we to accept plaintiffs' relevant market, virtually all franchise tying agreements requiring the franchisee to purchase inputs such as ingredients and supplies from the franchisor would violate antitrust law. Courts and legal commentators have long recognized that franchise tying contracts are an essential and important aspect of the franchise form of business organization because they reduce agency costs and prevent franchisees from freeriding—offering products of ***441** sub-standard quality insufficient to maintain the reputational value of the franchise product while benefitting from the quality control efforts of other actors in the franchise system. [12] Franchising is a bedrock of the American economy. More than one third of all dollars spent in retailing transactions in the United States are paid to franchise outlets. [13] We do not believe the antitrust laws were designed to erect a serious barrier to this form of business organization. [14]

The purpose of the Sherman Act "is not to protect businesses from the working of the market; it is to protect the public from the failure of the market." *Spectrum Sports, Inc. v. McQuillan,*

506 U.S. 447, 458, 113 S.Ct. 884, 891, 122 L.Ed.2d 247 (1993). Here, plaintiffs' acceptance of a franchise package that included purchase requirements and contractual restrictions is consistent with the existence of a competitive market in which franchises are valued, in part, according to the terms of the proposed franchise agreement and the availability of alternative franchise opportunities. Plaintiffs need not have become Domino's franchisees. If the contractual restrictions in section 12.2 of the general franchise agreement were viewed as overly burdensome or risky at the time they were proposed, plaintiffs could have purchased a different form of restaurant, or made some alternative investment. [15] They chose not to do so. Unlike the plaintiffs in *Kodak,* plaintiffs here must purchase products from Domino's Pizza not because of Domino's market power over a unique product, but because they are bound by contract to do so. If Domino's Pizza, Inc. acted unreasonably when, under the franchise agreement, it restricted plaintiffs' ability to purchase supplies from other sources, plaintiffs' remedy, if any, is in contract, not under the antitrust laws. [16]

For these reasons, we agree with the district court that plaintiffs have not pleaded a valid relevant market. [17]

*442 C.

Plaintiffs' claim for attempt to monopolize fails for the same reasons. To prevail on an attempted monopolization claim under § 2 of the Sherman Act, "a plaintiff must prove that the defendant (1) engaged in predatory or anticompetitive conduct with (2) specific intent to monopolize and with (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc. v. McQuillan,* 506 U.S. 447, 456, 113 S.Ct. 884, 890, 122 L.Ed.2d 247 (1993). *Ideal Dairy Farms, Inc. v. John Labatt, Ltd.,* 90 F.3d 737, 750 (3d Cir.1996); *Advo, Inc. v. Philadelphia Newspapers, Inc.,* 51 F.3d 1191, 1197 (3d Cir.1995). In order to determine whether there is a dangerous probability of monopolization, a court must inquire "into the relevant product and geographic market and the defendant's economic power in that market." *Spectrum Sports, Inc. v. McQuillan,* 506 U.S. 447, 459, 113 S.Ct. 884, 892, 122 L.Ed.2d 247 (1993); *Ideal Dairy Farms* at 750; *Pastore v. Bell Telephone Co. of Pennsylvania,* 24 F.3d 508, 512 (3d Cir.1994).

Plaintiffs' attempted monopoly claim is predicated on the identical proposed relevant market underlying its monopoly claim: a market in the ingredients, supplies, and materials used by Domino's pizza stores. Because the products within this proposed market are interchangeable with other products outside of the proposed market, the claim was properly dismissed.

D.

Plaintiffs allege exclusive dealing arrangements entered into by Domino's Pizza, Inc. have unreasonably restrained trade in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. Section 1 of the Sherman Act provides: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal." 15 U.S.C. § 1.

To establish a section 1 violation for unreasonable restraint of trade, a plaintiff must prove (1) concerted action by the defendants; (2) that produced anti-competitive effects within the relevant product and geographic markets; (3) that the concerted action was illegal; and (4) that the plaintiff was injured as a proximate result of the concerted action. *Mathews v. Lancaster General Hospital,* 87 F.3d 624, 639 (3d Cir.1996); *Orson Inc. v. Miramax Film Corp.,* 79 F.3d 1358, 1366 (3d Cir.1996); *Petruzzi's IGA Supermarkets, Inc. v. Darling–Delaware Co., Inc.,* 998 F.2d 1224, 1229 (3d Cir.1993).

Plaintiffs allege defendant's actions caused anticompetitive effects within the market for ingredients and supplies used by Domino's pizza stores. Again, this claim fails because the products within the proposed market are interchangeable with products outside the proposed market. [18]

E.

Plaintiffs allege Domino's Pizza, Inc. imposed an unlawful tying arrangement by requiring franchisees to buy ingredients and supplies from them as a condition of obtaining Domino's Pizza fresh dough, in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. "In a tying arrangement, the seller sells one item, known as the tying product, on the condition that the buyer also purchases another item, known as the tied product." *Allen–Myland, Inc. v. International Business Machines Corp.,* 33 F.3d 194, 200 (3d Cir.1994). "[T]he antitrust concern over tying arrangements is limited to those situations in which the seller can exploit its power in the market for the

tying product to force buyers to purchase the tied product when they otherwise ***443** would not, thereby restraining competition in the tied product market." *Id.* "Even if a seller has obtained a monopoly in the tying product legitimately (as by obtaining a patent), courts have seen the expansion of that power to other product markets as illegitimate and competition suppressing." *Town Sound and Custom Tops, Inc. v. Chrysler Motors Corp.,* 959 F.2d 468, 475 (3d Cir.1992). "The first inquiry in any § 1 tying case is whether the defendant has sufficient market power over the tying product, which requires a finding that two separate product markets exist and a determination precisely what the tying and tied products markets are." *Allen–Myland,* 33 F.3d at 200–201.

Here, plaintiffs allege Domino's Pizza, Inc. used its power in the purported market for Domino's-approved dough to force plaintiffs to buy unwanted ingredients and supplies from them. This claim fails because the proposed tying market—the market in Domino's-approved dough—is not a relevant market for antitrust purposes. Domino's dough is reasonably interchangeable with other brands of pizza dough, and does not therefore constitute a relevant market of its own. All that distinguishes this dough from other brands is that a Domino's franchisee must use it or face a suit for breach of contract. As we have noted above, the particular contractual restraints assumed by a plaintiff are not sufficient by themselves to render interchangeable commodities non-interchangeable for purposes of relevant market definition. If Domino's had market power in the overall market for pizza dough and forced plaintiffs to purchase other unwanted ingredients to obtain dough, plaintiffs might possess a valid tying claim. But where the defendant's "power" to "force" plaintiffs to purchase the alleged tying product stems not from the market, but from plaintiffs' contractual agreement to purchase the tying product, no claim will lie. For that reason, plaintiffs' claim was properly dismissed.

F.

Plaintiffs allege Domino's Pizza, Inc. imposed an unlawful tie-in arrangement by requiring franchisees to buy ingredients and supplies "as a condition of their continued enjoyment of rights and services under their Standard Franchise Agreement," in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. This claim is meritless. Though plaintiffs complain of an illegal tie-in arrangement, they have failed to point to any particular tying product or service over which Domino's Pizza, Inc, has market power. Domino's Pizza's control over plaintiffs' "continued enjoyment of rights and services under their Standard Franchise Agreement" is not a "market." Rather, it is a function of Domino's contractual powers under the franchise agreement to terminate the participation of franchisees in the franchise system if they violate the agreement. Because plaintiffs failed to plead any relevant tying market, the claim was properly dismissed.

G.

On appeal, the plaintiffs advance a new claim based on a different relevant market theory—that Domino's has a monopoly in a relevant market comprised of pizza franchise opportunities of the type that Domino's Pizza, Inc. offers. Plaintiffs raise this new theory, which the district court did not address, in the hopes of obtaining a remand.

Plaintiffs' argument that Domino's Pizza has monopolized a relevant market comprised of franchise opportunities of a particular sort was not raised or mentioned in their complaint, first amended complaint, memorandum of law in support of their motion for leave to file a second amended complaint, or in the "claims for relief" section of the proposed second amended complaint. When the district court denied plaintiffs leave to file a second amended complaint, on grounds of futility, it had no idea that plaintiffs intended or desired to raise such a claim. "This court has consistently held that it will not consider issues that are raised for the first time on appeal." *Harris v. City of Philadelphia,* 35 F.3d 840, 845 (3d Cir.1994).

Nonetheless, plaintiffs argue that this claim was raised before the district court. In support of this contention, they note that facts which might support such a claim were ***444** pleaded in paragraphs 60 and 65 of their proposed second amended complaint. Though we construe pleadings liberally, plaintiffs have a duty to make the district court aware that they intend to rely on a particular relevant market theory. This is particularly true in a complex case like this one, where plaintiffs bring multiple antitrust claims based on multiple and alternative relevant market theories. *See Pastore v. Bell Telephone Co. of Pennsylvania,* 24 F.3d 508, 513 (3d Cir.1994) (plaintiff bound by relevant market theory raised before district court); *TV Communications Network. Inc. v. Turner Network Television, Inc.,* 964 F.2d 1022, 1025 (10th Cir.1992) (same); *Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.,* 637 F.2d 105, 117 (3d Cir.1980) (same). We do not believe a fleeting reference in a proposed second amended complaint to facts that might

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

support a proposed relevant market is sufficient, on its own, to preserve that relevant market theory for appellate review. *See Frank v. Colt Industries, Inc.,* 910 F.2d 90, 100 (3d Cir.1990) (issues not raised before district court are waived on appeal; fleeting reference to issue before district court insufficient to preserve it for appellate review). "Particularly where important and complex issues of law are presented, a far more detailed exposition of argument is required to preserve an issue." *Id.* at 100. Because this claim was not properly raised before the district court and is not properly before us, we decline to address it. *See generally Salvation Army v. Department of Community Affairs of State of N.J.,* 919 F.2d 183, 196 (3d Cir.1990) ("The matter of what questions may be taken up and resolved for the first time on appeal is one left primarily to the discretion of the courts of appeals, to be exercised on the facts of each case.").

H.

Plaintiffs also contend the district court held that the availability of contract remedies prohibited recovery under antitrust laws. But this misstates the district court's holding. The district court held that Domino's Pizza's ability to block franchisees from purchasing ingredients from other sources stemmed from its exercise of contractual powers, not market power, and the remedy for this problem lies, if at all, under contract law. The court did not say that as a matter of law the availability of common law remedies prohibits recovery under an antitrust theory. We see no error.

I.

The district court declined to exercise supplemental jurisdiction over the plaintiffs' remaining state law contract claims. This decision is committed to the sound discretion of the district court. *Stehney v. Perry,* 101 F.3d 925, 939 (3d Cir.1996); *Growth Horizons, Inc. v. Delaware County, Pa.,* 983 F.2d 1277, 1284–85 (3d Cir.1993). Because all federal claims were correctly dismissed and dismissal of the remaining contract claims would not be unfair to the litigants or result in waste of judicial resources, we see no abuse of discretion.

IV.

For the foregoing reasons, we will affirm the judgment of the district court.

LAY, Circuit Judge, dissenting.
I respectfully dissent.

The district court, at the pleading stage, dismissed plaintiffs' complaint alleging violations under § 1 and § 2 of the Sherman Antitrust Act holding that plaintiffs failed to allege a relevant market. The issue is complex. Judge Scirica's opinion is logically reasoned. Our differences lie in the interpretation and application of the Supreme Court's recent opinion in *Eastman Kodak Co. v. Image Technical Servs., Inc.,* 504 U.S. 451, 112 S.Ct. 2072, 119 L.Ed.2d 265 (1992). I respectfully submit, for the reasons that follow, that the district court's opinion in this case rests on several incorrect hypotheses. To the extent that the majority adopts the district court's rationale, I dissent.

The district court rejected as a matter of law the plaintiffs' alleged relevant market, that of the derivative aftermarket for ingredients and supplies among Domino's Pizza, Inc. ("DPI")'s franchisees. The district court found that "[t]he economic power DPI possesses results not from the unique nature of ***445** the product or from its market share in the fast food franchise business, but from the franchise agreement." [1]

The plaintiffs allege that DPI has harmed the competitive process by "foreclos [ing] interbrand competition in the market for distributing approved Ingredients and Supplies to Domino's franchisees." The plaintiffs argue that DPI prevented a franchise cooperative and other distributors of ingredients and supplies from entering that market. By stopping any interbrand competition for ingredients and supplies for DPI franchisees, DPI, according to the pleadings, has excluded other potential distributors, and thereby preempted market forces from disciplining the sale of ingredients and supplies.

Interchangeability

In adopting the district court's approach to relevant market definition, the majority reasons that all ingredients and supplies, whether or not approved by DPI, are interchangeable for making pizzas generally and therefore must be included within the relevant market. Kodak made a similar argument. As in *Kodak,* this ignores

the reality that there are no substitutes for ingredients and supplies sold only by DPI. The majority's approach to the interchangeability concept is not faithful to the purpose of interchangeability analysis or the Supreme Court's understanding of market definition and power. The purpose of analyzing interchangeability is to find competing products which are reasonable substitutes and thereby prevent market power.[2] In *Kodak,* the question was whether the cross-elasticity of demand between the equipment market and the derivative aftermarkets for parts and service was sufficient to deprive Kodak of market power. Our question is whether the interchangeability of, or cross-elasticity of demand between, DPI-approved ingredients and supplies and other ingredients and supplies is sufficient to make the alleged relevant market invalid. The issue, whether under the framework of market power as it was in *Kodak,* or as market definition as here, is whether competition from other providers of ingredients and supplies for pizzas will restrain the power of DPI over ingredients and supplies it sells to franchisees. *See Kodak,* 504 U.S. at 469 n. 15. The plaintiffs allege not only that they are limited to buying ingredients and supplies from DPI, but also that information and switching costs prevented them from anticipating and being able to respond to DPI's power to substantially raise price for the ingredients and supplies. They allege that competition from independent providers of ingredients and supplies does not restrain DPI's power in the aftermarket for ingredients and supplies, and therefore ingredients and supplies not approved by DPI need not be included in the relevant market.[3]

***446** *Information and Switching Costs*

A closely related problem with the district court's opinion is its scant treatment of information and switching costs and their relevance to defining a valid relevant market. The plaintiffs argue that they have experienced information and switching costs which have prevented them from anticipating or responding to the price increases for ingredients and supplies from DPI. They argue that these information and switching costs create a "lock-in" which makes the aftermarket for DPI-approved ingredients and supplies the relevant market. Specifically, the imperfect information they proffer is that the franchisees "could not foresee that Domino's would not follow the policy represented in its Offering Circular and would, instead, commence excluding potential suppliers in order to foreclose competition in the aftermarket." They suggest switching costs arise from sunk costs in the franchise, limits on franchisees's ability to sell their franchise, and noncompetition covenants in the Standard Franchise Agreement.

An important part of the Supreme Court's decision in *Kodak* that the plaintiffs presented a triable claim was that "there is a question of fact whether information costs and switching costs foil the simple assumption that the equipment and service markets act as pure complements to one another." *Kodak,* 504 U.S. at 477, 112 S.Ct. at 2087. In fact, other circuit courts have held that the presence of these market imperfections was the crucial factor in *Kodak,* and that had Kodak's policy been known at the time businesses bought copiers from Kodak, the result would have been different.[4] *See PSI Repair Servs., Inc. v. Honeywell, Inc.,* 104 F.3d 811, 820 (6th Cir.1997) ("We likewise agree that the change in policy in *Kodak* was the crucial factor in the Court's decision. By changing its policy after its customers were 'locked in,' Kodak took advantage of the fact that its customers lacked the information to anticipate this change."), *cert. denied,* 520 U.S. 1265, 117 S.Ct. 2434, 138 L.Ed.2d 195; *see also Digital Equip. Corp. v. Uniq Digital Techs., Inc.,* 73 F.3d 756, 763 (7th Cir.1996); *Lee v. Life Ins. Co. of North America,* 23 F.3d 14, 20 (1st Cir.1994). Several commentators have described how the analysis from *Kodak* could mean that franchisors' derivative aftermarkets may be relevant antitrust markets. Meese, 95 Mich. L.Rev. at 152 ("Under current law, [post-contract market power] can arise once the cost to the franchisee of switching to a different franchise is significant...."); Warren S. Grimes, *When Do Franchisors Have Market Power? Antitrust Remedies For Franchisor Opportunism,* 65 Antitrust L.J. 105, 112 (1996) ("A franchisor has market power if it can, without losing substantial sales, raise the price of a good or service sold to a franchisee above the level at which an equivalent good or service is available from other suppliers."); *see also* Robert H. Lande, *Chicago Takes It On The Chin: Imperfect Information Could Play A Crucial Role In The Post-*Kodak *World,* 62 Antitrust L.J. 193, 195 (1993) ("Another important lesson of *Kodak* is that imperfect information can be a crucial factor in ***447** defining relevant markets."). *But see* Alan Silberman, *The Myths of Franchise "Market Power",* 65 Antitrust L.J. 181, 217 (1996).

Uniqueness

In rejecting the plaintiffs' theory that the information and switching costs they face justify the alleged relevant market under *Kodak,* the majority states: "*Kodak* does not hold that the existence of information and switching costs alone,

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

such as those faced by the Domino's franchisees, renders an otherwise invalid relevant market valid." *Ante* at 439 (footnotes omitted). Both the district court and the majority make a more difficult argument, that a necessary factor in Kodak was that the repair parts were "unique." They state that this uniqueness is what gave Kodak market power, and that the lack of this factor herein warrants rejecting the plaintiffs' alleged relevant market. The basis for not applying *Kodak* in this case lies in two arguments: (1) the aftermarket ingredients and supplies are not unique, and (2) the franchisees knew of the policy because it was contained in the franchise agreement.

The first argument fails as a matter of law. Whether the product is unique was not the key component of the *Kodak* opinion. Even if the Court was somehow preoccupied with the "uniqueness" of the Kodak replacement parts, the opinion itself as well as economic theory suggest that uniqueness was not a *sine qua non* in finding a triable claim of market power. Justice Blackmun describes the plaintiffs' allegations regarding the market realities, including the facts that Kodak had excluded independent parts distributors and service competition and then boosted prices above prior levels. After this discussion, Justice Blackmun states: "Under our prior precedents, this evidence would be sufficient to entitle respondents to a trial on their claim of market power." 504 U.S. at 465.[5] The term unique seems to be important for antitrust purposes only in describing a product which has no reasonable substitutes.[6] The fact that Kodak parts were unique was important only because it limited the choices available to Kodak equipment owners seeking to replace worn out parts. The Court stated: "The relevant market for antitrust purposes is determined by the choices available to Kodak equipment owners." 504 U.S. at 481–82. Here, the plaintiffs' choices are limited to DPI-approved ingredients and supplies, and therefore the alleged relevant market is identical in kind to that involved in *Kodak.*

In *Wilson v. Mobil Oil Corp.,* 940 F.Supp. 944 (E.D.La.1996), the district court analyzed the relevance of the *Kodak* opinion to the franchise context. The defendants argued that *Kodak* does not apply to the franchisor/franchisee relationship and cited the district court opinion from this case for support. *Wilson,* 940 F.Supp. at 951. The court rejected the argument that the lack of unique products, like Kodak parts, makes *Kodak* inapplicable to the franchise relationship:

> This Court is not convinced that a principled distinction can be drawn as a matter of law between the franchise context and the durable equipment market involved in *Kodak.* No facts have been adduced to indicate that a business format franchise cannot create a derivative aftermarket for the purchase and sale of products that must be used in the franchise operation by the franchise network. Nor have facts been adduced that such an aftermarket could not be subject to the same economic dislocations that permitted market power to be possible in *Kodak.* The *Kodak* court did not purport to base its market power analysis solely on the fact that Kodak's machines were unique, nor did it limit the ***448** application of its reasoning to durable equipment markets. If anything, *Kodak* cautions against making economic assumptions on a blank factual record. See *Kodak,* 504 U.S. at 466–67, 112 S.Ct. at 2081–82.

Id. at 951–52. This analysis is compelling because it incorporates the understanding that a unique product does not itself confer market power and then analyzes the workings of the market in question.[7]

The majority also distinguishes *Virtual Maintenance, Inc. v. Prime Computer, Inc.,* 11 F.3d 660 (6th Cir.1993), on the basis of the importance of a unique product. In *Virtual Maintenance,* the Sixth Circuit was directed by the Supreme Court, in light of its opinion in *Kodak,* to reconsider the Sixth Circuits' earlier rejection of the plaintiff's antitrust claims. Upon reconsideration in light of *Kodak,* the court upheld the alleged relevant market for "the sale of software revisions and support of software necessary to do business with Ford Motor Company." *Id.* at 664 (citation omitted). In upholding the derivative aftermarket as a relevant market, the court held: "Like Kodak, Prime is able to exercise control over the sale of software support because of its exclusive distribution license from Ford, and Ford's requirement that its automotive design

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

suppliers use the most current version of Prime's software support." *Id.* at 666. The majority in the present case rejects application of *Virtual Maintenance* to this case: "But Prime had a monopoly because it possessed a unique product that no one else sold. Since the product was unique, and not interchangeable with any other products, it constituted its own relevant market for antitrust purposes. By contrast, Domino's does not sell a unique product or service." *Ante* at 440–41. However, this misstates the facts; Prime's product was not unique. In fact, the plaintiffs in *Virtual Maintenance* made products that were reasonably interchangeable with that of Prime. Thus, this analysis slights the significance of Prime's distribution license from Ford and Ford's requirement that suppliers use the latest version of Prime's product. The Sixth Circuit analyzed the market realities, including evidence of price manipulation and an economic lock-in, and concluded that under *Kodak* the alleged relevant market was valid.

The Franchise Agreement

The second argument, that the alleged relevant market fails because franchisees knew of the policy, fails as a matter of fact. Adopting the district court's position, the majority states that the franchisees knew the potential costs and economic risks of DPI forcing them to buy ingredients and supplies only from DPI at supracompetitive prices because the franchise agreement gave DPI the power to do so. *Ante* at 440. This statement is illusory for two reasons. First, it ignores the information in the Offering Circulars: the plaintiffs are supposed to have anticipated these actions despite the fact that they are directly contrary to what DPI told them. The plaintiffs argue that the Offering Circulars DPI presented when they were considering a DPI franchise stated that there would be alternative suppliers for the ingredients and supplies. Second, it would be illogical for the franchisees to expect that the franchisor's right to sell ingredients and supplies coupled with its approval power in the franchise agreement, included for the very legitimate purpose of franchise quality control, ***449** would be applied in such an odd and predatory way.[8] It seems hard for DPI to argue that the franchise agreement justifies its actions when all it's doing is buying the ingredients and supplies, marking up the prices, and then reselling them to the franchisees.[9]

Conclusion

Concern is expressed about the possible impact on the franchise industry from adopting plaintiffs' theory of relevant market definition. However, plaintiffs still have to prove the arguments they present for the alleged relevant market, and seek more discovery in order to do so. There are many defenses, which have not been argued, which may be applicable in this case or other franchisor/ franchisee antitrust disputes. My main concern with affirming the district court's opinion is the broad rejection of the basis for any antitrust claims by franchisees against franchisors in derivative aftermarkets. *See* Grimes, 65 Antitrust L.J. at 125–26 (describing several types of post-contract franchisor opportunism which may lead to antitrust claims if the franchisor has market power). There may be other problems, which are not before the court, with the plaintiffs' allegations of monopolization and illegal tying in the derivative aftermarkets by a franchisor, but the Supreme Court's clear direction in *Kodak* that information and switching costs are relevant to the ultimate determination of market power is honored by the district court only in the breach. The reality of the aftermarket for ingredients and supplies faced by these plaintiffs, according to the pleadings, is that alternative suppliers do not restrain DPI's ability to increase price, and information and switching costs lock-in the franchisees thereby preventing any competitive response to the price increases from DPI.

For the reasons set forth, I would reverse the district court's 12(b)(6) dismissal of plaintiffs' complaint.

All Citations

124 F.3d 430, 1997-2 Trade Cases P 71,909

Footnotes

* The Honorable Donald P. Lay, United States Circuit Judge for the Eighth Judicial Circuit, sitting by designation.

1 *See* the analysis of the economics of franchising in Warren S. Grimes, *When Do Franchisors Have Market Power?,* 65 Antitrust L.J. 105, 107–110 (1996).

2 Domino's Pizza, Inc. sells ingredients and supplies through its division, Domino's Pizza Distribution Division, "DPDD." DPDD was formerly a subsidiary of Domino's Pizza, Inc.

3 Domino's Pizza, Inc. argued before the district court that IFAC is without standing in this case. *Queen City Pizza, Inc. v. Domino's Pizza, Inc.,* 922 F.Supp. 1055, 1057 (E.D.Pa.1996). The district court apparently found it unnecessary to address this issue in light of its order dismissing the case for failure to state a claim.

4 The plaintiffs originally filed the complaint on behalf of themselves and a purported class of all present and future Domino's franchisees in the United States. Their amended complaint abandoned their claim to represent all Domino's franchisees.

5 "In a tying arrangement, the seller sells one item, known as the tying product, on the condition that the buyer also purchases another item, known as the tied product." *Allen–Myland, Inc. v. International Business Machines Corp.,* 33 F.3d 194, 200 (3d Cir.1994).

6 Cross-elasticity is a measure of reasonable interchangeability. As one treatise observes: "The economic tool most commonly referred to in determining what should be included in the market from which one then determines the defendant's market share is cross-elasticity of demand. Cross-elasticity of demand is a measure of the substitutability of products from the point of view of buyers. More technically, it measures the responsiveness of the demand for one product to changes in the price of a different product." E. Thomas Sullivan and Jeffrey L. Harrison, *Understanding Antitrust and its Economic Implications* 217 (1994).

7 In *Mozart Co. v. Mercedes–Benz of North America,* 833 F.2d 1342 (9th Cir.1987), the Court of Appeals for the Ninth Circuit observed that market power exists in three circumstances: where the government has granted a seller a patent or similar monopoly, where the seller possesses a unique product, or where the seller possesses a high market share. *Id.* at 1345–1346. The court made no mention of contractual limitations as a source of market power.

8 In a typical antitrust case, plaintiffs assert that the products or services in their proposed relevant market are reasonably interchangeable because they possess positive cross-elasticity of demand: a rise in the price of one product in the market will increase demand for the other items in the market. By contrast, in *Kodak* the defendants argued that Kodak copier parts, though not reasonably interchangeable with the copiers themselves, were not a relevant market because of negative cross-elasticity between parts and copiers: an increase in the price of parts would, they argued, decrease demand for copiers using those parts.

9 A franchisee considering exiting one franchise system faces information costs associated with researching alternative investment opportunities and switching costs stemming from the loss of invested funds that may not be recovered if it abandons its current business and start-up costs associated with the new venture.

10 If Kodak repair parts had not been unique, but rather, could be obtained from additional sources at a reasonable price, Kodak could not have forced copier purchasers to buy repair parts from Kodak. This would be true even if the copier purchasers faced information and switching costs that locked them into to use of Kodak copiers. This fact indicates that switching and information costs alone cannot create market power. Rather, it is the lack of a competitive market in the object to be purchased—for instance, a competitive market in Kodak parts—that gives a company market power.

11 *See* Alan Silberman, *The Myths of Franchise "Market Power",* 65 Antitrust L.J. 181, 217 (1996).

12 *See Mozart Co. v. Mercedes–Benz of North America, Inc.,* 833 F.2d 1342, 1349–50 (9th Cir.1987); Alan J. Meese, *Antitrust Balancing in a (Near) Coasean World: The Case of Franchise Tying Contracts,* 95 Mich. L.Rev. 111, 117–119 (1996); Warren S. Grimes, *When Do Franchisors Have Market Power?,* 65 Antitrust L.J. 105 145–47 (1996); Benjamin Klein and Lester F. Saft, *The Law and Economics of Franchise Tying Contracts,* 28 J.L. & Econ. 345, 346–48 (1985).

13 Warren S. Grimes, *When Do Franchisors Have Market Power?,* 65 Antitrust L.J. 105, 105 n.1 (1996).

14 *See United States v. Arnold, Schwinn & Co.,* 388 U.S. 365, 387, 87 S.Ct. 1856, 1869, 18 L.Ed.2d 1249 (1967) (Stewart, J., concurring in part and dissenting in part) ("Indiscriminate invalidation of franchising arrangements would eliminate their creative contributions to competition and force suppliers to abandon

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

franchising and integrate forward to the detriment of small business. In other words, we may inadvertently compel concentration by misguided zealousness.") (internal quotations omitted). The majority's opinion in *Arnold* was later overturned. *See Continental T.V., Inc. v. GTE Sylvania Inc.,* 433 U.S. 36, 97 S.Ct. 2549, 53 L.Ed.2d 568 (1977).

15 As one scholar has noted, there are thousands of franchise opportunities available to investors and disclosure laws to help them make informed choices about these alternatives. George A. Hay, *Is the Glass Half–Empty or Half–Full?: Reflections on the Kodak Case,* 62 Antitrust L.J. 177, 188 (1993).

16 The dissent contends Domino's has acted in a "predatory way." But plaintiffs may have a right to sue for breach of contract.

17 The reasoning adopted by the district court in this case has been criticized recently by two other district court decisions. *See Wilson v. Mobil Oil Corp.,* 940 F.Supp. 944 (E.D.La.1996); *Collins v. International Dairy Queen, Inc.,* 939 F.Supp. 875 (M.D.Ga.1996). In *Wilson,* the court disagreed with the district court's interpretation of *Kodak,* arguing that under *Kodak* information and switching costs alone, absent a unique product or service, may create a relevant market for antitrust purposes. As noted above, we disagree with this interpretation, for the Supreme Court specifically found that the copier parts involved in the case were unique. The basis of the *Collins* court's criticism of the district court's decision here is less clear, though it appears the court believed that the district court's holding was too expansive. The *Collins* court apparently wished to reserve judgment whether some franchise tying arrangements might be deemed anti-competitive in the future. The approach taken by the district court in this case has received support in recent scholarly literature. *See* Alan J. Meese, *Antitrust Balancing in a (Near) Coasean World: The Case of Franchise Tying Contracts,* 95 Mich. L.Rev. 111, 128 (1996) ("economic theory suggests ... that tying contracts that actually reduce free riding are unrelated to any exercise of market power"); Alan H. Silberman, *The Myths of Franchise "Market Power",* 65 Antitrust L.J. 181 (1996).

18 Monopoly power under § 2 requires "something greater" than market power under § 1. *Kodak,* 504 U.S. at 481, 112 S.Ct. at 2089 This does not imply, however, that the analyses employed in the two types of cases to define relevant markets differ. In the past, we intimated that the relevant market analysis required under § 2 of the Sherman Act was "instructive" in § 1 cases, though perhaps not identical. *See Tunis Bros.,* 952 F.2d at 724 n. 3. The Supreme Court and lower courts have consistently held that relevant markets under both sections are defined by the same two factors: reasonable interchangeability of use and cross-elasticities of demand. *See, e.g., Allen–Myland,* 33 F.3d at 201 and 201 n. 8 (applying *Brown Shoe* relevant market test of reasonable interchangeability and cross-elasticity of demand in § 1 tying case). In this case, we see no difference in the relevant market analyses required under the two provisions.

1 The district court relied on "two influential commentators," Benjamin Klein and Lester F. Saft, *The Law and Economics of Franchise Tying Contracts,* 28 J.L. & Econ. 345, 356 (1985) and two pre-*Kodak* cases, *Mozart Co. v. Mercedes–Benz of North America, Inc.,* 833 F.3d 1342 (9th Cir.1987), and *Tominaga v. Shepherd,* 682 F.Supp. 1489 (C.D.Cal.1988). The district court adopted the Ninth Circuit's analysis from *Mozart* that an alleged economic-lock-in is irrelevant to the determination of a defendant's market power. *See Tominaga,* 682 F.Supp. at 1494 (quoting *Mozart,* 833 F.2d at 1346–47). This reasoning is simply irreconcilable with the Supreme Court's analysis of information and switching costs in *Kodak. See Kodak,* 504 U.S. at 473–77, 112 S.Ct. at 2085–87.

It should also be noted Professor Klein recognized, contrary to his original thesis, that *Kodak* permits the recognition of market power in a derivative aftermarket "despite the absence of market power in the equipment market, by taking advantage of imperfectly informed consumers that become 'locked-in' to their existing Kodak equipment." *See* Benjamin Klein, *Market Power in Antitrust: Economic Analysis After Kodak,* 3 Sup.Ct. Econ. Rev. 43, 48 (1993).

2 The basic definition of market power is "the power to raise prices above competitive levels without losing so many sales that the price increase is unprofitable." Herbert Hovenkamp, *Federal Antitrust Policy: The Law of Competition and its Practice* § 3.1, at 79 (1994) (footnote omitted).

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

3 The majority, in footnote 17, *ante* at 442, states that the district court's approach has "received support in recent scholarly literature," citing Alan J. Meese, *Antitrust Balancing in a (Near) Coasean World: The Case of Franchise Tying Contracts,* 95 Mich. L.Rev. 111, 128 (1996). However, Professor Meese does not argue that the approach taken is correct under current antitrust law. In fact, on page 126 he concedes that the *Kodak* decision "found that the existence of relationship-specific investments can confer 'market power' ", and at 152–55 he states that "under current law" franchisors may have market power over derivative aftermarkets due to "lock-in" of the franchisees, and because of this he proposes a new framework for analyzing such claims. He argues that "the focus on market power and less restrictive alternatives, though perfectly natural given the partial equilibrium framework that dominates antitrust law and the premises that underlie tying jurisprudence," does not properly apply to the franchise tying context. *Id.* at 128. Professor Meese argues that tying contracts that reduce free riding, a form of opportunistic behavior taken at the expense of the franchise system, should be prima facie legal. Whatever the value of Professor Meese's argument, he presupposes that "under current law" from the Supreme Court the district court in this case may have erred. *Id.* at 152. In addition, it is not even clear that Professor Meese would find the plaintiffs' allegations insufficient as a matter of law because they allege that DPI charged supracompetitive prices for the ingredients and supplies. *See id.* at 155.

4 This conclusion seems quite sensible. If Kodak customers knew about Kodak's subsequent parts-and-service policy when they bought the copiers, or were not economically restricted from switching to other copiers, then Justice Scalia's dissent, which assumes a perfect competition/perfect information world, should be right. Kodak is merely a concession to fact that markets do not always work perfectly, and sometimes, but not always, these imperfections can create sufficient market power to justify possible antitrust liability.

5 In *Market Power in Aftermarkets: Antitrust Policy and the* Kodak *Case,* 40 U.C.L.A. L.Rev. 1447 (1993), Professor Hovenkamp argues that whether a product requires "unique" replacement parts is absolutely irrelevant to whether the manufacturer of that product has market power. He states that the portion of the *Kodak* opinion about unique parts is wrong, but that the evidence cited of increased prices was relevant to the question of market power. *Id.* at 1454–55.

6 For example, if someone patented a new material for bottling soft drinks, it would certainly be true that there were no other materials just like it. But, provided glass and plastic were still reasonable substitutes, the description "unique" would not be meaningful for antitrust analysis.

7 The majority cities *United Farmers Agents v. Farmers Ins. Exchange,* 89 F.3d 233 (5th Cir.1996), *cert. denied,* 519 U.S. 1116, 117 S.Ct. 960, 136 L.Ed.2d 846 (1997), for the argument that a derivative aftermarket defined by contractual restraints must be rejected. However, this case does not stand for the proposition for which it is cited. In *United Farmers,* the 5th Circuit does cite the statement from Professors Klein and Saft, that the economic power derived from contractual agreements has nothing to do with market power for purposes of antitrust. 89 F.3d at 236–7. However, the court proceeded to expressly address whether there were sufficient information and switching costs to justify invoking *Kodak* and upholding the plaintiffs' alleged relevant market. The district court in *Wilson* addressed the importance of the *United Farmers* opinion and concluded: "If anything, this decision suggests that when parties seek to invoke *Kodak,* issues of information costs and switching costs must be addressed before tying claims can be rejected out of hand." *Wilson,* 940 F.Supp. at 952.

8 It is alleged the DPI's Offering Circular represented to prospective franchisees that DPI would approve a sufficient number of suppliers to ensure a competitive aftermarket for ingredients and supplies, and that it would only utilize its approval power to maintain quality control.

9 Moreover, the majority's analysis, that what the plaintiffs knew when they entered the franchise agreement is an important distinguishing factor, concedes that imperfect information is a crucial factor in determining relevant market definition.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-26

Restatement (First) of Contracts § 166 (1932)

Restatement of the Law - Contracts | October 2019 Update

Restatement (First) of Contracts

Chapter 7. Assignment of Rights and Delegation of Duties or Conditions

§ 166 Promises to Assign in the Future

Comment:
Case Citations - by Jurisdiction

(1) A contract to assign a right in the future is not an assignment. But a contract to assign as security a right which is specified and capable of effective present assignment under §§ 151, 154, gives the promisee a right against the obligor inferior to that of an assignee only in that the right will be extinguished if, before satisfaction is obtained by the promisee, an assignment of the obligee's right is made to a bona fide purchaser for value without notice of the prior contract.
(2) The obligor may require that the promisor be joined in any action to enforce the right brought against him by the promisee.

Comment:

a. The Section relates to contracts to assign in the future. By definition an assignment contemplates no further action on the part of the assignor to complete the right of the assignee [see § 149(1)]. A contract to assign involves a promise to do some further act in order to perfect the right of the promisee against the obligor. There is often a question of interpretation to be decided whether the language of the owner of a right indicates an intention to transfer the right immediately, or only an intention to bind himself to make such a transfer in the future. If there is merely a contract to assign in the future and the promise has not been performed, any recognition of ownership by the promisee must be based on specific enforcement of the promise. The Section states that the rights of the parties are to be adjusted as if the contract were specifically enforced, if the contract is made to secure some performance due from the promisor to the promisee, but not otherwise.

b. The promisee's right, moreover, is defeasible by a subsequent assignment to a bona fide purchaser for value without notice of the prior right, in this respect differing from a present assignment of a future right (see § 154). What is meant by “value” and by “notice” in the phrase bona fide purchaser for value without notice is not always identical in different kinds of transactions. The law regarding this is stated in the Restatement of Trusts.

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Illustrations:

1. A promises B, in consideration of a horse sold to him by B, that A will thereafter assign to him money which will fall due to A from C under an existing employment. A subsequently assigns for value the right to D, who neither knows nor has reason to know of the previous promise. B learns of this assignment and thereafter collects the money when due from C. B acquires no right against C or power to discharge C and therefore D can recover from B the money so collected or can get judgment against C.

2. A, on borrowing money from B, and as part of the consideration for the loan, says: "I expect to sell some goods soon and when I do I will assign to you as security so much of my right to the price as will equal the sum due you from me." A later sells goods to C on credit and before C pays the price becomes bankrupt. The promise does not sufficiently identify the right intended to be assigned. B can only prove his claim as a general creditor.

3. A, when borrowing money from B, and as part of the consideration for the loan, says: "I have contracted to sell on credit some goods to C, and as soon as I do I will assign my right for the price to you as security for your loan to me." Thereafter A sells the goods to C, and before making any assignment to B, and before C pays the price, becomes bankrupt. B has a right to receive so much of the sum due from C as is necessary to pay B's loan to A.

Case Citations - by Jurisdiction

W.D.Ky.
D.Mass.
Ohio App.
Or.App.
R.I.

W.D.Ky.

W.D.Ky.1952. Com. a, Ill. 3 cit. in sup. Insured's oral promise as part of property settlement agreement with wife to make proceeds of group life insurance policies payable to children constituted an equitable assignment of policies to children whose rights were superior to insured's second wife who was subsequently designated as beneficiary. McPhail v. John Hancock Mut. Life Ins. Co., 108 F.Supp. 902, 906.

D.Mass.

D.Mass. Subsec. (2) cit. in dictum. Defendants in anti-trust action may obtain joinder of assignors of cause of action with their assignee. Momand v. Universal Film Exchange, 43 F.Supp. 996, 1007.

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Ohio App.

Ohio App.1947. Cit. in sup. in diss. op. Instrument by purchaser of house under land contract which stated that he had received purchase price in full from plaintiff, that house was to be free of mortgage and that he would transfer deed, constituted an equitable assignment of the land contract entitling plaintiff to sue thereunder for specific performance. Morris v. George C. Banning, Inc., 77 N.E.2d 372, 375.

Or.App.

Or.App.1980. Subsec. (1) quot. in sup. Plaintiff brought this action for conversion by wrongful execution. The restaurant, the contents of which were the subject of this action, was the subject of an agreement of sale between the original owner and the defendants to this action. The agreement was breached by the original owner and a judgment was granted in favor of the defendants herein. Subsequently, the original owner purported to convey the restaurant to the plaintiff. Following this, plaintiff entered into an agreement to sell the restaurant to another party. As part of the agreement that party was required to get defendants in the present action to assign to plaintiffs the judgment it had obtained against the original owner. Such assignment was executed and placed in escrow, pending closing of the sale and review for form. The assignment was still in escrow when the writ of execution was issued. The trial court granted judgment for the plaintiff, but it found that there had been no valid assignment of rights to the plaintiff. On appeal this court affirmed, holding that due to the fact that conditions still existed to be performed, the attempted assignment did not indicate an unconditional intent to transfer without further action as is required for a valid assignment; therefore, the trial court was entitled to conclude that there had been no assignment in the legal sense. Springfield International Restaurant v. Sharley, 44 Or.App. 133, 605 P.2d 1188, 1192.

R.I.

R.I.1940. Subsec. (1) quot. as not applicable. A promise to assign to a discount company the accounts receivable held by a corporation is not a valid contract of assignment when the assignee indicated that it contemplated an actual assignment and not a mere promise to assign. Wheeler Co. v. Abbott-Beeber Co., 64 R.I. 421, 425, 12 A.2d 657, 659.

Restatement of the Law - Contracts © 1932-2019 American Law Institute.
Reproduced with permission. Other editorial enhancements © Thomson Reuters.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-27

Restatement (Second) of Contracts § 316 (1981)

Restatement of the Law - Contracts | October 2019 Update

Restatement (Second) of Contracts

Chapter 15. Assignment and Delegation

§ 316 Scope of This Chapter

Comment:
Reporter's Note
Case Citations - by Jurisdiction

(1) In this Chapter, references to assignment of a right or delegation of a duty or condition, to the obligee or obligor of an assigned right or delegated duty, or to an assignor or assignee, are limited to rights, duties, and conditions arising under a contract or for breach of a contract.
(2) The statements in this Chapter are qualified in some respects by statutory and other rules governing negotiable instruments and documents, relating to interests in land, and affecting other classes of contracts.

Comment:

a. Contractual right; chose in action. Statements in this Chapter are limited to contractual rights and duties. Such rights include debts, rights to non-monetary performance and rights to damages and other contractual remedies, whether or not a right to payment has been earned. On the other hand, "chose in action" is a much broader term. In its primary sense it includes debts of all kinds, tort claims, and rights to recover ownership or possession of real or personal property; it has been extended to instruments and documents embodying intangible property rights, to such intangible property as patents and copyrights, and even to equitable rights in tangible property. The rules stated here may have some application to non-contractual choses in action, but the transfer of non-contractual rights is beyond the scope of the Restatement of this Subject.

b. Negotiable instruments and documents; conveyances of land. The rules governing negotiable instruments and documents and the benefits and burdens attached to successive owners of real property by virtue of a contract in a prior conveyance or lease are to some extent different from the law governing contracts in general. The law governing negotiable instruments and documents derives from the law merchant and is now largely statutory. See Comment to § 6. The law relating to covenants in conveyances and leases of land grew up as part of the law of real property and is left to the Restatement, Second, of Property.

c. Assignment and delegation. In this Chapter rights are said to be "assigned"; duties are said to be "delegated." The phrase "assignment of the contract," which may refer to either or both, is avoided because "contract" is defined in § 1 in terms of the act or acts of promising. See § 328. "Assignment" is the transfer of a right by the owner (the obligee or assignor) to another person (the assignee). See § 317. A person subject to a duty (the obligor) does not ordinarily have such a power to substitute another

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

in his place without the consent of the obligee; this is what is meant when it is said that duties cannot be assigned. “Delegation” of performance may be effective to empower a substitute to perform on behalf of the obligor, but the obligor remains subject to the duty until it has been discharged by performance or otherwise. Compare the usage of terms in Uniform Commercial Code § 2-210. Delegation of performance of a condition is similar in effect to delegation of performance of duty.

d. Involuntary transfer. In accordance with common usage, assignment and delegation in this Chapter include only transfers made or powers created by virtue of a manifestation of intention of the assignor or obligor. The manifestation may be made to the assignee or the person delegated or to another person on his behalf, but transfers made and powers created by operation of law are excluded. Such transfers and powers, including transfers to and powers of an executor, administrator, trustee in bankruptcy or receiver by virtue of his office, are in general beyond the scope of this Restatement. As to the equitable remedies of constructive trust, equitable lien, and subrogation, which sometimes operate much like an assignment, see Restatement of Restitution §§ 160- 62; Restatement of Security § 141.

Reporter's Note

See 3 Williston, Contracts §§ 404, 407 (3d ed.1960); 4 Corbin, Contracts §§ 859-64 (1951); Holdsworth, The History of the Treatment of Choses in Action by the Common Law, 33 Harv.L.Rev. 997 (1920); Corbin, Assignment of Contract Rights, 74 U.Pa.L.Rev. 207 (1926). 1 Gilmore, Security Interests in Personal Property Ch. 7 (1965), 2 id. Ch. 41 (1965).

Comment a. On the elimination, in the 1972 Amendments to the Uniform Commercial Code, of the term “contract right,” and its inclusion within “account,” see Uniform Commercial Code, Appendix II, § 9-106 Reasons for 1972 Change, and Reporter's Note to the Introductory Note to this Chapter.

Comment c. For some of the problems caused by unclear analysis (by both the parties and the court) of a transaction alleged to be an assignment, see University Caseworks Systems v. Bahre, 172 Ind.App. 624, 362 N.E.2d 155 (1977). For an analysis that would have been clearer and easier had “delegation” been used in the place of “assignment,” see Smith v. Wrehe, 199 Neb. 753, 261 N.W.2d 620 (1978).

Comment d. For a distinction between the impermissible assignment of a personal injury claim (§ 317 Comment *c* and Illustration 8) and the permissible subrogation of an insurer advancing payment, see Western Cas. and Sur. Co. v. Bowling, 39 Colo.App. 357, 565 P.2d 970 (1977); Higgins v. Allied American Mut. Fire Ins. Co., 237 A.2d 471 (D.C.Ct.App.1968); Annot., 19 A.L.R.3d 1054 (1968).

Case Citations - by Jurisdiction

—

- C.A.3,
- C.A.8
- C.A.10
- M.D.Fla.
- W.D.Pa.
- D.P.R.
- E.D.Va.
- Ariz.
- Ariz.App.
- Cal.App.
- Conn.App.
- Minn.App.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

N.Y.Sup.Ct.
Pa.Super.
Wis.

C.A.3,

C.A.3, 2016. Subsec. (1) and com. (a) quot. in disc. Trucking company that was assigned direct purchaser's antitrust claims filed a putative antitrust class action to represent Class 8 truck purchasers against, among others, manufacturers of transmissions for Class 8 heavy-duty trucks, alleging that defendants engaged in a monopolization conspiracy. The district court granted defendants' motion to dismiss. This court reversed and remanded, holding that an assignment of a federal antitrust claim did not need to be supported by bargained-for consideration in order to confer standing on an indirect purchaser. Citing Restatement Second of Contracts § 317, the court rejected defendants' argument, which cited § 316 to claim that an assignment was limited to contractual causes of action and did not extend to choses in action, explaining that the distinction between contractual rights and choses in action no longer had a significant effect on the common law. Wallach v. Eaton Corporation, 837 F.3d 356, 369.

C.A.8

C.A.8, 1994. Com. (a) cit. in sup. and cit. in headnote. Two brothers, through their company, developed and sold lures exclusively to purchaser and then assigned purchaser their patent rights to the lure. While it was allegedly contemplated that brothers' company would continue to manufacture lures for purchaser, one brother did not become shareholder in new entity from which purchaser continued to buy lures. Ousted brother brought action seeking declaratory judgment that patent assignment he made to purchaser was void for lack of consideration. District court entered summary judgment for purchaser, holding that plaintiff received consideration for the assignment in the form of the expectation of continued lure purchases by purchaser from plaintiff's company. Affirming on other grounds, this court held, in part, that patent assignment was a completed voluntary conveyance of a chose in action, and that it therefore was not subject to attack for lack of consideration. Keller v. Bass Pro Shops, Inc., 15 F.3d 122, 123, 125.

C.A.10

C.A.10, 1990. Com. (c) cit. in disc. A California employee of a Kansas corporation resigned shortly before a corporate merger. The surviving corporation sued to enforce a covenant not to compete contained within the employee's contract with the merged corporation. The trial court granted the surviving corporation a preliminary injunction prohibiting the employee from violating the covenant. This court affirmed, holding that a covenant not to compete was an assignable contract right. The court stated that the surviving corporation had automatically succeeded to that right of the merged corporation, and so could sue to enforce the covenant not to compete. Equifax Services, Inc. v. Hitz, 905 F.2d 1355, 1361.

M.D.Fla.

M.D.Fla.1994. Com. (c) cit. in disc. Motel franchisor brought an action to recover franchise fees from limited partnership that purchased motel property from franchisee. Denying the parties' cross-motions for summary judgment, the court held that genuine issues of material fact precluding summary judgment existed as to whether there was a valid assignment and delegation of the franchise agreement from franchisee to limited partnership and thus whether limited partnership was in privity with motel franchisor. Quality Inns Intern. v. Tampa Motel Associates, 154 F.R.D. 283, 290.

W.D.Pa.

W.D.Pa.2000. Cit. in disc. Mortgagors brought claims for breach of contract and breach of fiduciary duty, inter alia, against Federal Home Loan Mortgage Corporation (FHLMC) and FHLMC's servicing agent, which acted as original mortgagee, alleging that FHLMC was directly liable and liable as successor-in-interest for conduct of original and subsequent servicing

agents. This court granted FHLMC's motion to dismiss, holding that it was not liable for conduct engaged in by original or subsequent servicing agent prior to FHLMC's acquisition of mortgage, because FHLMC was not "successor-in-interest" as to mortgage contract. FHLMC's status as to subsequent servicing agent was as assignee of mortgage rights, and it did not assume all obligations and consequences of mortgage contracts entered into between servicing agents and mortgagors. Paslowski v. Standard Mortg. Corp. of Georgia, 129 F.Supp.2d 793, 798.

D.P.R.

D.P.R.2002. Com. (c) quot. in sup. Former exclusive dealer for coffee brand sued new and former owners of coffee's brand name, among others, alleging that its dealer contract was terminated without just cause. Granting former owner's motion to dismiss, this court held that former owner's assignment of its right to coffee's brand name to new owner released former owner from any obligation to dealer. Goya de Puerto Rico, Inc. v. Rowland Coffee, 206 F.Supp.2d 211, 217.

E.D.Va.

E.D.Va.1994. Subsec. (2) cit. in disc. Resolution Trust Corporation (RTC) assignees sued the makers and guarantors of a promissory note, seeking to recover on the note. The court granted defendants' motion to dismiss, holding that the Federal Institutions Reform, Recovery and Enforcement Act (FIRREA) six-year statute of limitations applicable to actions brought by RTC as receiver was a benefit personal to RTC and was not transferable for the benefit of assignees. The court stated that the law of assignments did not apply with full force to negotiable instruments. Wamco, III, Ltd. v. First Piedmont Mortg., 856 F.Supp. 1076, 1087.

Ariz.

Ariz.2008. Com. (a) quot. in disc. Insureds' judgment creditor, as assignee of insureds, sued insurance agent, alleging negligence and breach of fiduciary duty based on agent's failure to advise insureds that they could have purchased liquor-liability coverage. The trial court dismissed these claims, and the court of appeals affirmed. Reversing and remanding, this court held, inter alia, that insureds' claims for professional negligence were assignable to their judgment creditor. The court distinguished this situation from claims against lawyers for legal malpractice, and noted that, under Arizona law, unliquidated claims were generally assignable, except those involving personal injury; where the legislature had not prohibited assignability of claims between insurance agent and client, and the public-policy concerns expressed did not support a rule generally barring assignability, the general rule applied. Webb v. Gittlen, 217 Ariz. 363, 174 P.3d 275, 276.

Ariz.App.

Ariz.App.2000. Cit. in ftn. to spec. conc. op. Decedent's biological father, who had previously relinquished his parental rights, sued decedent's mother and adoptive father for breach of a contract to split the proceeds of defendants' wrongful-death action. The trial court entered judgment for defendants on the ground that the parties' agreement was unenforceable. Affirming, this court held that neither a wrongful-death cause of action nor the proceeds from it were assignable. Concurrence believed that, while there should be a prohibition on the assignment of causes of action, there was no reason to prevent the assignment of the resulting proceeds. Lingel v. Olbin, 198 Ariz. 249, 8 P.3d 1163, 1172.

Cal.App.

Cal.App.1992. Cit. in disc., coms. cit. generally in disc. A business that purchased/cashed checks purchased a $50 check from a payee. After the check was dishonored by drawee bank, check purchaser filed claim in small claims court against check drawer. The small claims court dismissed the claim on the ground that purchaser, as assignee, could not maintain a claim in small claims court. Trial court entered a writ of mandate directing small claims court to vacate its judgment of dismissal and to entertain

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the claim. This court issued a peremptory writ of mandate directing trial court to set aside its judgment. The court held that the holder after endorsement of a check was an assignee of a claim, and assignees were barred from maintaining a claim in small claims court. The court noted that there was some ambiguity in the term "assignee," but the California Supreme Court previously determined that "assignee" was to be construed broadly. Municipal Court v. Superior Court, 9 Cal.App.4th 1867, 12 Cal.Rptr.2d 519, 521, review dismissed, cause remanded 22 Cal.Rptr.2d 276, 856 P.2d 1132 (1993).

Conn.App.

Conn.App.2012. Sec. and com. (c) cit. in ftn. Real estate broker that located a tenant for a commercial property sued former landlord and current landlord, seeking to recover a commission pursuant to its exclusive listing agreement with former landlord. Following a bench trial, the trial court found against both defendants. Affirming, this court rejected current landlord's argument that the trial court improperly rendered judgment against it because it was not a party to the agreement, holding that current landlord was bound by the agreement as an assignee of former landlord; by the terms of the agreement, former landlord's obligations were intended to be binding upon its assignees. Sunset Gold Realty, LLC v. Premier Bldg. and Development, Inc., 133 Conn.App. 445, 452-453, 36 A.3d 243, 249.

Minn.App.

Minn.App.2010. Cit. in sup. Assignee of a loan that was originally disbursed under state agency's student loan program commenced a collection action against borrower. The trial court granted summary judgment for plaintiff. Affirming, this court held, as a matter of first impression, that plaintiff's action was not time-barred by any Minnesota statute of limitations, because plaintiff was a valid assignee of agency's right under an amendment to the Higher Education Act not to be subject to any state statutes of limitation. The court explained that, while the amendment did not, by its terms, extend its statutes-of-limitations exemption to assignees of named lenders, under the common law, a contractual right to recover student-loan debt was assignable and did not fall within the personal-rights exclusion to the assignment rule. Mountain Peaks Financial Services, Inc. v. Roth-Steffen, 778 N.W.2d 380, 385.

N.Y.Sup.Ct.

N.Y.Sup.Ct.1984. Com. (c) cit. in sup. Plaintiffs held bonds issued by a Utah corporation in 1902 for a railroad located in Mexico. Defendant was the successor indenture trustee of the corporation's collateral. Subsequently, Mexico nationalized the railroads and the Mexican state railway company agreed to pay interest and principal to the bondholders. In 1982, defendant sold the American collateral to a Mexican corporation at the insistence of the Mexican government. Plaintiffs brought an action for negligence and breach of fiduciary duty, claiming that the price was grossly under market value. Defendant moved for summary judgment, alleging that plaintiffs lacked standing to sue because failure to register the bonds pursuant to a 1942 decree caused title in the bonds to pass to the Mexican government. The trial court denied defendant's motion, holding that plaintiffs had rights under the bonds because they never assented to the transfer of obligations from the Utah corporation to the Mexican state railway, thus no novation took place. Beck v. Manufacturers Hanover Trust Co., 125 Misc.2d 771, 481 N.Y.S.2d 211, 218.

Pa.Super.

Pa.Super.1995. Com. (c) cit. in case cit. in disc. A health-care provider sued an insurance company for refusing to pay for patients' chiropractic treatments pursuant to the terms of an ERISA group health insurance policy. Trial court dismissed provider's complaint. This court reversed and remanded, holding, inter alia, that the provider had the capacity to sue under ERISA because it had obtained assignments from the legitimate insurance plan beneficiaries. It also held that the specific nonassignment clause contained in the group contract did not preclude plaintiff from achieving any remedy. The court found nothing in the provision that prevented a subscribing member from assigning his or her right to bring an action to enforce the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

contract in the event that benefits were denied. It noted that the right to assign a cause of action was separate and distinct from the right to assign benefits. Chiropractic Nutritional v. Empire Blue Cross and Blue Shield, 447 Pa.Super. 436, 669 A.2d 975, 983.

Wis.

Wis.2006. Cit. in disc. Chiropractor sued patient's attorney, seeking to enforce an agreement signed by patient, but not signed by her attorney, directing attorney to pay chiropractor for treatment received by patient and purporting to give chiropractor a lien against any proceeds from patient's personal-injury action, after attorney distributed the action's proceeds without paying him. The trial court granted summary judgment for plaintiff. The court of appeals reversed. Affirming, this court held, inter alia, that plaintiff could not hold attorney liable for payment because attorney had not signed the agreement or otherwise agreed to be liable; the court declined to address the issue of the assignability of a claim or right arising from a tort but observed that such a claim or right was generally not as easily assignable as one arising under a contract. Yorgan v. Durkin, 290 Wis.2d 671, 715 N.W.2d 160, 163.

Restatement of the Law - Contracts © 1932-2019 American Law Institute.
Reproduced with permission. Other editorial enhancements © Thomson Reuters.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-28

Restatement (Second) of Contracts § 322 (1981)

Restatement of the Law - Contracts | October 2019 Update

Restatement (Second) of Contracts

Chapter 15. Assignment and Delegation

Topic 1. What Can Be Assigned or Delegated

§ 322 Contractual Prohibition of Assignment

Comment:
Reporter's Note
Case Citations - by Jurisdiction

(1) Unless the circumstances indicate the contrary, a contract term prohibiting assignment of "the contract" bars only the delegation to an assignee of the performance by the assignor of a duty or condition.

(2) A contract term prohibiting assignment of rights under the contract, unless a different intention is manifested,

(a) does not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation;

(b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective;

(c) is for the benefit of the obligor, and does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition.

Comment:

a. Rationale. In the absence of statute or other contrary public policy, the parties to a contract have power to limit the rights created by their agreement. The policy against restraints on the alienation of property has limited application to contractual rights. Compare Restatement of Property §§ 404- 17. A term in a contract prohibiting assignment of the rights created may resolve doubts as to whether assignment would materially change the obligor's duty or whether he has a substantial interest in personal performance by the obligee (see §§ 317- 19); or it may serve to protect the obligor against conflicting claims and the hazard of double liability (see §§ 338- 43). But as assignment has become a common practice, the policy which limits the validity of restraints on alienation has been applied to the construction of contractual terms open to two or more possible constructions. Compare Restatement of Property §§ 418- 23.

b. Ineffective terms. In some circumstances where contractual prohibitions of assignment are regularly limited by construction, explicit contractual provision would not change the result. Where a right to the payment of money is fully earned by performance, for example, a provision that an attempt to assign forfeits the right may be invalid as a contractual penalty. See § 356. If there is

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

no forfeiture, and the obligee joins in demanding payment to the assignee, a contractual prohibition which serves no legitimate interest of the obligor is disregarded. Uniform Commercial Code §§ 2-210 and 9-318 render contractual prohibitions ineffective in additional circumstances, and in some situations a prohibition is invalid as a restraint on alienation aside from statute. See Uniform Commercial Code § 9-311.

Illustrations:

1. A holds a policy of industrial insurance issued to him by the B Insurance Company. After lapse for failure to pay premiums, B refuses to pay the "cash surrender value" provided for in the policy. A and others similarly situated assign their claims to C for collection. The assignment is effective without regard to any contractual prohibition of assignment.

2. A and B contract for the sale of land by B to A. A fully performs the contract, becomes entitled to specific performance on B's refusal to convey the land, and then assigns his rights to C. C is entitled to specific performance against B without regard to any contractual prohibition of assignment. See Restatement of Property § 416.

c. Construction. The rules stated in this Section do not exhaust the factors to be taken into account in construing and applying a prohibition against assignment. "Not transferable" has a clear meaning in a theatre ticket; in a certificate of deposit the same words may refer to negotiability rather than assignability. Where there is a promise not to assign but no provision that an assignment is ineffective, the question whether breach of the promise discharges the obligor's duty depends on all the circumstances. See §§ 237, 241.

d. Consent of the obligor. Ordinarily a contractual prohibition of assignment is for the benefit of the obligor. In such cases third parties cannot assert the invalidity of a prohibited assignment if the obligor makes no objection. Where, however, the prohibition is not solely for the benefit of the obligor, waiver by the obligor may not validate the assignment. The validity of restraints on alienation in such cases is governed by considerations similar to those governing the validity of spendthrift trusts. See Restatement, Second, Trusts §§ 153- 57.

Illustrations:

3. B contracts to transfer land to A on payment of $5000. The contract provides that A shall not assign his right. A assigns his right to C. B, on receiving $5000 from C, conveys the land to him. B's duty under his contract with A is discharged.

4. A Manufacturing Company contracts with B Insurance Company for group insurance on the lives of A's employees. The policy and certificates issued under it to individual employees limit the class of permitted beneficiaries, permit the employee to change the beneficiary, forbid irrevocable designation of a beneficiary,

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

and provide that the certificate is not assignable. A certificate is issued to C, a widower, who designates his son D as beneficiary and delivers the certificate to D as a gift. Later C remarries and designates his second wife E as beneficiary. On C's death B interpleads D and E, paying the insurance money into court. E is entitled to the fund.

Reporter's Note

This Section is new. Subsection (1) is based on Uniform Commercial Code § 2-210(3), which applies to contracts for the sale of goods. Comment *d* changes former § 176 from a rule of law to a canon of construction. See 3 Williston, Contracts § 422 (3d ed.1960); 4 Corbin, Contracts §§ 872, 873 (1951); Annot., 37 A.L.R.2d 1251 (1954). But see Gilmore, The Commercial Doctrine of Good Faith Purchase, 63 Yale L.J. 1057, 1118-20 (1954).

Comment b. Reasoning from Uniform Commercial Code § 9-318, the Oklahoma Supreme Court found a legislative purpose to bar all anti-assignment clauses, even in situations not subject to Article Nine of the Code, American Bank of Commerce v. City of McAlester, 555 P.2d 581 (Okl.1976). Illustration 1 is based on National Life & Acc. Ins. Co. v. Magers, 319 S.W.2d 53 (Ct.App.1958), aff'd, 329 S.W.2d 752 (Mo.1959); see also International Rediscount Corp. v. Hartford Accident and Indem. Co., 425 F.Supp. 669 (D.Del.1977); Annots., 56 A.L.R. 1391 (1928), 122 A.L.R. 144 (1939). Illustration 2 is based on Gunsch v. Gunsch, 71 N.W.2d 623 (N.D.1955); cf. Socony Mobil Oil Co. v. Continental Oil Co., 335 F.2d 438 (10th Cir.1964); see Annots., 138 A.L.R. 205 (1942), 148 A.L.R. 1361 (1944).

Comment c. See Trubowitch v. Riverbank Canning Co., 30 Cal.2d 335, 182 P.2d 182 (1947); Union Bond and Trust Co. v. M and M Wood Working Co., 256 Or. 384, 474 P.2d 339 (1970); Detroit Greyhound Emp. Fed. Credit Union v. Aetna Life Ins. Co., 381 Mich. 683, 167 N.W.2d 274 (1969). But see Rother-Gallagher v. Montana Power Co., 164 Mont. 360, 522 P.2d 1226 (1974). As to franchise agreements, see Annot., 59 A.L.R.3d 244 (1974). As to certificates of deposit, see Annot., 59 A.L.R. 1478 (1929). As to assignment of wages, see Annot., 76 A.L.R. 1304 (1932).

Comment d. That a waiver by the obligor must be clear and unequivocal, and that the assignee of an ineffective assignment retains rights against the assignor, see Paul v. Chromalytics Corp., 343 A.2d 622 (Del.Super.Ct.1975). Illustration 3 was Illustration 1 to former § 176. Illustration 4 is based on Bimestefer v. Bimestefer, 205 Md. 541, 109 A.2d 768 (1954); cf. Thomas v. Thomas, 192 Cal.App.2d 771, 13 Cal.Rptr. 872 (1961).

Case Citations - by Jurisdiction

—

C.A.3,
C.A.3
C.A.7
C.A.8
C.A.9
C.A.9, Bkrtcy.App.
C.A.10
C.A.D.C.
Ct.Fed.Cl.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

D.Del.
D.Del.Bkrtcy.Ct.
M.D.Fla.Bkrtcy.Ct.
N.D.Ga.
N.D.Ga.Bkrtcy.Ct.
S.D.Ga.Bkrtcy.Ct.
N.D.Ill.
S.D.Ind.
D.Kan.
D.Md.
D.Mass.
E.D.Mich.
W.D.Mich.Bkrtcy.Ct.
S.D.N.Y.
E.D.N.C.
N.D.Ohio
D.Or.
E.D.Pa.
W.D.Pa.
W.D.Tenn.
E.D.Va.
E.D.Wis.
Ala.
Ala.App.
Colo.
Colo.App.
Conn.
Del.Super.
Fla.App.
Ga.App.
Idaho,
Idaho App.
Ill.App.
Kan.
Kan.App.
Mass.App.
Mich.App.
Minn.
Minn.App.
Mo.App.
Mont.
Neb.App.
Nev.
N.H.
N.J.
N.J.Super.
N.M.
N.M.App.
N.Y.Sup.Ct.

Okl.
Pa.Super.
Tenn.App.
Tex.App.
Utah
Wash.App.
Wis.App.

C.A.3,

C.A.3, 2018. Com. (a) quot. in sup. Medical provider that performed surgery on patient who participated in a health-insurance plan governed by ERISA, acting as assignee of patient's claims and under a limited power of attorney granted by patient, sued issuer of the plan after it failed to reimburse provider for services provided to patient, alleging violations of ERISA and breach of contract. The district court granted defendant's motion to dismiss for lack of standing based on an anti-assignment clause contained in the plan. Affirming, this court held that anti-assignment clauses in ERISA-governed health-insurance plans were enforceable. The court cited Restatement Second of Contracts § 322 in support of its conclusion that a plan trustee could limit the ability of a beneficiary to assign claims, because, among the parties' power to limit the rights created by their agreement was the power to restrict ownership interest to particular holders. American Orthopedic & Sports Medicine v. Independence Blue Cross Blue Shield, 890 F.3d 445, 454.

C.A.3

C.A.3, 1999. Cit. in headnotes and sup., quot. in case quot. in sup. An American lubricant manufacturer sued to compel its South African distributor and the distributor's directors and officers to arbitrate the manufacturer's claims of unfair competition, fraud, and misappropriation. New Jersey federal district court ordered defendants to arbitrate plaintiff's claims. This court affirmed in part and reversed in part, holding that the distributor was bound to arbitrate the dispute and that the district court had personal jurisdiction over the directors and officers. The court concluded, however, that the directors and officers were not bound to arbitrate plaintiff's claims. The trade agreements' assignment clauses did not contain the requisite clear language to limit the predecessor assigning company's power to assign the trade agreements. The assignment to the distributor was therefore enforceable, and the distributor was bound to arbitrate claims relating to the trade agreements pursuant to their arbitration clauses. Bel-Ray Co., Inc. v. Chemrite (Pty) Ltd., 181 F.3d 435, 441-442.

C.A.7

C.A.7, 2003. Subsec. (2) and com. (c) quot. in sup. Secured creditors' agent claimed a security interest in Chapter 7 debtor's assets, including $14 million in a rabbi trust; trustee in bankruptcy claimed the assets for unsecured creditors. Bankruptcy court held that assets were not subject to security agreement, and so ruled for trustee. District court affirmed. On appeal, agent argued that Illinois law would enforce a contractual antiassignment provision, such as provision in the trust that forbade assigning a security interest in rabbi trust's assets to creditors, against an assignee only if provision stated that assignor had no power to assign. This court affirmed, concluding, inter alia, that while an antiassignment provision was unenforceable against assignee unless different intention was manifested, circumstances here weighed in favor of enforcing provision. Bank of America, N.A. v. Moglia, 330 F.3d 942, 948.

C.A.8

C.A.8, 1982. Subsec. (1) cit. in sup., subsec. (2)(b) quot. in sup. The assignees of contracts for the sale of real property sued the sellers for breach of contract and tortious interference with contracts. The district court dismissed on the grounds that the plaintiffs lacked standing to sue or, alternatively, that the plaintiffs initially breached the contracts and therefore could not recover for any breach by the defendants. This court reversed, holding that the plaintiffs had standing to use and under the

evidence presented, were entitled to recover for the sellers's breach of contract. The assignment clause in the contract served only as a restriction on delegation of duties, not on assignment of rights. There was no change in the sellers' duty to convey title to realty as a result of the assignment. Acceptance of the assignment by the assignee was presumed to be a promise to perform the assignor's unperformed duties. The exception to this rule was where the contract involved a sale of land. However, a valid and binding promise to assume the assignor's duties could be implied from the conduct of the assignees. In the instant case, an implied promise was found even though the assignees failed to comply with the contract's requirement of a written promise to assume the assignor's duties. It would be unreasonable to expect a written promise in a period of one day. The sellers could not avoid their duties under the contract on grounds that the assignor was made a limited partner of the assignee corporation instead of a general partner because it was evident that this was not an essential provision of the contract. Even if the right to assign was prohibited by the assignment clause, it did not render a subsequent assignment void. It merely gave rise to damages for breach of contract. Since the contract was therefore still enforceable after the assignment, the sellers' total repudiation of the contract gave the assignees a claim for damages for total breach of contract, and relieved the assignees of any further duties under the contract. Cedar Point Apartments v. Cedar Point Inv. Corp., 693 F.2d 748, 753, 754, certiorari denied 461 U.S. 914, 103 S.Ct. 1893, 77 L.Ed.2d 283 (1983), on remand 580 F.Supp. 507 (1984), judgment affirmed as modified 756 F.2d 629 (8th Cir.1985).

C.A.9

C.A.9, 1991. Com. (a) cit. in disc. Dentists who did not participate in a nonprofit health care plan providing dental benefits to employees under a welfare benefit plan governed by ERISA and thus were not paid directly by the plan but had to collect from the plan beneficiaries, who were then reimbursed by the plan, sued the plan for a preliminary injunction to order it to honor assignments by beneficiaries of their rights to payment from the plan to the plaintiffs. The district court granted the injunction. Reversing and remanding, this court held that the beneficiaries of an ERISA welfare benefit plan could not assign their payment rights in the face of an express nonassignment clause in the plan. Davidowitz v. Delta Dental Plan of California, 946 F.2d 1476, 1478.

C.A.9, 1990. Subsec. (2) and com. (a) quot. in disc. When an airline sued a discount ticket broker, the district court entered a permanent injunction prohibiting the company from brokering the airline's frequent flyer coupons. Affirming in part, vacating in part, and remanding, this court held, inter alia, that the public policy against restraints on free alienation of property was inapplicable to frequent flyer coupons and presented no barrier to the enforcement of the airline's tariffs against holders of brokered coupons. In concluding that traditional restraints upon the alienation of property rights did not apply, the court emphasized the contractual nature of frequent flyer coupons and found that the coupons did not embody rights of property. The court compared the common law of property, which has categorically condemned disabling restraints, with the common law of contracts, in which the hostility toward assignment of contractual rights has almost completely disappeared except where there is an explicit contractual provision forbidding assignment. TransWorld Airlines v. American Coupon Exchange, 913 F.2d 676, 685.

C.A.9, Bkrtcy.App.

C.A.9, Bkrtcy.App.2005. Cit. in disc., quot. in case cit. in sup., quot. in ftn. Chapter 13 debtor brought adversary proceeding to avoid creditor's security interest in annuity payments from debtor's structured tort settlement agreement, the rights to which she had assigned to creditor despite a nonassignment clause in the agreement. The bankruptcy court granted summary judgment for debtor. Affirming, this court held, inter alia, that, under general contract principles, where the intent of the parties was clear and the nonassignment clause was unambiguous, the clause was enforceable, and the provisions of UCC Article 9 would not operate to bar such enforcement where the settlement agreement was based on a tort claim. In re Gallagher, 331 B.R. 895, 900, 904.

C.A.10

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

C.A.10, 1988. Subsec. (2)(b) cit. in sup. A corporation and an accounting firm were involved in several transactions relating to sales of health club memberships and of interests in companies engaged in that business and its financing. The corporation sued several individual defendants and the accounting firm, asserting claims under the federal securities laws. The district court entered judgment on a jury verdict finding the individual defendants liable and the accounting firm not liable. Affirming, this court held, inter alia, that the trial court was correct in its determination that a provision prohibiting assignment of rights in a 1973 purchase agreement involving the sale of a financing company to a subsidiary of the plaintiff did not prevent the subsidiary's subsequent assignment to the plaintiff of its legal claims arising out of the sale. U.S. Industries, Inc. v. Touche Ross & Co., 854 F.2d 1223, 1234.

C.A.D.C.

C.A.D.C.1971. Section 154 of Tentative Draft 3 which is now Section 322 of the Official Draft quot. in part, com. d quot. in ftn., and com. a quot. in part in sup. Plaintiff sub-subcontractor sued defendant subcontractor and defendant's surety for breach of contract. Plaintiff won a judgment and the surety paid the amount of the judgment into the registry of the court. Then, the United States and the prime contractor intervened asserting claims, based on amounts allegedly due to them from the plaintiff, to the funds. The plaintiff had assigned to the prime contractor all monies due and to become payable under its contract with the defendant, as security for a loan from the prime contractor, without the consent of the defendant even though the contract required the defendant's consent for such an assignment. The prime contractor's claim for the past due loan was based on this assignment and the United States' claim was based on a tax lien filed after the assignment. The issue between the prime contractor and the United States was which had first priority to the plaintiff's money judgment, it being assumed that the prime contractor had priority only if the assignment from the plaintiff was valid. The United States claimed that the lack of permission from the defendant for the assignment made it completely invalid. The court rejected this claim and followed the canon of interpretation that the contractual prohibition against assignment was for the benefit of the defendant only absent any expression in the contract of a contrary intention, and that it had no effect upon the relationship between the prime contractor's rights against the plaintiff and the United States' rights against the plaintiff. Thus, the United States could not assert the lack of defendant's permission for the assignment as grounds for declaring the assignment invalid in the face of the United States' claim. Fox-Greenwald Sheet Metal Co. v. Markowitz Bros., Inc., 147 App.D.C. 14, 452 F.2d 1346, 1351-1353.

Ct.Fed.Cl.

Ct.Fed.Cl.2006. Subsec. (2)(a) quot. in sup. Bank sued the United States, alleging that passage of the Financial Institutions Reform, Recovery and Enforcement Act breached certain supervisory-merger contracts that bank's predecessors-in-interest had entered with government. Granting in part bank's motion for summary judgment on liability, this court held, inter alia, that government was liable to bank for breach of the express contracts. The court found that bank's express contract claims were not barred on the ground that bank's predecessors-in-interest did not obtain written consent to transfer rights under an assistance agreement in connection with previous mergers and acquisitions, noting that a contractual prohibition on assignment of rights would not forbid assignment of a right to damages for breach of the whole contract. Holland v. U.S., 74 Fed.Cl. 225, 257.

D.Del.

D.Del.2015. Cit. in sup.; subsec. (1) quot. in sup. and in ftn. Purchaser of ophthalmic products from distributor, as assignee of distributor's claims under a distribution-services agreement with seller, filed a putative class action against seller and other owners or licensees of patents for the products, alleging antitrust violations. This court granted seller's motion to dismiss for lack of subject-matter jurisdiction, holding that the agreement's anti-assignment clause restricted distributor from assigning its right to bring suit against seller. The court noted that its decision was consistent with Restatement Second of Contracts § 322 —which provided that, unless circumstances indicated otherwise, a contract term prohibiting assignment of a contract barred only the delegation to an assignee of the performance by the assignor of a duty or condition—because the agreement at issue

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

indicated that the right to bring an antitrust action could not be assigned from a direct purchaser to an indirect purchaser. Hartig Drug Company Inc. v. Senju Pharmaceutical Co. Ltd., 122 F.Supp.3d 202, 207, 208.

D.Del.Bkrtcy.Ct.

D.Del.Bkrtcy.Ct.2018. Subsec. (1) cit. but dist. and quot. in ftn.; subsec. (2) cit. and quot. in disc., cit. in ftn.; com. (a) quot. in disc.; Rptr's Note cit. in disc. Chapter 11 debtors objected to a proof of claim filed by purported assignee of three promissory notes that debtors had signed in favor of lenders, alleging that lenders' attempt to assign the notes was null and void under the anti-assignment clauses contained in the notes. This court sustained debtors' objection, finding that the anti-assignment clauses were enforceable and that lenders' attempted assignment of the notes was void. The court rejected assignee's argument that it had purchased only the notes' underlying claims or causes of actions, rather than the notes themselves, and that, under Restatement Second of Contracts § 322, the clauses did not bar lenders' ability to transfer their rights, claims, or causes of action related to the notes, noting that § 322 applied to contracts for the sale of goods, rather than to promissory notes. In re Woodbridge Group of Companies, LLC, 590 B.R. 99, 104, 105.

M.D.Fla.Bkrtcy.Ct.

M.D.Fla.Bkrtcy.Ct.1999. Subsec. (1) cit. in headnote and quot. in disc. Chapter 7 trustee sued for a determination that the debtor railroad employee's right to payments under an annuity contract was not validly assigned prepetition and was included in the estate's property. The assignee counterclaimed for a determination as to the nondischargeability of the debtor's obligation for payments wrongfully obtained. This court entered judgment for creditor, holding, inter alia, that while debtor's assignment of payments from an annuity purchased to facilitate a structured settlement agreement frustrated the intent of that agreement, no legal basis existed to invalidate the transaction between debtor and purchaser. The language of the annuity contract did not specifically prohibit the sale of debtor's right to receive payments. In re Berghman, 235 B.R. 683, 690.

M.D.Fla.Bkrtcy.Ct.1999. Subsec. (1) quot. in sup. Chapter 7 debtor moved for an award of sanctions against company that purchased his annuity, alleging that company's refusal to release a writ of garnishment on sums belonging to the bankruptcy estate constituted a violation of the automatic stay. Specifically, debtor argued that, because an anti-assignment provision in his settlement agreement with payer of annuity was valid, the purchase agreement he executed with garnishing party was invalid, and therefore the sums at issue were estate property. Denying the motion, the court held that debtor failed to show that his case came within an exception to the general rule allowing the assignment of the right to receive contractual payments. In re Freeman, 232 B.R. 497, 502.

N.D.Ga.

N.D.Ga.1999. Quot. in ftn. After insurer refused to honor its obligation, assignee of the right to receive periodic payments from insurer sought declaration that assignment was valid and enforceable under the terms of the settlement agreement executed by insurer and original payee. Entering summary judgment for assignee, the court held, in part, that the agreement's prohibition against original payee's right to accelerate, defer, increase, or decrease the payments did not constitute antiassignment provision, and that, even if it did, insurer's remedy was damages, not avoidance of the assignment. Settlement Funding, LLC v. Jamestown Life Ins. Co., 78 F.Supp.2d 1349, 1360.

N.D.Ga.Bkrtcy.Ct.

N.D.Ga.Bkrtcy.Ct.2000. Subsec. (1) quot. in sup. The bankruptcy trustee and the purchaser of part of debtor's interest in an annuity filed objections to debtor's Chapter 13 plan, arguing that the portion of the annuity bought by purchaser did not constitute estate property. Sustaining the objections, the court held that, under Georgia law, an antiassignment clause in the nonexecutory settlement agreement providing for the annuity payments to debtor did not bar debtor's partial assignment of his interest in the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

annuity, and that therefore the portion of the annuity's income stream transferred to purchaser was not property of the estate. In re Terry, 245 B.R. 422, 427.

S.D.Ga.Bkrtcy.Ct.

S.D.Ga.Bkrtcy.Ct.1999. Subsec. (2) cit. in disc. After Chapter 7 trustee moved to sell benefits owing to debtor arising from prepetition settlement of tort claim for wrongful death of her husband, insurance company that provided annuity for periodic payments of structured settlement intervened and objected to sale of settlement benefits. Granting trustee's motion, the court held, inter alia, that antiassignment provision in settlement agreement was unenforceable, where debtor had fully performed her duties under agreement, and insurance company, as obligor, would not suffer significant harm as a result of the assignment. In re Cooper, 242 B.R. 767, 771.

N.D.Ill.

N.D.Ill.2015. Subsec. (2) quot. in sup. and cit. in case cit. in sup. Winning bidder of a contract to perform work at a research facility—which assigned its rights under the contract to a third party with facility owner's consent, but was later reassigned those rights from the third party without owner's consent—sued owner for breach of contract, alleging that it incurred cost overruns because the work was more difficult, costly, and time-intensive than defendant had represented in the bidding documents. This court denied defendant's motion to dismiss, holding that plaintiff's claims were not barred by the contract's anti-assignment provision. Although it was undisputed that defendant did not consent in writing to the third party's reassignment of its rights under the contract back to plaintiff, Illinois followed the modern view expressed in Restatement Second of Contracts § 322, which provided that an anti-assignment provision did not prohibit the assignment of a contractual right to sue for money damages. Omicron Safety and Risk Technologies, Inc. v. UChicago Argonne, LLC, 181 F.Supp.3d 508, 510-512.

N.D.Ill.1993. Subsec. (2)(a) quot. in disc. and cit. in sup., subsec. (2)(b) cit. and quot. in disc. Company affiliated with the assignee of the contract rights of a shopping center owner sued a consulting engineer for faulty design and construction of the shopping center. Defendant moved to dismiss on the ground that nonassignability clauses in its contract with its original client voided assignment of any part of the contract absent its written consent. Denying defendant's motion, the court held that although the nonassignability clauses prohibited assignment of the duties and responsibilities of the contract while it was still executory, they did not clearly and unambiguously prohibit the assignment of the right to pursue a claim for breach of contract once the contract was fully performed. Lomas Mortg. v. W.E. O'Neil Const., 812 F.Supp. 841, 843-845.

S.D.Ind.

S.D.Ind.2006. Subsec. (1) quot. and cit. in sup. Owner of recording studio brought, as part of a broader action, breach-of-contract claim against software company to whom it licensed voice recordings for use in software in exchange for company's stock, after company licensed its right to sell the software to another company and then became, in essence, defunct, rendering plaintiff's stock worthless. Granting judgment for defendants, this court held, inter alia, that, because the anti-assignment provision in the contract between the parties failed to clearly state that it was intended to prohibit company's assignment of rights under the contract, the provision referred only to the delegation of contractual duties, not to the assignment of rights. Traicoff v. Digital Media, Inc., 439 F.Supp.2d 872, 879, 880.

D.Kan.

D.Kan.1986. Com. (b) quot. in sup. A hospital and a health care finance supplier sued a competing supplier of health care financing for state and federal antitrust violations, alleging that the defendant's threatened termination of its care provider contract with a major supplier of hospital care was for the sole purpose of harming its competitor. The court denied the defendant's motion for summary judgment on the antitrust claims, and refused to validate the "nonassignment of benefits

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

to noncontracting facilities” clause in the defendant's subscribers' policies, holding that well-established policy favored free alienability of contract rights, and that the health care financing provider was not permitted to refuse to honor the assignment where the prohibition against assignment served no legitimate interest of the obligor. Reazin v. Blue Cross & Blue Shield of Kansas, Inc., 635 F.Supp. 1287, 1335.

D.Md.

D.Md.2000. Cit. in sup., cit. generally in case cit. in sup., subsec. (2)(b) cit. and quot. in sup. Insurance companies sought declaratory relief to resolve the rights and duties of the parties under a personal-injury settlement agreement and its funding annuity. This court held that the settlement agreement manifested an intent to deny insured the power to assign his rights to the periodic payments, and therefore his assignment of monthly annuity payments to a financial firm was void as validly precluded by contract. Liberty Life Assurance Company of Boston v. Stone Street Capital, Inc., 93 F.Supp.2d 630, 637, 638.

D.Mass.

D.Mass.2008. Subsec. (c)(2)(b) quot. in ftn. Export-trading company sued manufacturer of LCD displays and the purchaser of manufacturer's assets for, in part, breach of contract in connection with manufacturer defendant's sale of certain specialized aircraft LCD displays to plaintiff, and purchaser defendant's failure to provide contracted-for support to plaintiff. Granting plaintiff's motion for partial summary judgment on the issue of assignment, this court held, inter alia, that the unambiguous terms of the asset-purchase agreement between the two defendants established that manufacturer fully assigned all of its contracts with plaintiff to purchaser. The court rejected purchaser's argument that a nonassignment clause in those contracts prevented them from being assigned; rather, such clause could provide plaintiff with a cause of action for damages against defendant manufacturer for breaching the clause. Atlantech Inc. v. American Panel Corp., 540 F.Supp.2d 274, 283.

E.D.Mich.

E.D.Mich.1998. Cit. in headnote, subsecs. (1) and (2)(c) quot. in sup. Beneficiary of annuity contract sought declaration that anti-assignment provision contained in the policy was invalid and unenforceable. Entering judgment for beneficiary, the court held that the provision was not unenforceable under § 9-104(g) of the U.C.C.; however, the current trend with respect to contractual prohibitions on assignments was to interpret such clauses narrowly, as barring only the delegation of the performance of a duty or condition, and not necessarily precluding the assignment of rights from assignor to assignee. Wonsey v. Life Ins. Co. of North America, 32 F.Supp.2d 939, 940, 943.

W.D.Mich.Bkrtcy.Ct.

W.D.Mich.Bkrtcy.Ct.2004. Subsec. (1) quot. in sup. Settlement capital company that prepetition was assigned bankruptcy debtor's rights to remaining annuity payments received from insurer in settlement of tort claim moved to have bankruptcy stay lifted, alleging that payments were not property of the estate. Granting the motion in part so that settlement capital company could continue to receive future payments, the court found that although the settlement agreement contained an anti-assignment clause, debtor maintained the right to sell her interest in the annuity without insurer's consent and irrespective of the clause because she had no remaining contractual duties or obligations left to perform. In re Jackson, 311 B.R. 195, 201.

W.D.Mich.Bkrtcy.Ct.2000. Cit. in ftn. Settlement funding company to which debtor husband had made a prepetition assignment of his right to receive periodic payments under a structured settlement agreement objected to confirmation of debtors' Chapter 13 plan, which provided for funding of the plan with the settlement payments. Entering judgment for settlement funding company, the court held that debtor's prepetition assignment was valid under Michigan law; thus the payment stream was not property of the bankruptcy estate, and debtors could not use it to fund their Chapter 13 plan. In re Brooks, 248 B.R. 99, 105.

S.D.N.Y.

S.D.N.Y.2013. Cit. in sup. In three coordinated actions, healthcare provider sued ERISA and non-ERISA welfare benefit plans, seeking payment for close to 200 surgical procedures performed on plan members. Granting in part defendants' motions to dismiss, this court held, inter alia, that plaintiff failed to demonstrate that it received valid assignments of rights from plan members with respect to claims arising under ERISA-governed welfare plans containing certain anti-assignment clauses, specifically, personal-rights clauses and limited-circumstances clauses, and thus it lacked standing to bring those claims under ERISA. The court rejected plaintiff's argument that the breach of anti-assignment clauses by plan members entitled defendants to damages from the plan members, but did not affect the validity of the assignments to plaintiff, explaining that New York considered an assignment void when contracts unambiguously prohibited assignments. Neuroaxis Neurosurgical Associates, PC v. Costco Wholesale Co., 919 F.Supp.2d 345, 356.

S.D.N.Y.2005. Subsecs. (2)(a)-(2)(b) cit. in ftn. Health-services broker and network administrator sued administrators of insurance benefit plans, to whom plaintiffs provided access to provider organizations in exchange for a percentage of the savings realized by defendants from providers' reduced rates, alleging, in part, breach of contract. Denying in part defendants' motion for summary judgment, the court held, inter alia, that although plaintiff-broker assigned its rights under the contract to a successor organization formed between plaintiff-broker and another company, the successor organization stood in the shoes of plaintiff-broker as the original party to the contract, and thus had the same rights and obligations thereunder, including the right to seek relief for defendants' alleged breach. Health Alliance Network, Inc. v. Continental Casualty Co., 354 F.Supp.2d 411, 417.

E.D.N.C.

E.D.N.C.2008. Cit. in disc. and sup.; subsec. (2) cit. in disc. and sup., and cit. in case cit. in sup.; subsec. (2)(a) cit. in disc. and sup. (erron. cit. as § 322(a)(2)); subsec. (2)(b), coms. (a) and (b), and illus. (1) and (2) cit. in sup. After purchaser agreed to purchase nearly all of company's assets, and company and its secured creditors created a trust to liquidate company's assets and assigned company's right to receive the proceeds from company's agreement with purchaser to trust, trustee sued for breach of contract when purchaser refused to pay under the agreement. Denying purchaser's motion for summary judgment, this court held, inter alia, that company's assignment of its right to receive the proceeds of the sale to trust was not void under the agreement's anti-assignment clause. The court noted that policy rationales underlying anti-assignment clauses were not implicated here; company's personal performance was immaterial because the recipient of the money was fungible, and, relatedly, there was no risk of double liability because company stated that payment was due only to trustee. Gallagher v. Southern Source Packaging, LLC, 564 F.Supp.2d 503, 506-508, 514, 515.

N.D.Ohio

N.D.Ohio, 2007. Subsec. (1) cit. and quot. but dist., com. (a) quot. in sup. Company that financed construction of operator's emissions-testing stations, and then leased them back to operator under a master lease agreement, sued operator's successor, alleging, in part, breach of the agreement's anti-assignment clause, after operator's stock was sold to defendant, but operator assigned and transferred to its previous owner all of its right, title, and interest in the security deposit that plaintiff was obligated to repay. Denying defendant's motion for summary judgment, this court held, inter alia, that the general rule permitting assignments was inapplicable, and the anti-assignment clause was enforceable, because it contained language that specifically prohibited assignment of both contractual rights and duties, and specifically stated that the parties were bound by it. Ohio Environmental Development Ltd. Partnership v. Envirotest Systems Corp., 478 F.Supp.2d 963, 979-981.

D.Or.

D.Or.1986. Subsec. (2) cit. in disc. A union sued a logging company for breach of an alleged contract to reach a working agreement with logging employees when the defendant decided to end logging operations and laid off 62 of 68 logging

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

employees. This court dismissed the union's claims, holding that the parties' Memorandum of Agreement was not an enforceable contract, nor was it enforceable as a "agreement to agree." The court reasoned that key terms of the agreement failed to define the nature and extent of the parties' obligations with reasonable certainty and provided no basis for determining the occurrence of a breach or for providing a remedy. The court added that for an agreement to agree to have effect, accord must have been expressed on all essential terms. Local 3-7, Intern. Woodworkers v. Daw Forest Products Co., 643 F.Supp. 122, 124.

E.D.Pa.

E.D.Pa.2001. Cit. in disc. Buyer and seller of an annuity sought declaration that purported assignments between the annuitant and a purchaser of the annuitant's right to payments, as well as between the purchaser and the assignee of the purchaser's rights, were void and unenforceable, as was a state court judgment upholding the assignments. This court granted plaintiffs' motions for summary judgment, holding that the antiassignment clause in the settlement agreement was enforceable, and therefore, as against the plaintiffs, that portion of the state court judgment decreeing that assignee was entitled to collect five payments directly from plaintiffs was null and void. CGU Life Ins. Co. of America v. Metropolitan Mortg. & Securities Co., Inc., 131 F.Supp.2d 670, 678.

W.D.Pa.

W.D.Pa.2012. Cit. and quot. but not fol. Assignee of franchisor under a franchise agreement for the operation of a retail store sued franchisees, seeking to compel franchisees to arbitrate disputes stemming from the agreement. Denying assignee's motion for summary judgment, this court held that a genuine dispute of material fact existed as to whether assignee could enforce the agreement's arbitration clause, in light of franchisees' allegations that the assignment violated the agreement. While some courts had found that a contractual clause restricting assignment nevertheless resulted in a valid assignment and simply entitled the obligor to damages for breach of contract, any assignment made contrary to contractual language restricting or prohibiting assignment was ineffective and void under North Carolina law. STS Refills, LLC v. Rivers Printing Solutions, Inc., 896 F.Supp.2d 364, 372, 373.

W.D.Tenn.

W.D.Tenn.1996. Com. (a) cit. in case quot. in disc. In ERISA action, hospital/assignee sued employee welfare benefit plan to recover costs incurred in treating plan participant/assignor. Defendant moved for summary judgment on the ground that any purported assignment of participant's medical benefits was invalid under the antiassignment provision of his insurance plan. Denying the motion, the court held, in part, that ERISA-regulated plans were functionally trusts; that assignments furthered the goals of ERISA while protecting beneficiaries; and that summary judgment was inappropriate because the antiassignment provision was ambiguous when read in light of other plan provisions specifically allowing for direct payment from defendant to medical providers. Univ. of TN. Wm. F. Bowld Hosp. v. Wal-Mart Stores, 951 F.Supp. 724, 729.

E.D.Va.

E.D.Va.2003. Quot. in sup. Construction contractor sued subcontractor that was hired to perform demolition, disposal, and excavation work and the surety that issued performance and payment bonds on subcontractor's behalf, alleging that subcontractor breached the subcontracts. This court granted surety's motion to enforce settlement reached between plaintiff and surety and to dismiss subcontractor's counterclaims, holding that, through the settlement, plaintiff effectively waived its right to challenge assignment of subcontracts to surety. The court held that anti-assignment provisions did not render assignment of subcontracts to surety, by operation of the indemnity agreement, invalid. Plaintiff did not object in any way to the assignment, and anti-assignment provisions were for plaintiff's benefit and protection. Bell BCI Co. v. Old Dominion Demolition Corp., 294 F.Supp.2d 807, 813.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

E.D.Wis.

E.D.Wis.2011. Cit. in ftn. (citing § 154, T.D. No. 3, 1967, which is now § 322 of the Official Text). Insured property owner and its assignee brought a breach-of-contract action against excess insurer, alleging that, after the property sustained damage from Hurricane Katrina, defendant denied its obligation under the insurance policy to reimburse insured for repairs and replacement. While this court denied plaintiffs' motion for summary judgment, it held, as a matter of first impression, that, even though the policy contained a clause barring insured's transfer of its rights and duties under the policy without defendant's consent, the Supreme Court of Mississippi would find that the transfer to assignee of insured's right to repair-and-replacement proceeds-post-loss but prior to actual repair or replacement-was valid. Edgewood Manor Apartment Homes LLC v. RSUI Indem. Co., 782 F.Supp.2d 716, 735.

Ala.

Ala.2001. Com. (d) quot. in sup. Insured sued health insurer and car insurer for breach of contract and fraud in connection with car insurer's payment of benefits to health insurer. Trial court entered judgment on jury verdict for insured. This court reversed the judgment against car insurer, holding, inter alia, that car insurer was not liable for breach of contract, because its payment was made in accordance with its policy and as directed by insured's subrogation agreement with health insurer. The court rejected insured's assertion that car insurer violated the policy provision against assignments by honoring the subrogation agreement, stating that insured's assignment of the right to payment could constitute a breach only on the part of insured, not car insurer. Thus, car insurer's honoring of the assignment would constitute, if anything, a waiver of the policy's consent requirement. Auto-Owners Ins. Co. v. Abston, 822 So.2d 1187, 1193.

Ala.App.

Ala.App.1996. Subsec. (2)(b) cit. in disc. and cit. but dist. Customers of a waste collection company sued the company and an affiliated corporation, seeking a judgment declaring that their service agreements with defendants were void for breach of the nonassignment clause contained therein. Affirming in part the trial court's entry of judgment for plaintiffs, this court rejected defendants' argument based on Restatement (Second) of Contracts § 322(2)(b) that the trial court incorrectly held the service agreements at issue to be automatically void. Stating that § 322(2)(b) did not apply, the court said that the trial court did not hold that the agreements were automatically void, but rather that they were voidable at the option of the customer; further, the transfer at issue in this case was not an assignment, but a sale of assets. ISS Intern. v. Ala. Motor Express, 686 So.2d 1184, 1189.

Colo.

Colo.2011. Subsec. (2)(a) cit. and quot. in sup., subsec. (2)(b) cit. in case cit. in ftn., com. (c) cit. and quot. in sup. After ex-husband assigned ex-wife his rights to vote in and receive distributions from LLC, ex-wife sued other members of LLC, alleging that members' subsequent purchase of ex-husband's membership interest tortiously interfered with the prior assignment to her. The trial court granted summary judgment for defendants; the court of appeals affirmed. Affirming, this court held that an anti-assignment clause in LLC's operating agreement rendered ex-husband powerless to make the nonconforming transfer to plaintiff. The court concluded that, given the plain meaning of the operating agreement, which prohibited assignments that—like this one—were not consented to by all LLC members, and given the clear public policy in favor of allowing the members of a closely-held LLC to tightly control who could receive rights or duties under the operating agreement, the assignment had no legal effect. Condo v. Conners, 266 P.3d 1110, 1112, 1114, 1116-1119.

Colo.App.

Colo.App.2010. Subsec. (2)(b) quot. in disc. Former wife, who, as part of a divorce settlement, was assigned ex-husband's right to monetary distributions from a limited-liability company (LLC) of which he was a member, brought, inter alia, a claim

for tortious interference with contract against the other members and the LLC's attorney, after the other members purchased husband's membership interest from him. The trial court granted summary judgment for defendants. Affirming, this court held that, based on an anti-assignment clause in the LLC's operating agreement, the assignment to wife was void under Colorado law because it was obtained without written consent of the other members, and thus wife's tortious-interference action was not viable. The court noted that, in jurisdictions that followed the modern approach in determining the sufficiency of anti-assignment clauses, as opposed to the classical approach followed by Colorado courts, a contract term that merely prohibited the right to assign contractual rights gave the obligor a right to damages for breach of the terms forbidding assignment but did not render the assignment ineffective. Condo v. Conners, 271 P.3d 524, 528.

Conn.

Conn.2000. Cit. in sup., cit. and quot. in diss. op., subsec. (2)(b) quot. in sup., subsec. (c) and com. (a) quot. in diss. op. Payee under structured settlement agreement sought declaration that antiassignment clause in annuity was unenforceable. The trial court entered judgment for payee. Affirming, this court held that an antiassignment clause that did not expressly limit the power, rather than the right, to assign payments did not make an assignment ineffective; however, breach of the clause gave rise to payer's right to sue either payee or assignee for damages. Dissent believed that the language of the antiassignment provision, which was presumed to be a product of fair dealing and negotiation, was sufficiently clear and unambiguous to permit its enforcement. Rumbin v. Utica Mut. Ins. Co., 254 Conn. 259, 757 A.2d 526, 528, 530, 535-537, 541.

Del.Super.

Del.Super.1975. Section 154 of Tentative Drafts 1 through 7, Revised and Edited, which is now Section 322 of the Official Draft quot. in part in sup. A corporation president brought this action against the purchasing corporation's assignee and the corporation. Plaintiff sought, inter alia, payment for promissory notes assigned him by the corporation and damages for breach of an employment contract by the purchaser's assignee. The purchaser's assignee contended that plaintiff lacked standing to sue on the promissory notes by virtue of a contract provision prohibiting assignment of rights under the contract without the consent of the purchaser. The court held that the corporation's assignment of promissory notes to plaintiff was void as to the purchaser and the purchaser's assignee, in the absence of a clear, distinct, and unequivocal waiver of the purchase agreement's consent requirement. Nevertheless, the court upheld plaintiff's action against the corporation assignor. Motions of summary judgment and for dismissal, granted in part, denied in part. Paul v. Chromalytics Corp., 343 A.2d 622, 626.

Fla.App.

Fla.App.1991. Subsec. (1) quot. in sup. The assignee of a commercial tenant's right to receive a construction allowance from its landlord sued the landlord for the amount of the allowance. The trial court awarded the defendant summary judgment. Reversing and remanding, this court held that the lease provision barring the assignment of "the lease" did not bar the tenant from assigning its right to receive the allowance. Aldana v. Colonial Palms Plaza, Ltd., 591 So.2d 953, 955.

Ga.App.

Ga.App.2015. Subsecs. (1) and (2)(a) quot. in sup. After insurer and reinsurer filed a joint demand for arbitration against claims manager in connection with its allegedly negligent handling of a claim, claims manager moved to stay arbitration. The trial court denied claims manager's motion and granted insurer and reinsurer's cross-motion to compel arbitration, finding that insurer's assignment to reinsurer of its right to pursue arbitration against claims manager was valid and enforceable. Affirming, this court held that the assignment did not violate the anti-assignment provisions of insurer's claims-management agreement with claims manager, because no claims-handling services remained to be performed at the time of the assignment. The court noted that, under Georgia law and Restatement Second of Contracts § 322, unless the circumstances indicated otherwise or a different intention was shown, a contract term prohibiting assignment of a contract barred only the delegation to an assignee

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

of the performance by the assignor of a duty or condition; it did not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of its entire obligation. McLarens Young Intern., Inc. v. American Safety Cas. Ins. Co., 780 S.E.2d 464, 467.

Ga.App.2001. Cit. in disc. Payor under structured settlement agreement sued for a declaratory judgment that payees' sale and assignment to assignee of future payments under the agreement in exchange for the present payment of a discounted lump sum was invalid; payees counterclaimed for a declaration that the sales were valid. The trial court denied payor's motion for summary judgment, and granted payees' and assignee's cross-motion for partial summary judgment as to the validity of the assignments. Reversing in part, this court upheld the agreement's nonassignment clause. Affirming in part, the court held that, to be enforceable, antiassignment language need not specify that an assignment was "invalid" or "void," or that the obligor had the right to disregard any assignment. CGU Life Ins. Co. v. Singer Asset Finance Co., LLC, 250 Ga.App. 516, 525, 553 S.E.2d 8, 15, judgment affirmed 275 Ga. 328, 567 S.E.2d 9 (2002).

Idaho,

Idaho, 2019. Com. (e) quot. in disc. Property owners brought a declaratory-judgment action against real-estate investor and investor's successor in interest, alleging that a right-of-first-refusal provision to plaintiffs' property, which was sold to investor through an addendum to a previous deed conveying a different parcel of plaintiffs' property, could not be enforced against investor's heirs and successors, because the right was personal to plaintiffs and investor, and not binding on the parties' successors. The trial court granted plaintiffs' motion for declaratory judgment. This court vacated the trial court's ruling and remanded, holding that, while the right of first refusal was personal to the parties and nonassignable, the right was not extinguished when investor attempted to assign it to successor. The court cited Restatement Second of Contracts § 322 in explaining that the fact that investor lacked the right to assign did not render the assignment ineffective, but rather only gave plaintiffs a right to sue for damages. Mulberry v. Burns Concrete, Inc., 435 P.3d 509, 514.

Idaho App.

Idaho App.1997. Subsec. (2) quot. in disc. Buyers and seller entered into an agreement for the sale of farm property. Four months later, the parties executed an option agreement giving the seller the right to repurchase the same real property at any time during the existence of the escrow. After buyers decided to sell the property, seller brought an action seeking specific performance of the option agreement. Buyers counterclaimed, requesting specific performance of the land sale contract or, alternatively, damages. Trial court granted judgment to seller and ordered that the buyers perform pursuant to the terms of the option agreement. This court affirmed, holding, inter alia, that the seller's assignment of the option right did not render his exercise of the option ineffective. Even if the seller held the option in his capacity as trustee of a living trust, the option was effectively exercised in this case. It was not necessary that the seller identify himself as a trustee or disclose the trust's interest in order to exercise the option. Dennett v. Kuenzli, 130 Idaho 21, 936 P.2d 219, 228.

Ill.App.

Ill.App.2006. Cit. but dist., subsecs. (1) and (2)(c) cit. and quot. but dist. After estate settled a wrongful-death action, estate administrator entered into an agreement with structured-settlement buyer to transfer a portion of the structured-settlement-payment rights in exchange for a lump-sum payment. Buyer petitioned for approval of the transfer, and annuity issuer and structured-settlement obligor objected. The trial court approved the transfer. Reversing and remanding for entry of an order dismissing the petition, this court held, inter alia, that no assignment was permitted under the settlement agreement because the clear and unambiguous language of the agreement specifically expressed the intention of the parties to prohibit assignment of any kind and for any duration. In re Foreman, 365 Ill.App.3d 608, 302 Ill.Dec. 950, 850 N.E.2d 387, 392-393.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Ill.App.2000. Subsec. (1) cit. in disc. Plaintiff in a negligence action filed a petition seeking court approval of an assignment of certain of the periodic payments due him under a structured settlement agreement. After the trial court approved the assignment, insurer that issued an annuity policy to fund the payments appealed. Reversing and remanding, this court held, inter alia, that the antiassignability provision of the agreement was enforceable against petitioner. Petitioner owed a duty to insurer not to assign the periodic payments, since such an assignment could result in the loss of favorable tax treatment. In re Nitz, 317 Ill.App.3d 119, 128, 250 Ill.Dec. 632, 640, 739 N.E.2d 93, 101.

Ill.App.1999. Cit. in disc. Personal injury plaintiff sued to allow assignment of annuity benefits he received from the settlement of a personal injury suit. Trial court refused to allow the assignment, holding that the settlement agreement clearly and unambiguously prohibited the parties from assigning any of the periodic payments. This court affirmed, holding, inter alia, that the antiassignment provision of the settlement agreement was a bargained-for provision that was intended to benefit all parties and, therefore, was enforceable against plaintiff. Henderson v. Roadway Express, 308 Ill.App.3d 546, 549, 242 Ill.Dec. 153, 156, 720 N.E.2d 1108, 1111.

Kan.

Kan.2002. Cit. and quot. in sup. Chiropractor sued patient-insured's automobile insurer for breach of contract after insurer claimed that insured could not assign her right to personal injury protection (PIP) benefits to chiropractor. The trial court granted insurer summary judgment. Reversing and remanding, this court held, inter alia, that as a matter of first impression, insurance policy's provision restricting assignment of post-loss PIP benefits was unenforceable as against Kansas public policy. Bolz v. State Farm Mut. Auto. Ins. Co., 52 P.3d 898, 902.

Kan.App.

Kan.App.2006. Quot. in sup. Contractor filed a demand for arbitration, alleging that developer owed payment for work performed under contract, and then, contractor assigned its right, title, and interest in the arbitration proceeding to bank. The arbitrator issued an award in favor of contractor, and the district court granted bank's petition to confirm the award. Affirming, this court held, inter alia, that the assignment was not prohibited by the contract's provision barring assignment; because contractor did not assign the contract itself, but instead assigned its choses in action, assignment of the right to damages for breach of the whole contract was not forbidden. Missouri Bank & Trust Co. v. Gas-Mart Development Co., Inc., 35 Kan.App.2d 291, 130 P.3d 128, 134.

Mass.App.

Mass.App.2008. Cit. but dist. After surety for city's general contractor paid subcontractor the full amount of its claim under a payment bond for its performance of abatement work on city's project to renovate a local community center, surety sought to recover the payment from city. The trial court dismissed part of surety's action. Reversing, this court held, inter alia, that the anti-assignment clause in the construction contract entered into by city and general contractor was not intended to eliminate subrogation rights otherwise held by surety. The court specifically refused to base its conclusion on language found in Restatement Second of Contracts § 322 limiting the scope of anti-assignment provisions noting that city could argue that the breadth of language in the anti-assignment provision might have constituted a “circumstance” indicating that the clauses were not to be given the narrow scope invited by the Restatement. Reliance Ins. Co. v. City of Boston, 71 Mass.App.Ct. 550, 559, 884 N.E.2d 524, 530, 531.

Mich.App.

Mich.App.2018. Subsecs. (1) and (2)(a) quot. in conc. and diss. op. Healthcare providers, on their own behalf and as assignees of patient who was injured in a car accident, brought a claim to recover medical expenses under the state's no-fault act against

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

patient's insurer, after insurer refused to pay their claims for services rendered to patient. The trial court granted summary judgment for insurer, finding that providers were not entitled to bring a direct action against insurer under Michigan law, and that an anti-assignment clause contained in the patient's policy prohibited him from assigning his claims to providers. This court reversed and remanded, holding that the clause was unenforceable to prohibit the assignment that occurred here—an assignment after the loss occurred of an accrued claim to payment—because it would violate Michigan public policy. The concurring and dissenting opinion noted that, under Restatement Second of Contracts § 322, a contract term prohibiting assignment of rights under a contract did not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his or her entire obligation. Jawad A. Shah, M.D., PC v. State Farm Mutual Automobile Insurance Company, 920 N.W.2d 148, 167.

Minn.

Minn.2009. Subsec. (2)(a) quot. in ftn. to conc. op. In separate cases, auto-glass vendors who repaired insureds' windshields and were assigned insureds' claims petitioned for arbitration after insurers paid them less than the amount that they directly billed insurers. After consolidating the cases, the court of appeals, among other things, agreed with the two trial courts that vacated the arbitrators' award for vendors, holding that the anti-assignment clauses in the respective insurance policies prohibited assignment of the policies as well as the loss proceeds. This court reversed and remanded to the trial courts. The concurring opinion agreed with the majority that the policies' anti-assignment clauses did not preclude policyholders' assignment of post-loss proceeds to vendors, but would not have relied on the state's statutory scheme in reaching that result, pointing instead to precedent holding that such assignments were not assignments of the policy but permissible assignments of choses in action. Star Windshield Repair, Inc. v. Western Nat. Ins. Co., 768 N.W.2d 346, 351.

Minn.2004. Quot. in disc., cit. and quot. but not fol., cit. in case cit. in sup., subsec. (2)(b) cit. in case quot. in disc. Assignee of shareholder's rights to compensation under management agreement with real-estate-development corporation filed demand for arbitration, after corporation canceled the agreement and refused to pay assignee the compensation allegedly due it. The trial court granted corporation's motion to stay arbitration, but the court of appeals reversed and remanded. Reversing, this court held that management agreement's nonassignment clause precluded assignment of the right to payment, even though the clause did not explicitly limit, beyond the express nonassignment terms contained in the clause, the power of assignment, or provide that any purported assignment be invalid or void. Travertine Corp. v. Lexington-Silverwood, 683 N.W.2d 267, 271, 272, 273.

Minn.App.

Minn.App.2003. Subsec. (2) quot. in sup. After corporation cancelled management agreement, manager's judgment creditor, as manager's purported assignee, filed demand for arbitration, alleging that it was entitled to compensation due manager under management agreement. Trial court granted corporation's motion to stay arbitration, holding that transfer of manager's right to compensation was not a valid assignment. This court reversed and remanded, holding that creditor received valid assignment of compensation due from corporation and that assignment allowed creditor to compel arbitration. The nonassignment clause did not render void the assignment of compensation, because management agreement did not explicitly limit manager's power to assign, nor did it explicitly render assignments void. Travertine Corp. v. Lexington-Silverwood, 670 N.W.2d 444, 447, reversed 683 N.W.2d 267 (Minn.2004).

Mo.App.

Mo.App.1983. Cit. in disc. In accordance with the licensor's right of first refusal under a license agreement, a licensee sent notice of an assignment of its interest in the agreement. The assignee promptly ordered goods from the licensor and made a royalty payment pursuant to the assigned agreement, but then sent notice of rescission of the assignment. Allegedly unaware of the rescission, the licensor sent notice of its acceptance of the assignment. In an action by the licensor, the trial court granted the assignee's motion to dismiss for lack of personal jurisdiction. This court affirmed, holding that although the assignee had

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

by its conduct become a party to the license agreement, the assignee did not have the minimum contacts necessary to satisfy the state's long-arm statute. Medicine Shoppe Intern., Inc. v. J-Pral Corp., 662 S.W.2d 263, 271.

Mont.

Mont.2000. Subsec. (2)(b) cit. in disc. Alleged assignee of decedent's business interest brought suit against personal representatives of decedent's estate to have title to the interest quieted in herself. The court entered judgment for defendants, who claimed title via a residuary devise in decedent's will. Affirming, this court held that restrictions in decedent's contract with corporation on assignment of decedent's business interest were valid and enforceable, and that because they were not met in the alleged transfer of decedent's business interest to plaintiff, the assignment to plaintiff was not valid. Hedges v. Woodhouse, 301 Mont. 180, 8 P.3d 109, 111.

Neb.App.

Neb.App.2000. Cit. in sup. Assignee of architect's accounts receivable sued client for breach of contract. The trial court entered judgment for plaintiff. Affirming in part, this court held, inter alia, that contract provisions prohibiting the assignment of contractual rights did not, absent a manifestation of intent by the parties, prohibit the assignment of the right to recover damages for breach. Folgers Architects Ltd. v. Kerns, 9 Neb.App. 406, 612 N.W.2d 539, 548, affirmed in part, reversed in part 262 Neb. 630, 633 N.W.2d 114 (2001).

Nev.

Nev.2010. Subsecs. (a)-(c) cit. in sup. Real-estate broker's assignee sued seller, seeking to recover a commission that it claimed it was owed under an exclusive right-to-sell brokerage agreement for the sale of seller's office-suite business. The trial court ruled in favor of seller and against broker's assignee. Reversing and remanding, this court held, inter alia, that the commission was assignable, and that real-estate broker validly assigned it to assignee; as a result, assignee had real-party-in-interest status in this case. The court noted that broker's assignment of commission rights to assignee did not materially change the terms of the brokerage agreement as to seller. Easton Bus. Opp. v. Town Executive Suites, 230 P.3d 827, 830.

N.H.

N.H.2007. Subsec. (2)(c) quot. in sup. Finance company sued payee entitled to structured-settlement-agreement payments, alleging that she entered into a contract with company to exchange certain of the periodic payments for immediate cash, but breached the contract by redirecting the payments to herself. The trial court granted summary judgment in favor of defendant on the breach-of-contract claim. Affirming, this court held, inter alia, that an anti-assignment clause in defendant's settlement agreement contained a clear expression of her intent to eliminate her power to assign the periodic payments, rendering void her agreements with plaintiff; there was no evidence in the record that the company making the periodic payments waived enforcement of the settlement agreement's anti-assignment clause, or even that it had knowledge that such payments had been assigned. Singer Asset Finance Co., LLC v. Wyner, 156 N.H. 468, 937 A.2d 303, 310.

N.J.

N.J.2001. Cit. in sup., subsec. (2) adopted and quot. in cases cit. in disc. Tort victim sued liability insurer for a declaratory judgment that a nonassignment clause in her structured settlement agreement was unenforceable. The trial court granted summary judgment for plaintiff, but the appellate division reversed and remanded. Reversing and remanding, this court held that, because the language in the nonassignment provision did not specifically restrict plaintiff's power of assignment, and because the assignment would not materially increase the burden or risk imposed on defendant, the nonassignment clause, in

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the context of this record, was unenforceable. Owen v. CNA Insurance/Continental Cas. Co., 167 N.J. 450, 460, 461, 467, 468, 771 A.2d 1208, 1213, 1214, 1218.

N.J.Super.

N.J.Super.2000. Cit. in diss. op. (citing § 154, T.D. No. 3, 1967, which is § 322 of the Official Draft), subsec. (2) quot. in disc. Tort victim who had entered into a structured settlement agreement with tortfeasors' insurer sued insurer for a declaratory judgment that the antiassignment clause in the settlement agreement was void and unenforceable. The trial court granted summary judgment for plaintiff. Reversing and remanding, this court held, inter alia, that the trial court's entry of judgment was improper in the absence of further development of both the materiality of the antiassignment provision and the legitimacy or reasonableness of the risks perceived to flow to defendant if the assignment were enforceable. The dissent argued that the conditional prohibition of assignment in this case was unenforceable both as a matter of stated law and as contrary to public policy. Owen v. CNA Ins./Continental Cas., 330 N.J.Super. 608, 620, 626, 750 A.2d 211, 218, 222, reversed 167 N.J. 450, 771 A.2d 1208 (2001). See above case.

N.M.

N.M.1985. Cit. in sup. A partnership sold an apartment complex to a family pursuant to a contract with a clause prohibiting assignment without consent. In case of nonpayment, the contract gave the partnership the option to obtain the return of the property or accelerate the entire purchase price. The family later transferred its interest to a limited partnership, which in turn later transferred its interest to a couple. None of these transfers was with the consent or approval of the partnership that originally sold the property. All payments under the original contract were made on time. The partnership sued the original and later purchasers, claiming a default because of the violation of the nonassignment clause. The trial court granted the defendants summary judgment on the theory that the transfers were not assignments. Affirming, this court held that the nonassignment clause was not ambiguous and prohibited only the delegation of the duties of the assignor. If there is no delegation of duties, said the court, there is no violation of a prohibition against assignment. Since neither of the later contracts of sale attempted to relieve the original purchasers of their obligations, the nonassignment clause was not violated. Paperchase Partnership v. Bruckner, 102 N.M. 221, 693 P.2d 587, 589.

N.M.App.

N.M.App.2006. Subsec. (2) quot. in sup. Deceased tort victim's children sought a declaratory judgment to establish their proper contingent-beneficiary status to victim's structured-settlement annuity, and lender's assignee intervened, claiming that annuity payments had been assigned by victim as collateral for a loan. The trial court granted summary judgment to assignee. Reversing and remanding, this court held, inter alia, that, although anti-assignment clauses were generally disfavored, here, the clause was enforceable and the assignment was rendered void because the clause's language established the clear intent of the parties that payments were not to be assigned or used as collateral. Espinosa v. United of Omaha Life Ins. Co., 139 N.M. 691, 137 P.3d 631, 639, certiorari denied 140 N.M. 225, 141 P.3d 1279 (2006).

N.Y.Sup.Ct.

N.Y.Sup.Ct.1983. Subsec. (2)(b) cit. in disc. The owner of a cooperative brought an action to bar a tenant's attempt to sell his apartment share to an outsider third party at an enormous profit. The “offering plan” which gave tenants the rights to purchase their respective apartments at a reduced “insider's price” also included an antiassignment clause which required written consent of the apartment corporation. In construing the clause, the court stated that the clause had to specifically eliminate the power as well as the right to assign the contract, otherwise the original obligor was given only the right to damages for the breach, and the assignment was still effective. Ultimately, the court denied the plaintiff's motion for a preliminary injunction, but granted leave to amend. University Mews Associates v. Jeanmarie, 122 Misc.2d 434, 471 N.Y.S.2d 457, 461.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Okl.

Okl.2001. Quot. and cit. in ftn. Creditor in bankruptcy proceeding sought relief from automatic stay, requesting permission to seize contracted-for annuity payments. The bankruptcy court certified questions. This court held, inter alia, that where antiassignment provision in settlement agreement prohibiting alienation of future payments made under annuity policy was clear and unambiguous, restriction on alienability was valid, but assignor of contract could not invoke the provision against its assignee. In re Kaufman, 37 P.3d 845, 850.

Pa.Super.

Pa.Super.1995. Cit. in ftn. A health-care provider sued an insurance company for refusing to pay for patients' chiropractic treatments pursuant to the terms of an ERISA group health insurance policy. Trial court dismissed provider's complaint. This court reversed and remanded, holding, inter alia, that the provider had the capacity to sue under ERISA because it had obtained assignments from the legitimate insurance plan beneficiaries. While health-care providers did not have independent standing to sue under ERISA because they were nonenumerated parties, nothing in ERISA prevented a health-care provider from bringing suit to enforce a valid assignment of health insurance benefits. Chiropractic Nutritional v. Empire Blue Cross and Blue Shield, 447 Pa.Super. 436, 669 A.2d 975, 980.

Tenn.App.

Tenn.App.1987. Cit. in sup. The owner of an apartment complex contracted for architectural services in connection with the renovation of 72 apartment units. The contract prohibited the owner from assigning, subletting, or transferring any interest in the agreement without the consent of the architect. After the contract was executed, the owner sold the apartment units to a purchaser who later became dissatisfied with the condition of the units. The purchaser sued the architect for breach of contract. The trial court awarded the architect summary judgment, holding that, since the terms of the contract between the former owner and the architect should be given effect, the assignment of the contract from the former owner to the purchaser was invalid. Reversing and remanding, this court held that a contractual provision prohibiting assignment of a contract by either party without the other party's written consent did not prohibit the assignment of a cause of action for breach of the contract. The court concluded that, since the purchaser's claim against the architect involved a cause of action for breach of the contract, the claim was both assignable and enforceable. Ford v. Robertson, 739 S.W.2d 3, 5.

Tex.App.

Tex.App.2003. Subsec. (2) cit. and quot. in disc. Assignee of account sued account debtor after debtor paid the account to assignor. Trial court granted debtor summary judgment and denied assignee's motion for partial summary judgment. Reversing and remanding, this court held, inter alia, that anti-assignment clause in services agreement was enforceable unless it infringed on an applicable statute, and sales chapter of Uniform Commercial Code (UCC) did not apply to render anti-assignment clause unenforceable. However, fact issues existed as to whether clause was unenforceable under Chapter 9 of UCC, and whether debtor waived clause. Texas Development Co. v. Exxon Mobil Corp., 119 S.W.3d 875, 881.

Tex.App.1985. Subsec. (2) quot. in sup. The owner of a car rental franchise sued the corporation for negligence and for violations of the Deceptive Trade Practices Act for failure to provide Yellow Pages advertising. The trial court ruled in favor of owner, and this court affirmed in part. It held that the corporation was obligated by contract to provide Yellow Page advertising to the owner even though the owner had recently bought the franchise. The court reversed on the Deceptive Trade Practices Act claim, ruling out the award of additional damages under the Act, since no actual damages had been proved, or the award of attorney's fees. Reuben H. Donnelley Corp. v. McKinnon, 688 S.W.2d 612, 615.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Utah

Utah, 2001. Cit. in disc. Subcontractor sued architectural consulting firm and others, seeking delay damages and other economic losses incurred on a construction project. Trial court granted defendants summary judgment, holding that an antiassignment clause in contract between consulting firm and county prohibited assignment by county to general contractor, and subsequently to subcontractor, of a breach-of-contract claim against consulting firm. This court reversed in part and remanded contract claim for a determination of whether parties intended antiassignment clause to prohibit only assignment of contract's performance, or whether it also prohibited assignment of a cause of action seeking money damages for breach of contract after contract had been fully performed. SME Industries, Inc. v. Thompson, Ventulett, Stainback and Associates, Inc., 28 P.3d 669, 674.

Wash.App.

Wash.App.2006. Cit., quot., and cit. generally but not fol., subsec. (1) cit. generally in disc., com. (b) quot. but not fol. Structured-settlement beneficiaries agreed, despite contractual prohibitions against assignment of payment rights, to give settlement company some rights to future payments in exchange for a present-day lump-sum payment, and company sought court approval for assignments after annuity holder objected. The trial court approved the assignments. Reversing, this court held, inter alia, that, because company failed to show that North Carolina law, under which the contracts were to be construed, had adopted the Restatement approach that anti-assignment clauses in structured-settlement agreements were to be disregarded where they served no legitimate interest of the obligor, and, here, the contracts at issue prohibited assignment in clear and unambiguous terms, the clauses were enforceable. Rapid Settlements Ltd's Application for Approval of Structured Settlement Payment Rights v. Symetra Assigned Benefits Service Co., 133 Wash.App. 350, 136 P.3d 765, 775, 776.

Wis.App.

Wis.App.2002. Cit. in disc., subsec. (2)(b) cit. and quot. in disc. Assignee of tort victim's future payments obtained in a structured settlement of a products-liability suit brought a declaratory-judgment action, seeking a ruling that the antiassignment clause in the annuity agreement between victim and insurer was unenforceable. Affirming the trial court's denial of plaintiff's motion for summary judgment, this court held, inter alia, that the antiassignment language was intended to retain a favorable tax provision and, as such, the clear and unambiguous language prohibiting any assignments was enforceable. J.G. Wentworth S.S.C. Ltd. Partnership v. Callahan, 256 Wis.2d 807, 813, 649 N.W.2d 694, 698.

Restatement of the Law - Contracts © 1932-2019 American Law Institute.
Reproduced with permission. Other editorial enhancements © Thomson Reuters.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-29

KeyCite Yellow Flag - Negative Treatment
Declined to Extend by Thompson v. Anderson, S.D.Miss., March 27, 2017

650 F.Supp.2d 1213
United States District Court,
S.D. Florida.

SIERRA EQUITY GROUP, INC., as assignee of Michael E. Splain, James W. Lees, and the Andrew Revocable Trust, Plaintiff,
v.
WHITE OAK EQUITY PARTNERS, LLC, Ross Statham, individually, Philip Orlando, individually, and Anthony Orlando, individually, Defendants.

No. 08–80017–CIV.
|
March 30, 2009.

Synopsis
Background: Selling agent, as assignee of investors, brought action against securities issuer and its officers, alleging breach of contract, unjust enrichment, fraudulent inducement, and securities fraud. Defendants moved to dismiss for failure to state a claim and for lack of personal jurisdiction.

Holdings: The District Court, Kenneth A. Marra, J., held that:

federal court had jurisdiction over defendants;

selling agent sufficiently stated breach of contract claim;

selling agent sufficiently stated claim of unjust enrichment;

declaratory relief was inappropriate; and

selling agent sufficiently stated claims of fraud and securities fraud.

Motions granted in part and denied in part.

Procedural Posture(s): Motion to Dismiss.

Attorneys and Law Firms

***1217** Geoffrey Michael Cahen, Stephen A. Mendelsohn, Greenberg Traurig et al., Boca Raton, FL, Steven Alan Lessne, Gray Robinson, Ft. Lauderdale, FL, for Plaintiff.

Ronald David Poltorack, Boca Raton, FL, Kelly Anne Luther, Matthew Koontz Cordis, Clarke Silverglate & Capmbell, P.A., Miami, FL, Mark Ressler, Michael P. Bowen, Kasowitz Benson Torres & Friedman, New York, NY, for Defendants.

OPINION AND ORDER ON MOTIONS TO DISMISS

KENNETH A. MARRA, District Judge.

THIS CAUSE comes before the Court on Defendants White Oak and Statham's Motion to Dismiss (DE 35) and Defendants Philip Orlando and Anthony Orlando's Motion to Dismiss the First Amended Complaint (DE 36). The motions are now fully briefed and ripe for review. The Court held a hearing on the motions on March 18, 2009. Following the hearing, Plaintiff and the Orlando Defendants filed supplemental memoranda as requested by the Court. (DE 57, 58). The Court has carefully ***1218** considered the motions and is otherwise fully advised in the premises.

Background
On December 5, 2007, Plaintiff Sierra Equity Group, Inc. ("Plaintiff") filed a Complaint against Defendants White Oak Equity Partners, LLC ("White Oak"), Ross Statham, Philip Orlando, and Anthony Orlando. The case was subsequently removed to this Court on January 9, 2008.

This action arises out of a private offering of securities. (Am.Compl.¶ 1). Plaintiff alleges that investors provided funds in connection with the offering, which was never completed in accordance with the representations of the Defendants. (Am.Compl.¶ 1). The investors never received the promised securities and, despite their demands, the investors' funds were never returned. (Am.Compl.¶ 1). Plaintiff asserts claims of Breach of Contract against White Oak (Count I); Unjust Enrichment against White Oak and the Orlandos (Count II); Fraudulent Inducement against all Defendants (Count III); Declaratory Judgment against White Oak (Count IV); Violation of Section 517.301, Florida Statutes, against all Defendants (Count V); and Violation of 15 U.S.C. § 78j(b) against all Defendants (Count VI).

The Amended Complaint alleges that in early 2006, the Orlandos contacted Statham in Georgia to discuss the White Oak securities transaction. (Am.Compl. ¶ 12). Statham and the Orlandos, "on behalf of White Oak, contacted Sierra in Florida, via telephone, and advised Sierra that White Oak intended to offer securities to certain qualified investors." (Am.Compl.¶ 15). During the telephone call, "the Defendants failed to advise Sierra that the Orlandos would receive a commission or otherwise profit from the Offering." (Am.Compl.¶ 16).

A Selling Agreement, dated August 23, 2006, was executed by White Oak and Plaintiff. (Am.Compl.¶ 19–20, Exh. A). In the Selling Agreement, White Oak contracted to use Plaintiff as a selling agent and to sell, through Plaintiff, an "Offering" of up to $232,000 in convertible debt securities in White Oak to investors. (Am.Compl.¶ 19). Under the Selling Agreement, White Oak represented that it would use the proceeds from the Offering to pay Plaintiff a cash commission and to acquire Gem Systems Common Stock and Volptech Common Stock. (Am.Compl.¶ 20). The Selling Agreement did not state that the Orlandos would receive compensation in connection with the Offering. (Am.Compl.¶ 21, 34). Plaintiff then solicited three investors (located in Arizona, California, and Massachusetts), each of whom contributed to the investment. The contribution from all three investors totaled $232,000. (Am.Compl.¶¶ 23–29). The investors also each signed a Subscription Agreement stating that White Oak would use the proceeds to buy common shares of Gem Systems and Volptech. (Am.Compl.Ex. B). White Oak received the investors' funds, but it failed to execute the Subscription Agreements, failed to buy Volptech shares and, upon demand, failed to return the money to the investors. (Am.Compl.¶¶ 35–46). White Oak provided at least $60,000 of the funds tendered by the investors to the Orlandos as compensation contingent upon the Offering being successful. (Am.Compl.¶ 39). The investors assigned their right, title and interest in the Offering, the Subscription Agreement and in White Oak to Plaintiff. (Am.Compl. ¶ 48, Exh. I).

In the Amended Complaint, Plaintiff asserts that the Court may exercise personal jurisdiction over all Defendants pursuant to Fla. Stat. § 48.193(1)(b) for committing a tortious act within the State of Florida and because Defendants engage in substantial and not isolated activity within Florida. (Am.Compl.¶¶ 3–6.) Further, Plaintiff asserts that Defendant White Oak ***1219** consented by contract to personal jurisdiction in Florida. On April 15, 2008, the parties were granted sixty (60) days to complete jurisdictional discovery (DE 21). Subsequently, all Defendants filed motions to dismiss the Amended Complaint for failure to state a claim upon which relief can be granted under Fed.R.Civ.P. 12(b)(6) and for lack of personal jurisdiction under Fed.R.Civ.P. 12(b)(2). (DE 35, 36).

Jurisdictional Facts

White Oak and Statham

Defendant White Oak Equity Partners, LLC ("White Oak") is a Georgia limited liability company. (Declaration of Ross Statham, DE 7–2 at ¶ 6). Defendant Ross Statham ("Statham") is a resident of Georgia and is White Oak's Managing Partner. (Declaration of Ross Statham, DE 7–2 at ¶¶ 2, 5). According to Statham's Declaration, he is a resident and citizen of Georgia; he votes in Georgia; he does not reside in Florida; he does not work in Florida; he does not own real property in Florida; he does not file or pay taxes in Florida; he does not maintain an office, telephone number or mailing address in Florida; he does not engage in business in Florida; he has not attended any business meetings in the last five years in Florida; he does not regularly travel to Florida; and he never met any representative of Plaintiff in Florida. (Declaration of Ross Statham, DE 7–2 at ¶¶ 2, 15–19, 21, 23, 25, 26–27).

Also, according to Statham's Declaration, White Oak does not own real property in Florida; it does not file or pay taxes in Florida; it does not maintain an office, telephone number or mailing address in Florida; no representative of White Oak has attended any business meetings in the last five years in Florida; and it does not engage in business in Florida. (Declaration of Ross Statham, DE 7–2 at ¶¶ 6, 20, 22, 24).

In early 2006, the Orlandos contacted Statham in Georgia to discuss the White Oak securities transaction. (Am.Compl.¶ 12). Statham and the Orlandos, "all purportedly on behalf of White Oak, contacted Sierra in Florida, via telephone, and advised Sierra that White Oak intended to offer securities to certain qualified investors." (Am.Compl.¶ 15). During the telephone call, "the Defendants failed to advise Sierra that the Orlandos would receive a commission or otherwise profit from the Offering." (Am.Compl.¶ 16).

Thereafter, on or about August 23, 2006, Statham executed the Selling Agreement as Managing Partner of White Oak in Georgia. (Declaration of Ross Statham, DE 7–2 at ¶ 31). According to the terms of the "Selling Agreement," to which White Oak and Sierra are parties, "[e]ach party hereby consents to any and all actions or controversies arising

from this agreement shall [ ] have venue in the exclusive jurisdiction of the state and federal courts located in Palm Beach County, Florida." (Am.Compl.Exh. A, § 9.10). There are also provisions in the unsigned Subscription Agreement (Am.Compl.Exh. B, § 9(d)) and unsigned convertible note (Am.Compl.Exh. C, § 4.6) which provide for jurisdiction in Palm Beach County, Florida.

The three investors wired the funds in question to White Oak in Georgia from the states of their respective residency and citizenship, California, Arizona, and Massachusetts. (Declaration of Ross Statham, DE 7–2 at ¶¶ 8, 9, 10, 11).

White Oak and Statham communicated by telephone with Sierra in Florida in connection with the purported Offering. (White Oak's Answers To First Set Of Interrogatories, DE–40, at ¶ 5; Statham Dep., DE 44 at 27:13–22, 33:23–34:4). According to the Affidavit of Alan Goddard, Statham and Goddard participated in approximately ***1220** ten phone calls related to the Offering (DE 46 at ¶ 7). Statham and Goddard also engaged in a great amount of email and other correspondence with Sierra in connection with the purported Offering. (DE 47 Ex. A; Statham Dep., DE 44 at 33:23–34:4; Goddard Aff., DE–46 at ¶ 8). Additionally, Statham personally created Sierra's website and made various changes to the website after it was completed. (Statham Dep., DE 44 at 28:5–30:1).

Philip and Anthony Orlando

With respect to the Orlandos, the Amended Complaint alleges, in part:

> 12. In early 2006, the Orlandos contacted Statham in Georgia to discuss a securities transaction in which a private company would be reverse merged into the shell of a public company. The Orlandos asked Statham whether he had a "clean" entity which they could use to accomplish this transaction and ultimately sell this investment to qualified investors. Statham offered the Orlandos White Oak as the entity to accomplish this transaction and the Orlandos consented.
>
> 13. Specifically, the transaction involved the reverse merger of Volptech International, Inc. ("Volptech") into a public shell company, Gem Systems, Inc. ("Gem"). The Orlandos were integral in structuring and negotiating the transaction.
>
> 14. White Oak and Statham agreed to pay the Orlandos a substantial commission contingent upon the completion of the securities transaction.
>
> 15. Soon thereafter, Statham, Philip Orlando and Anthony Orlando, all purportedly on behalf of White Oak, contacted Sierra in Florida, via telephone, and advised Sierra that White Oak intended to offer securities to certain qualified investors. During this telephone conversation, Philip Orlando and Anthony Orlando both stated to Alan Goddard of Sierra that White Oak intended to acquire shares of restricted common stock of Gem and Volptech with the proceeds of the Offering....
>
> 16. During the telephone call, the Defendants failed to advise Sierra that the Orlandos would receive a commission or otherwise profit from the Offering. ...
>
> 18. The Defendants intended that Sierra would pass on the representations and omissions made during this telephone conversation to potential investors and the Defendants intended for those potential investors to rely upon these representations and omissions.

Defendants Philip and Anthony Orlando ("the Orlandos") "are life-long residents of New York," and both currently reside and work in New York. (Dec. of P. Orlando, DE 5–2 at ¶ 2; Dec. of A. Orlando, DE 5–3 at ¶ 2). They have never had an office, work mailing address, or work telephone number in Florida; they do not own any real property or other assets in Florida; they do not file or pay taxes in Florida. (Dec. of P. Orlando, DE 5–2 at ¶ 5, 6, 7, 8; Dec. of A. Orlando, DE 5–3 at ¶ 5, 6, 7, 8).

The Orlandos conducted activities in connection with the Offering on behalf of White Oak. (Goddard Aff., DE–46, at ¶ 5). They worked with Florida-based Sierra to identify investors for the Offering. (Statham Dep., DE–44, 39:21–40:4). The Orlandos took four trips to Florida to discuss the Offering with Sierra. (*See* DE 41, 42 at ¶ 2; Goddard Aff. at ¶ 9; *see* DE 48 Ex. "C" Orlandos' travel records). During at least one of these trips, the Orlandos met with executives from Volptech in Florida. (Dep. of P. Orlando, DE 45 at 92:21–94:4; Dep. of A. Orlando, DE 43 at 60:18–64:14).

The Orlandos made hundreds of phone calls to Sierra in Florida. (*See* DE 48 Ex. "A" telephone records; Goddard Aff., DE ***1221** 46, at ¶ 6). However, the parties dispute whether the majority of the extensive phone contact had to do with

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

the White Oak Offering or other unrelated transactions. Sierra claims that most of the calls involved discussion of White Oak:

> During the time period of 2006 through the present, I have participated in hundreds of telephone calls with Anthony and Philip Orlando. In approximately 90% of these calls, we discussed matters relevant to the Offering of White Oak Equity Partners, LLC securities. During approximately 80% of these calls, we discussed matters relevant to other proposed business deals in Florida.

(Goddard Aff., DE 46, at ¶ 6). The Orlandos, on the other hand, claim that most of the telephone contact had to do with transactions other than White Oak:

> Q. Can you tell approximately how many of those calls you made to Mr. Goddard or at least Morningside made to Goddard referred to White Oak?
>
> A. I have no way of knowing. If you were to ask me on a percentage basis the total calls to Alan Goddard?
>
> Q. Yes, sir.
>
> A. Very small

(Dep. of P. Orlando, June 11, 2008 (Exhibit A, DE 51–2) at 50). The Orlandos also communicated extensively with Sierra via email concerning the Offering. (*See* DE 48 Ex. "B" email records; Goddard Aff., DE 46, at ¶ 8).

Additionally, from 2006 to the present, the Orlandos identified approximately 18 other transactions in which they have been involved with Florida-based persons. (*See* DE 41, 42 at ¶ 3; Schedule "A" to DE 42; Exhibit "D" to DE 48). During their four trips to Florida, the Orlandos met with many of the individuals involved in their business deals. (*See* DE 48 Ex. "B" email records; Goddard Aff. DE 46, at ¶ 9). The Orlandos' telephone records indicate many telephone calls to businesses in Florida that were associated with these 18 business transactions. (*See* DE 48 Ex. "A" telephone records). The Orlandos were previously registered under the blue sky laws of Florida. (*See* DE 41, 42 at ¶ 12).

The Orlandos did not receive compensation from any entity or individual located in Florida. (*See* P. Orlando Dep., Exh. "A," DE 51–2, at 25:22–26:5; A. Orlando Dep., Exh. "B", DE 51–3, at 55–71). The Orlandos emphasize that they did not seek business in Florida, but rather participated in these Florida discussions at the request of Goddard and Sierra Equity and on their behalf. (*See* P. Orlando Dep., Exh. "A," DE 51–2, at 55–62; A. Orlando Dep., Exh. "B", DE 51–3, at 55–71).

Analysis

Personal Jurisdiction

When considering a motion to dismiss for lack of personal jurisdiction, a court must accept the facts alleged in plaintiff's complaint as true, to the extent that they are not contradicted by defendant's affidavits. *See Morris v. SSE, Inc.,* 843 F.2d 489, 492 (11th Cir.1988); *Corneal v. CF Hosting, Inc.,* 187 F.Supp.2d 1372, 1373 (S.D.Fla.2001). The parties have submitted evidentiary materials in support of their respective positions. While the consideration of such materials ordinarily would convert a motion to dismiss into one for summary judgment, *see* Fed.R.Civ.P. 12(b), in the context of personal jurisdiction the motion remains one to dismiss even if evidence outside the pleadings is considered. *Bracewell v. Nicholson Air Services, Inc.,* 748 F.2d 1499, 1501 n. 1 (11th Cir.1984). An evidentiary hearing on a motion to dismiss for lack of personal jurisdiction is discretionary but not mandatory. *See, e.g., Madara v. Hall,* 916 F.2d 1510, 1514 (11th Cir.1990); *Bracewell,* 748 F.2d at 1504. Because the parties did not request an evidentiary hearing, the Court exercises its discretion not to conduct one.

***1222** The Court must accept as true all allegations of the complaint that are not controverted by evidence submitted by the defendant. *Id.* Once the plaintiff pleads sufficient material facts to form a basis for personal jurisdiction, the burden shifts to the defendant to challenge the plaintiff's allegations by affidavits or other pleadings. *See Future Tech. Today, Inc. v. OSF Healthcare Sys.,* 218 F.3d 1247, 1249 (11th Cir.2000). When the nonresident defendant meets this burden, the plaintiff must substantiate the jurisdictional allegations in its complaint by affidavits or other competent proof, and may not merely rely upon the factual allegations set forth in the complaint. *See Future Tech. Today, Inc.,* 218 F.3d at 1249; *Posner v. Essex Insurance Co.,* 178 F.3d 1209, 1215 (11th Cir.1999). Where the plaintiff's evidence and defendant's evidence conflict, all reasonable inferences must be construed in favor of the plaintiff. *Stubbs v. Wyndham Nassau Resort and*

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Crystal Palace Casino, 447 F.3d 1357, 1360 (11th Cir.2006); *Molina v. Merritt & Furman,* 207 F.3d 1351, 1356 (2000); *Morris v. SSE, Inc.,* 843 F.2d 489, 492 (11th Cir.1988).

A determination of whether personal jurisdiction over a nonresident defendant exists requires a two-part inquiry. First, the Court must consider the jurisdictional question under the Florida state long-arm statute. *Robinson v. Giarmarco & Bill, P.C.,* 74 F.3d 253 (11th Cir.1996); *see also* Fla. Stat. § 48.193(1). If there is a basis for the assertion of personal jurisdiction under the state statute, the court will next determine "whether the exercise of personal jurisdiction over the defendant would violate the Due Process Clause of the Fourteenth Amendment to the United States Constitution, which requires that the defendant have minimum contacts with the forum state and that the exercise of jurisdiction over the defendant does not offend traditional notions of fair play and substantial justice." *Mut. Serv. Ins. Co. v. Frit Indus.,* 358 F.3d 1312, 1319 (11th Cir.2004) (internal quotations omitted). Only if both prongs of the analysis are satisfied may a federal or state court exercise personal jurisdiction over a nonresident defendant. *See Robinson,* 74 F.3d at 256.

1. Florida's Long–Arm Statute

Florida's long-arm statute authorizes courts to exercise specific jurisdiction under § 48.193(1), Florida Statutes. Florida's long-arm statute states, in relevant part:

> (1) Any person, whether or not a citizen or resident of this state, who personally or through an agent does any of the acts enumerated in this subsection thereby submits himself or herself and, if he or she is a natural person, his or her personal representative to the jurisdiction of the courts of this state for any cause of action arising from the doing of any of the following acts: ...
>
> (b) Committing a tortious act within this state.

§ 48.193(1)(b), Fla. Stat. "Because the reach of the Florida long-arm statute is a question of Florida state law, federal courts are required to construe it as would the Florida Supreme Court." *Oriental Imports & Exports, Inc. v. Maduro & Curiel's Bank, N.V.,* 701 F.2d 889, 890–91 (11th Cir.1983) (*citing Moore v. Lindsey,* 662 F.2d 354, 357–58 (5th Cir.1981)). Furthermore, the Florida long-arm statute is to be strictly construed. *Id.* at 891.

Sierra argues that the Court has specific jurisdiction over Defendants under Florida's long-arm statute, which provides for jurisdiction against defendants who "commit[ ] a tortious act within this state." § 48.193(1)(b), Fla. Stat. The tortfeasor's physical presence in Florida is not required to obtain personal jurisdiction. *Horizon Aggressive Growth, L.P. v. Rothstein–Kass,* ***1223** *P.A.,* 421 F.3d 1162, 1168 (11th Cir.2005). "[A]llegations about an out-of-state defendant's 'telephonic, electronic, or written communications into Florida' are sufficient to trigger jurisdiction under the Long–Arm statute provided, however, that the cause of action arises from those communications." *See American Color Graphics, Inc. v. Brooks Pharmacy, Inc.,* 2007 WL 3202748 (M.D.Fla.2007) ("It is well-settled that a tortious act can occur in Florida 'through the nonresident defendant's telephonic, electronic, or written communications into Florida.' ") (*quoting Wendt v. Horowitz,* 822 So.2d 1252, 1260 (Fla.2002)); *ABL–USA Enters., Inc. v. Hawk Aviation, Ltd.,* 15 F.Supp.2d 1297, 1300 (S.D.Fla.1998) (tortious interference accomplished by telephone calls into Florida); *Acquadro v. Bergeron,* 851 So.2d 665, 677 (Fla.2003) (allegations sufficient to support jurisdiction where nonresident allegedly committed defamation in a single telephone call into Florida).

Moreover, fraudulent misrepresentations made from outside Florida and directed into Florida (by phone, fax, writing) constitute tortious acts committed within Florida under Florida's long-arm statute. *Machtinger v. Inertial Airline Services, Inc.,* 937 So.2d 730, 735 (Fla. 3d DCA 2006). *Contrast Sun Bank, N.A. v. E.F. Hutton & Co.,* 926 F.2d 1030 (11th Cir.1991) (no personal jurisdiction where the defendant made fraudulent misrepresentations over the telephone because the defendant did not purposefully direct its activities at Florida residents and the calls were merely fortuitous contacts). Florida district courts have found long-arm jurisdiction over nonresident defendants accused of making fraudulent misrepresentations and omissions via telephone. *See Hollingsworth v. Iwerks Entertainment, Inc.,* 947 F.Supp. 473, 478 (M.D.Fla.1996).

Here, the Amended Complaint alleges that Statham and the Orlandos, on behalf of White Oak, made a telephone call into Florida during which they made fraudulent representations, but more importantly, omitted material facts regarding their intended use of the investor funds. Am. Compl. at ¶¶ 15, 65–70. Defendants intended that Sierra would pass on the representations, absent the material information that was omitted, in order to induce the investors into purchasing the securities. Am. Compl. at ¶¶ 18, 65–68. Relying on the representations and fraudulent omissions of Defendants, Sierra advised its clients to invest in the Offering. Am. Compl.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

at ¶¶ 23–24, 69–70. Defendants intended for the potential investors to rely upon those passed-on representations and omissions. Am. Compl. at ¶¶ 18, 67–68. Accordingly, the Amended Complaint has sufficiently alleged a tortious act committed by a telephone call into Florida as a basis for Florida long-arm jurisdiction under § 48.193(1)(b), Fla. Stat.

To determine whether the requirements of the Florida long-arm statute have been met, the Court must decide if the evidence demonstrates that Defendants committed the alleged tort of fraudulent misrepresentation or omission during the telephone call at issue. That determination clearly requires a decision on the merits of the case. Issues involving details about what was said during this telephone call, whether Sierra and its investors relied on the representations and whether the omissions were material and, if know, would have affected the investors' decisions are "the very contested issues to be resolved in trying the cause of action." *Krilich v. Wolcott,* 717 So.2d 582, 584 (Fla. 4th DCA 1998). In situations "[w]here the jurisdictional issues are intertwined with the substantive merits, 'the jurisdictional issues should be referred to the merits, for it is impossible to decide one without the other.' " ***1224** *Eaton v. Dorchester Dev., Inc.,* 692 F.2d 727, 733 (11th Cir.1982) *quoting Chatham Condo. Assocs. v. Century Village, Inc.,* 597 F.2d 1002, 1011 (5th Cir.1979). [1] Reaching the merits requires developing a full factual record relating to jurisdictional issues. *See id.* at 729 ("federal courts have the power to order, at their discretion, the discovery of facts necessary to ascertain their competency to entertain the merits.") Accordingly, the Court will exercise its discretion to reserve ruling on the jurisdictional issues until a decision on the merits can be rendered. [2] *See Nissim Corp. v. ClearPlay, Inc.,* 351 F.Supp.2d 1343 (S.D.Fla.2004) (since personal jurisdiction over corporate officer will turn on whether the plaintiff could prove allegations that corporate officer actively induced patent infringement it is necessary to defer ruling on jurisdictional issue until trial or summary judgment). [3]

Additionally, White Oak is subject to personal jurisdiction in Florida by contract. "The requirement of personal jurisdiction represents an individual due process right, and the 'parties to a contract may agree in advance to submit to the jurisdiction of a given court.' " *Hickman v. Terrell,* 2008 WL 4417297, *3 (M.D.Ala.2008) (quoting *Ins. Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee,* 456 U.S. 694, 704, 102 S.Ct. 2099, 72 L.Ed.2d 492 (1982)). Here, the Selling Agreement contains a provision stating that each party to the contract (Sierra and White Oak) "consents to any and all actions or controversies arising from this agreement shall have venue in the exclusive jurisdiction of the state and federal courts located in Palm Beach County, Florida." (Am. Compl. ¶ 8, Exh. A to Complaint at § 9.10). The Subscription Agreements, upon which Sierra, as assignee of the investors, is suing, contain a similar provision stating "The parties and the individuals executing this Agreement and other agreements referred to herein or delivered in connection herewith on behalf of the Company agree to submit to the personal jurisdiction of [the civil or state courts of Florida or in the federal courts located in Palm Beach County, Florida]." (Exh. B to Complaint at § 9(d)). In some states, "[s]uch conferrals of exclusive jurisdiction have been specifically recognized as including *consents to personal jurisdiction." Rescuecom Corp. v. Chumley,* 522 F.Supp.2d 429, 443 (N.D.N.Y.2007) (string citing cases standing for this proposition) (emphasis in original). *See also Suntrust* ***1225** *Bank v. G.R. Auto Supply, Inc.,* 2007 WL 2226058, *1 (N.D.Ga.2007) ("The Court further finds that the parties consented to personal jurisdiction in this court by agreeing in the loan contract to have all disputes heard in Georgia.").

While it is true that a forum clause cannot operate as the "sole basis" to exercise personal jurisdiction in Florida over an objecting nonresident defendant, that is not the case at bar. Here, not only did White Oak agree to exclusive jurisdiction in Florida, but it also contracted to use Sierra, a Florida corporation, as its selling agent to sell the "Offering" of up to $232,000 in convertible debt securities in White Oak to investors [4] and it allegedly committed the tort of fraudulent inducement during the telephone call at issue. [5] (Am.Compl.¶ 2, 19, 64–70).

2. Due Process

An exercise of jurisdiction under a state's long-arm statute must also comport with due process. Due process authorizes the exercise of personal jurisdiction over a nonresident defendant when "(1) the nonresident defendant has purposefully established minimum contacts with the forum;" and "(2) the exercise of jurisdiction will not offend traditional notions of fair play and substantial justice." *S.E.C. v. Carrillo,* 115 F.3d 1540, 1542 (11th Cir.1997) (citation omitted); *see also Horizon Aggressive Growth, L.P. v. Rothstein–Kass, P.A.,* 421 F.3d 1162, 1166 (11th Cir.2005). Just a single act by a non-resident defendant directed to a forum state can be enough to confer specific personal jurisdiction if the act gave rise to the cause of action at issue.

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

See Burger King Corp. v. Rudzewicz, 471 U.S. 462, 476 n. 18, 105 S.Ct. 2174, 85 L.Ed.2d 528 (1985).

a. Minimum Contacts

In contrast to general jurisdiction, "[s]pecific jurisdiction arises out of a party's activities in the forum that are related to the cause of action alleged in the complaint." *McGow v. McCurry,* 412 F.3d 1207, 1214 n. 3 (11th Cir.2005) (citation omitted). The exercise of personal jurisdiction on a specific jurisdiction theory is proper where a defendant's contacts with the forum state satisfy all of the following criteria: (1) they are related or give rise to the plaintiff's cause of action, (2) they involve some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum, and (3) the defendant's contacts with the forum are such that the defendant should reasonably anticipate being haled into court there. *See, e.g., Sloss Industries Corp. v. Eurisol,* 488 F.3d 922 (11th Cir.2007); *McGow,* 412 F.3d at 1214. "[I]t is essential in each case that there be some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the ***1226** benefits and protections of its laws." *Hanson v. Denckla,* 357 U.S. 235, 253, 78 S.Ct. 1228, 2 L.Ed.2d 1283 (1958). The requirement is satisfied if the defendant purposefully directs activities at Florida and litigation arises out of those activities, or the defendant purposefully avails himself of the privilege of conducting activities within the forum state. *Achievers Unlimited, Inc. v. Nutri Herb, Inc.,* 710 So.2d 716, 719 (Fla. 4th DCA 1998).

The Defendants' contacts with Florida in this case meet the above criteria for minimum contacts. First, by directing their tortious conduct to Florida, Defendants could have reasonably anticipated being haled into court here. *See, e.g., OSI Industries, Inc. v. Carter,* 834 So.2d 362 (Fla. 5th DCA 2003). Additionally, White Oak contracted with a Florida corporation, Sierra, to be its selling agent for the Offering and to close on the transactions at Sierra's offices in Florida. [6] White Oak and Statham communicated by telephone with Sierra in Florida in connection with the purported Offering. (White Oak's Answers To First Set Of Interrogatories, DE–40, at ¶ 5; Statham Dep., DE 44 at 27:13–22, 33:23–34:4). According to the Affidavit of Alan Goddard, Statham and Goddard participated in approximately ten phone calls related to the Offering (DE 46 at ¶ 7). *See Achievers Unlimited, Inc. v. Nutri Herb, Inc.,* 710 So.2d 716 (Fla. 4th DCA 1998) (additional contacts with Florida established by communicating with plaintiff in Florida by telephone, telefax, and mail). Statham and Goddard also engaged in a great amount of email and other correspondence with Sierra in connection with the purported Offering. (DE 47 Ex. A; Statham Dep., DE 44 at 33:23–34:4; Goddard Aff., DE–46 at ¶ 8).

The Orlandos also had sufficient minimum contacts with Florida. The Orlandos worked with Sierra to identify investors for the Offering. (Statham Dep., DE–44, 39:21–40:4). They took four trips to Florida to discuss the Offering with Sierra. (*See* DE 41, 42 at ¶ 2; Goddard Aff. at ¶ 9; *see* DE 48 Ex. "C" Orlandos' travel records). During at least one of these trips, the Orlandos met with executives from Volptech in Florida. (Dep. of P. Orlando, DE 45 at 92:21–94:4; Dep. of A. Orlando, DE 43 at 60:18–64:14). The Orlandos made hundreds of phone calls to Sierra in Florida, most of which concerned matters relevant to the Offering. (*See* DE 48 Ex. "A" telephone records; Goddard Aff., DE 46, at ¶ 6). (Dep. of P. Orlando, June 11, 2008 (Exhibit A, DE 51–2) at 50). The Orlandos also communicated extensively with Sierra via email concerning the Offering. (*See* DE 48 Ex. "B" email records; Goddard Aff., DE 46, at ¶ 8).

b. Fair Play and Substantial Justice

"Once it has been determined that the nonresident defendant has purposefully established minimum contacts with the forum such that he should reasonably anticipate being haled into court there, these contacts are considered in light of other factors to decide whether the assertion of personal jurisdiction would comport with 'fair play and substantial justice.' " *Madara,* 916 F.2d at 1517 (*quoting Burger King Corp. v. Rudzewicz,* 471 U.S. 462, 476, 105 S.Ct. 2174, 85 L.Ed.2d 528 (1985)). These other factors include "the burden on the defendant in defending the lawsuit, the forum state's interest in adjudicating the dispute, the plaintiff's interest in obtaining convenient and effective relief, the interstate judicial system's interest in obtaining the most effective resolution of controversies and the shared interest of the states in furthering fundamental substantive social ***1227** policies." *Id.* (*quoting Burger King,* 471 U.S. at 476, 105 S.Ct. 2174).

Here, the Court finds that assertion of personal jurisdiction over Defendants "comport[s] with fair play and substantial justice." *Id.* at 476, 105 S.Ct. 2174 (*citing International Shoe,* 326 U.S. at 320, 66 S.Ct. 154) (internal quotation marks omitted). Adjudicating this dispute against all parties in Florida will provide Plaintiff with convenient and effective relief and will serve judicial efficiency on an interstate

level. Indeed, the individual defendants will undoubtedly be witnesses at trial and thus will not be unduly burdened by answering the claims against them in one forum. Lastly, Florida has a strong interest in adjudicating a dispute that involves a Florida corporation and a tort directed into Florida. For these reasons, the Court finds that the requirements of reasonableness and fairness of asserting jurisdiction over Defendants have been met.

Failure to State a Claim

Defendants also argue that the Amended Complaint must be dismissed for failure to state a claim. Rule 8(a) of the Federal Rules of Civil Procedure requires "a short and plain statement of the claims" that "will give the defendant fair notice of what the plaintiff's claim is and the ground upon which it rests." Fed.R.Civ.P. 8(a). The Supreme Court has held that "[w]hile a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the 'grounds' of his 'entitlement to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a right to relief above the speculative level." *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544, 127 S.Ct. 1955, 1964–65, 167 L.Ed.2d 929 (2007) (internal citations omitted). When considering a motion to dismiss, the Court must accept all of the plaintiff's allegations as true in determining whether a plaintiff has stated a claim for which relief could be granted. *Hishon v. King & Spalding,* 467 U.S. 69, 73, 104 S.Ct. 2229, 81 L.Ed.2d 59 (1984).

The Assignments

The Assignments at issue state, in pertinent part:

> *Transfer.* Effective immediately, ASSIGNOR hereby irrevocably contributes, assigns, transfers, sells and conveys to the ASSIGNEE all of the ASSIGNOR'S right, title and interest in the Subscription Agreement and in White Oak.

See Am. Compl. Exh. I. "An assignment is a transfer of all the interests and rights to the thing assigned. Following an assignment, the assignee 'stands in the shoes of the assignor' and the 'assignor retains no rights to enforce the contract' at all." *Leesburg Cmty. Cancer Ctr. v. Leesburg Reg'l Med. Ctr., Inc.,* 972 So.2d 203, 206 (Fla. 5th DCA 2007) (internal citations omitted). As such, Sierra, standing in the shoes of the Investors for purposes of the Subscription Agreements, may sue for breach of those contracts and for any cause of action in tort arising from those contracts. *See id.; Nationwide Mut. Fire Ins. Co. v. Pinnacle Medical, Inc.,* 753 So.2d 55, 57 (Fla.2000) ("The right of an assignee to sue for breach of contract to enforce assigned rights predates the Florida Constitution."); *Continental Ins. Co. v. Roberts,* 2007 WL 1175760, *3 (M.D.Fla.2007) (individual could not sustain claim for breach of contract unless contracting party "assigned her rights under that contract to him."); *ABL–USA Enterprises, Inc. v. Hawk Aviation, Ltd.,* 15 F.Supp.2d 1297 (S.D.Fla.1998) (corporation brought suit for breach of contract and for tort claim arising from contract pursuant to party's purchase of all rights and interests under that contract).

***1228** *Count I—Breach of Contract against White Oak*

Count I, breach of contract against White Oak, alleges that White Oak breached the Subscription Agreements. Am. Compl. ¶ 51–53. Under Florida law, a breach of contract action requires a valid contract, a material breach of that contract, and damages. *Hanover Specialties, Inc. v. Playmaker Services LLC,* 2009 WL 455443, *7 (S.D.Fla.2009). *See Beck v. Lazard Freres & Co., LLC,* 175 F.3d 913, 914 (11th Cir.1999); *Miller v. Nifakos,* 655 So.2d 192, 193 (Fla. 4th DCA 1995). Here, Plaintiff has sufficiently alleged each of these elements. The Amended Complaint alleges that (1) the Subscription Agreements are enforceable contracts; (2) pursuant to the Subscription Agreements, the Investors tendered $232,000.00 to White Oak; (3) White Oak accepted and deposited the money, thereby accepting the Subscription Agreement by conduct; and (4) White Oak breached the Subscription Agreements by failing to use the funds tendered by the Investors to acquire shares of Volptech Common Stock, by failing to deliver shares of GEM Common Stock to the Investors, and by using the proceeds of the Offering in an unauthorized manner (paying at least $60,000 to the Orlandos). Am. Compl. ¶ 51–53. The Amended Complaint also alleges that White Oak breached the implied covenant of good faith and fair dealing by failing to provide accurate and timely information regarding the status of the acquisition of Volptech Common Stock and by failing to disclose the payments to the Orlandos. Am. Compl. ¶ 54. Lastly, it alleges that White Oak's breaches of the Subscription Agreement caused the Investors to incur damages, including, but not limited to, the amount tendered by the Investors to White Oak pursuant to the Subscription Agreement. Am. Compl. ¶ 55–56.

White Oak argues that, since the Subscription Agreement was not signed by White Oak, no claim for its breach can be made against White Oak. (Mot. at 19). White Oak is incorrect

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

because it ignores the concept of assent by performance. A contract binds one who in some manner agreed to accept its terms. *Whetstone Candy Co., Inc. v. Kraft Foods, Inc.,* 351 F.3d 1067, 1073 (11th Cir.2003). "A contract may be binding on a party despite the absence of a party's signature. The object of a signature is to show mutuality or assent, but these facts may be shown in other ways, for example, by the acts or conduct of the parties." *Gateway Cable T.V., Inc. v. Vikoa Construction Corp.,* 253 So.2d 461, 463 (Fla. 1st DCA 1971). *See also Consolidated Resources Healthcare Fund I, Ltd. v. Fenelus,* 853 So.2d 500, 503 (Fla. 4th DCA 2003) (party assented to the contract by performing under the contract). The Amended Complaint alleges that in August, 2006, the Investors signed the Subscription Agreements and tendered their investment funds to White Oak. Am. Compl. ¶ 25. White Oak may be bound by the Subscription Agreement based on its conduct in accepting and depositing the $232,000.00 in funds tendered by the Investors to White Oak pursuant to the Subscription Agreement. If White Oak did not intend to be bound by the Subscription Agreement, it would have had no basis for retaining the Investor's funds. Whether White Oak accepted or rejected the Subscription Agreement is a question of fact appropriate for summary judgment or trial, and cannot be resolved on a motion to dismiss. Sierra has stated a claim in Count I for breach of contract against White Oak.

Count II—Unjust Enrichment against White Oak and the Orlandos

Count II, unjust enrichment, sets forth an alternative theory by which Sierra ***1229** seeks to recover the $232,000.00 tendered to White Oak by the Investors pursuant to the Subscription Agreements and the $60,000.00 allegedly provided to the Orlandos from the Investor's funds as undisclosed commission. The elements of a cause of action for unjust enrichment are: (1) plaintiff has conferred a benefit on the defendant, who has knowledge thereof; (2) defendant voluntarily accepts and retains the conferred benefit; and (3) the circumstances are such that it would be inequitable for the defendant to retain the benefit without paying the value thereof to the plaintiff. *Peoples Nat'l Bank of Commerce v. First Union Nat'l Bank of Fla.,* 667 So.2d 876, 879 (Fla. 3d DCA 1996) (*quoting Hillman Constr. Corp. v. Wainer,* 636 So.2d 576, 577 (Fla. 4th DCA 1994) (citations omitted)).

Defendants object to the unjust enrichment claim because Sierra pled a claim for breach of contract in Count I and a claim for unjust enrichment cannot be based on the same breach. *See, e.g., Ocean Communications, Inc. v. Bubeck,* 956 So.2d 1222, 1225 (Fla. 4th DCA 2007). First, this argument is inapposite to the Orlandos because there is no express contract between the Investors and the Orlandos.

Moreover, Defendants' argument ignores the basic tenet of alternative pleading under Rule 8(d)(2) of the Federal Rules of Civil Procedure. *Manicini Enterprises, Inc. v. American Exp. Co.,* 236 F.R.D. 695, 698–99 (S.D.Fla.2006). While Sierra can only recover once for the same actual damages, regardless of the number of alternative theories presented, it is not barred against pleading unjust enrichment simply because it has also plead breach of contract in Count I. "Until an express contract is proven, a motion to dismiss a claim for ... unjust enrichment on these grounds is premature." *Williams v. Bear Stearns & Co.,* 725 So.2d 397, 400 (Fla. 5th DCA 1998).

The Orlandos also argue that the unjust enrichment claim fails as to them for two reasons. First, they argue that there is no allegation that the Investors conferred a benefit on the Orlandos. They argue that, at most, the allegations show that White Oak conferred a benefit on the Orlandos. *See American Safety Ins. Service, Inc. v. Griggs,* 959 So.2d 322, 331 (Fla. 5th DCA 2007) ("The plaintiffs must show they directly conferred a benefit on the defendants."). As set forth above, the uniformly stated elements of a cause of action for unjust enrichment under Florida law are: (1) plaintiff has conferred a benefit on the defendant, who has knowledge thereof; (2) defendant voluntarily accepts and retains the conferred benefit; and (3) the circumstances are such that it would be inequitable for the defendant to retain the benefit without paying the value thereof to the plaintiff. *Peoples Nat'l Bank.,* 667 So.2d at 879. Plaintiff has alleged each of these elements against the Orlandos in the Amended Complaint. *See* Am. Comp. ¶¶ 57–63. Whether the Orlandos did or did not receive a direct benefit from Plaintiff is a question of fact that cannot be resolved at the motion to dismiss stage in this case. *See Romano v. Motorola, Inc.,* 2007 WL 4199781 (S.D.Fla.2007) (denying motion to dismiss unjust enrichment claim) (Defendant is correct in stating that "Florida law does not support a cause of action for unjust enrichment unless the plaintiff can allege that he conferred a direct benefit on the defendant." However, Defendant erroneously equates direct contact with direct benefit in arguing that "[b]ecause plaintiff here did not purchase either his phone or his batteries from Motorola, plaintiff conferred no direct benefit on Motorola.") (internal citations omitted). Therefore, the Orlandos' motion to dismiss the unjust enrichment claim is denied without prejudice to raise this issue later ***1230** in the proceedings at summary judgment or trial.

Second, the Orlandos argue that there is no allegation that they were paid the $60,000 *unfairly,* since it is alleged that "White Oak provided at least $60,000 of the funds tendered by the Investors to the Orlandos as compensation contingent upon the Offering being successful." Am. Compl. ¶ 39. This argument is without merit. The Offering was, by all accounts, not successful. Moreover, the Orlandos are alleged to have been involved in the wrongful conduct through which they received the $60,000 benefit.

Count IV—Declaratory Judgment against White Oak

Count IV, declaratory judgment against White Oak, alleges that this is an action for a declaratory judgment as to entitlement to the funds being held by White Oak. Am. Compl. ¶ 72. Sierra contends it is entitled to the funds tendered to White Oak by the Investors, whereas White Oak contends that it is entitled to retain the Investors' funds. Am. Compl. ¶ ¶ 73–74. Sierra asks the Court to declare that Sierra is entitled to a return of the Investors' funds, with interest.

The Declaratory Judgment Act, 28 U.S.C. § 2201 states in pertinent part:

> (a) In a case of actual controversy within its jurisdiction ... any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought. Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such.

28 U.S.C. § 2201. The Supreme Court has held that "[t]he Declaratory Judgment Act was an authorization, not a command. It gave the federal courts competence to make a declaration of rights; it did not impose a duty to do so." *Public Affairs Associates, Inc. v. Rickover,* 369 U.S. 111, 112, 82 S.Ct. 580, 7 L.Ed.2d 604 (1962). "The declaratory judgment is an all-purpose remedy designed to permit an adjudication whenever the court has jurisdiction, there is an actual case or controversy, and an adjudication would serve a useful purpose." *Allstate Ins. Co. v. Employers Liability Assur. Corp.,* 445 F.2d 1278, 1280 (5th Cir.1971).[7] "The purpose behind the Declaratory Judgment Act is to afford a[ ] form of relief from uncertainty and insecurity with respect to rights, status, and other legal relations." *Casualty Indem. Exch. v. High Croft Enter.,* 714 F.Supp. 1190, 1193 (S.D.Fla.1989). The Declaratory Judgment Act "permits actual controversies to be settled before they ripen into violations of law or a breach of contractual duty." *See* 10B C. Wright & A. Miller, *Federal Practice & Procedure,* Civil 3d § 2751 (2004). Similarly, other courts have held that "declaratory judgment is inappropriate solely to adjudicate past conduct." *Gruntal & Co. v. Steinberg,* 837 F.Supp. 85, 89 (D.N.J.1993); *see also Beazer Homes Corp. v. VMIF/Anden Southbridge Venture, LPI,* 235 F.Supp.2d 485, 494 (E.D.Va.2002) (a declaration that involves the adjudication of past conduct serves no useful purpose); *Hoagy Wrecker Serv., Inc. v. City of Fort Wayne,* 776 F.Supp. 1350, 1358 (N.D.Ind.1991) (the Declaratory Judgment Act was designed to ***1231** prevent the accrual of avoidable damages, not those damages which had already occurred).

Sierra's Declaratory Judgment Act claim asks for this Court to make factual determinations regarding possible breaches of contract and tortious acts that White Oak is alleged to have committed in the past. There is no demand for relief that seeks a purely legal ruling, such as a request to resolve differences in the interpretation of specific language in an agreement. Nor does the requested relief seek a result that would lead to a change in conduct by either party in order to conform their behavior to the law or to minimize the danger of future monetary loss by the parties.

Thus, in order to render a declaratory judgment, the Court would need to make various factual determinations regarding the past conduct of the parties. However, questions regarding whether torts have been committed or a contract was adequately performed is unrelated to the purpose behind the Declaratory Judgment Act. Indeed, the purpose of the Declaratory Judgment Act is to clarify the legal relations at issue and to settle controversies prior to a legal breach of duty or contract. *See e.g., Keener Oil & Gas Co. v. Consolidated Gas Utilities Corp.,* 190 F.2d 985, 989 (10th Cir.1951) ("a party to a contract is not compelled to wait until he has committed an act which the other party asserts will constitute a breach, but may seek relief by declaratory judgment and have the controversy adjudicated in order that he may avoid the risk of damages or other untoward consequences."). Here, the Court concludes that Sierra has failed to allege sufficiently a basis upon which declaratory relief would be appropriate. Therefore, the Court finds that declaratory relief

is inappropriate and grants Defendant's motion to dismiss this claim.

Count III, V, and VI—The Fraud Claims Against All Defendants

Count III (fraudulent inducement against all Defendants), Count V (violation of Section 517.301, Florida Statutes), and Count VI (violation of 15 U.S.C. § 78j(b)) each allege fraud-based claims against all Defendants. Defendants contend that Sierra has failed to state claims for fraud and securities fraud because: (1) fraud is not pled with particularity; (2) the claims are impermissibly founded upon "scheme liability"; (3) the Investors could not have relied upon any misrepresentations or omissions because they were made directly to Sierra; (4) Sierra cannot demonstrate reliance; and (5) the economic loss rule bars such claims. The Court addresses each argument in turn.

First, the Orlandos argue that fraud is not pled with the required particularity.[8] Specifically, the Orlandos argue that, "[w]hile plaintiff alleges in a conclusory way that the Orlandos knew that White Oak intended not to use the proceeds of the transaction as required under the written contract terms and instead intended to divert $60,000 to the Orlandos, nothing in the Amended Complaint provides any basis for concluding the Orlandos could have known that." (Mot. at 15). The Orlandos are incorrect. The Amended Complaint alleges that, *prior* to the telephone call at ***1232** issue in which allegedly fraudulent misrepresentations and omissions were made regarding the nondisclosure of the Orlandos' commission, White Oak, Statham, and the Orlandos *agreed* that the Orlandos would be paid a substantial commission contingent upon the completion of the securities transaction. Am. Compl. ¶ 14–15. Thus, contrary to the Orlandos' present argument, Plaintiff has provided a basis for alleging that the Orlandos knew that White Oak intended not to use the proceeds of the transaction as disclosed to Plaintiff at the time of the telephone call at issue.

The Orlandos also argue that the fraud claims must be dismissed because they are impermissibly founded upon "scheme liability." Specifically, they argue that Sierra has not made any direct allegations against them and that "scheme liability" for securities fraud has been foreclosed by *Stoneridge Inv. Partners, LLC v. Scientific–Atlanta,* 552 U.S. 148, 128 S.Ct. 761, 169 L.Ed.2d 627 (2008). However, the "scheme liability" doctrine is inapplicable here because Sierra alleges *direct* liability against the Orlandos. Specifically, Sierra alleges that Statham and the Orlandos, "all purportedly on behalf of White Oak, contacted Sierra in Florida, via telephone, and advised Sierra that White Oak intended to offer securities to certain qualified investors." (Am.Compl.¶ 15). During the telephone call, "the Defendants failed to advise Sierra that the Orlandos would receive a commission or otherwise profit from the Offering." (Am.Compl.¶ 16). Defendants intended that Sierra would pass on the representations and omissions to potential investors, who would rely upon them, and Sierra did so. (Am.Compl.¶ 18, 24). The Orlandos' actions are directly tied to the alleged misstatements and omissions, which is more than adequate to satisfy the requirements of *Stoneridge.* Accordingly, Sierra's claims do not rely upon "scheme liability" and the Orlandos' argument is inapposite under the allegations of the Amended Complaint.

Defendants also argue that the Investors could not have relied upon any misrepresentations or omissions, or that the misrepresentations and omissions were not material, because they were made directly to Sierra, not to the Investors. The court rejected this argument for purposes of a motion to dismiss in *Slayter v. DC 701, LLC,* 2009 WL 223838 (M.D.Fla.2009):

> Finally, the Court rejects Stokes's contention that the claims asserted by Plaintiffs Donald and Camille Gillis should be dismissed because they have not alleged that Stokes directly communicated with them any fraudulent misrepresentation or omission. Their allegation that "Stokes knew his false representations to [co-Plaintiffs] the Clarks and Peter Gillis were being passed along to [them]" is sufficient to state a claim. (*Id.* at ¶ 51.) Under § 10(b), "there is no requirement that the alleged violator directly communicate misrepresentations to investors for primary liability to attach." *SEC v. Wolfson,* 539 F.3d 1249, 1261 (10th Cir.2008) (citations omitted).

Id. at *3. Similarly, here Sierra has alleged that Statham and the Orlandos, all purportedly on behalf of White Oak, contacted Sierra in Florida, via telephone, and advised Sierra that White Oak intended to offer securities to certain qualified investors. During this telephone conversation, Philip Orlando and Anthony Orlando both stated to Alan Goddard of Sierra that White Oak intended to acquire shares of restricted common stock of Gem and Volptech with the proceeds of the Offering.... During the telephone call, the Defendants failed to advise Sierra that the Orlandos would receive a commission or otherwise profit from the Offering.... The Defendants ***1233** intended that Sierra would pass on the

representations and omissions made during this telephone conversation to potential investors and the Defendants intended for those potential investors to rely upon these representations and omissions. Am. Compl. ¶ 15–18. These allegations of knowledge and intent to have Sierra pass the misrepresentations and omissions along to the Investors is sufficient to state a claim. *See Slayter,* 2009 WL 223838, *3.

Defendants additionally contend that Sierra cannot demonstrate the necessary element of reliance. They argue that the merger clause in the contracts preclude reasonable reliance. However, reliance is presumed in cases involving omissions:

> Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision.

Affiliated Ute Citizens of Utah v. U.S., 406 U.S. 128, 153–54, 92 S.Ct. 1456, 31 L.Ed.2d 741 (1972).

Defendants' reliance on *Mergens v. Dreyfoos,* 166 F.3d 1114 (11th Cir.1999) is misplaced. *Mergens* is distinguishable from the instant case because, in *Mergens,* the parties had been in an adversarial relationship and the plaintiff had made prior allegations of fraud. Under those circumstances, the court found that the plaintiffs had not proven the reliance element of fraud because reliance on misrepresentations or omissions by the opposing parties negotiating a settlement agreement in the context of a contentious and adversarial relationship is unreasonable as a matter of law. *Id.* at 1116. In contrast, here, there is no allegation that Sierra or the Investors had an adversarial relationship with the Defendants.

Defendants assert that they cannot be liable for fraud based on a material omission because they had no duty to disclose the Orlandos' commission to the Investors. "[A] defendant's omission to state a material fact is proscribed only when the defendant has a duty to disclose." *Ziemba,* 256 F.3d at 1206 (*citing Rudolph v. Arthur Andersen & Co.,* 800 F.2d 1040, 1043 (11th Cir.1986)). A duty to disclose arises under two circumstances: (1) "[w]here a defendant's failure to speak would render the defendant's own prior speech misleading or deceptive;" and (2) "where the law imposes special obligations, as for accountants, brokers, or other experts, depending on the circumstances of the case." *Id.* Factors to be considered in determining whether a duty to disclose exists include: "the relationship between the plaintiff and defendant, the parties' relative access to the information to be disclosed, the benefit derived by the defendant from the purchase or sale, defendant's awareness of plaintiff s reliance on defendant in making its investment decision, ... defendant's role in initiating the purchase or sale [,] ... the extent of the defendant's knowledge and the significance of the misstatement, fraud or omission, [and] ... [t]he extent of the defendant's participation in the fraud." *Id.; Cordova v. Lehman Bros., Inc.,* 526 F.Supp.2d 1305 (S.D.Fla.2007). Consideration of these factors suggests that Defendants may have had a duty to disclose in this situation, which is ultimately a question of fact. It is alleged that Defendants had full access to the undisclosed information prior to the transaction, whereas Plaintiff had no access to the information. Am. Compl. ¶ 14, 16. Defendants are alleged to have derived a substantial benefit, namely $232,000 to White Oak and Statham and $60,000 to the Orlandos, from this transaction. Am. Compl. ¶ 52–53. Sierra alleges that Defendants intended that Sierra ***1234** would pass on the misrepresentations/omissions to the Investors and that Defendants intended for the Investors to rely on such. Am. Compl. ¶ 18. Defendants are alleged to have initiated the securities transaction at issue. Am. Compl. ¶ 12–15. The Amended Complaint alleges that, *prior* to the telephone call at issue in which allegedly fraudulent misrepresentations and omissions were made regarding the nondisclosure of the Orlandos' commission, White Oak, Statham, and the Orlandos agreed that the Orlandos would be paid a substantial commission contingent upon the completion of the securities transaction. Am. Compl. ¶ 14–15. Accordingly, based on the allegations in the Amended Complaint, there are sufficient allegations pled that Defendants had a duty to disclose the Orlandos' commission, which was undoubtedly significant, accounting for more than 25% of the entire investment funds, and correspondingly reducing the amount of operating capital available for the company the investors intended to acquire through the Offering. The Court cannot conclude on a motion to dismiss that there was no duty to disclose as a matter of law.

Lastly, Defendants argue that the fraud claims are barred by the economic loss rule. Under Florida law, "[t]he economic loss rule is a judicially created doctrine that sets forth the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

circumstances under which a tort action is prohibited if the only damages suffered are economic losses." *Indem. Ins. Co. v. Am. Aviation, Inc.,* 891 So.2d 532, 536 (Fla.2004). In relevant part, this doctrine applies "when the parties are in contractual privity and one party seeks to recover damages in tort for matters arising from the contract." *Id.* The rule is "designed to prevent parties to a contract from circumventing the allocation of losses set forth in the contract by bringing an action for economic loss in tort." *Id.* However, the economic loss doctrine is not applicable to Sierra's fraud claims. First, "the economic loss rule does not bar tort actions based on fraudulent inducement." *D & M Jupiter, Inc. v. Friedopfer,* 853 So.2d 485, 487 (Fla. 4th DCA 2003). *See also Allen v. Stephan Co.,* 784 So.2d 456 (Fla. 4th DCA 2000) ("The law is well established that the economic loss rule does not bar tort actions based on fraudulent inducement."); *May v. Nygard Holdings Ltd.,* 203 Fed.Appx. 949, 2006 WL 2918908, *1–2 (11th Cir.2006). Similarly, the economic loss rule does not bar Sierra's statutory claims, such as the fraud claims brought for violations of Section 517.301, Florida Statutes, and 15 U.S.C. § 78j(b). *Comptech Intern., Inc. v. Milam Commerce Park, Ltd.,* 753 So.2d 1219 (Fla.1999).

Conclusion

For the foregoing reasons, it is hereby **ORDERED AND ADJUDGED** as follows:

1. Defendants White Oak and Statham's Motion to Dismiss (DE 35) is **GRANTED IN PART AND DENIED IN PART** as follows:

a. The motion to dismiss for lack of personal jurisdiction is **DENIED** as to White Oak and Statham.

b. The motion to dismiss for failure to state a claim is **GRANTED** as to Count IV, declaratory judgment against White Oak. The motion is **DENIED** as to the remaining counts against White Oak and Statham.

2. Defendants Philip Orlando and Anthony Orlando's Motion to Dismiss the First Amended Complaint (DE 36) is **DENIED.**

All Citations

650 F.Supp.2d 1213

Footnotes

1 Although *Eaton* and the binding Fifth Circuit cases upon which it relies address subject matter jurisdiction, the Court concludes that the reasoning of these cases apply with equal force to personal jurisdiction.

2 Defendants may renew their arguments in a summary judgment motion. However, if genuine issues of material issues of fact exist, then the issue will need to be presented at trial. *Lawrence v. Dunbar,* 919 F.2d 1525, 1530 (11th Cir.1990).

3 The alleged tort of fraudulent misrepresentation or omission and the other tort and contract-related claims in this case arise out of a common nucleus of operative facts. Thus, the doctrine of "pendent personal jurisdiction" comes into play. Under this doctrine, as long as personal jurisdiction can be asserted over Defendants for the tort claims, there would be also be personal jurisdiction over them for the related claims. *See Cincinnati Ins. Co. v. Belkin Corp.,* No. 07–0615–WS–C, 2008 WL 4949783, at *16 (S.D.Ala. Nov. 14, 2008) *citing Action Embroidery Corp. v. Atlantic Embroidery, Inc.,* 368 F.3d 1174 (9th Cir.2004); *United States v. Botefuhr,* 309 F.3d 1263, 1272–75 (10th Cir.2002); *Robinson Eng'g Co., Ltd. Pension Plan Trust v. George,* 223 F.3d 445, 449–50 (7th Cir.2000); *ESAB Group, Inc. v. Centricut, Inc.,* 126 F.3d 617, 628–29 (4th Cir.1997); *IUE AFL–CIO Pension Fund v. Herrmann,* 9 F.3d 1049, 1056–57 (2d Cir.1993); *Oetiker v. Werke,* 556 F.2d 1, 5 (D.C.Cir.1977); *Robinson v. Penn Cent. Co.,* 484 F.2d 553, 555–56 (3d Cir.1973). Additionally, White Oak is subject to personal jurisdiction in Florida by contract. *See infra.*

4 Under the terms of the Selling Agreement between Sierra and White Oak, each Closing between the investors and White Oak was to be held at Sierra's offices in Boca Raton, FL, at a time and date mutually agreed upon by White Oak and Sierra. (Am. Comp. Ex. "A" at ¶ 1.7.). The Subscription Agreements, similarly, provided for the Closings to occur at Sierra's offices in Boca Raton, Florida. (Am. Comp. Ex. "B" at ¶ 2.). It could also be argued that, by allegedly breaching the Subscription Agreements, White Oak is alleged to have breached

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

a contract that was to be performed in Florida, providing an additional basis for long-arm jurisdiction against White Oak. *See* § 48.193(1)(g), Fla. Stat.

5 Similarly, Statham can be bound by the Florida forum selection clause as he is the sole and controller shareholder of White Oak and, as such, the Offering would inure to his personal benefit. *See XR Co. v. Block & Balestri, P.C.,* 44 F.Supp.2d 1296, 1298 (S.D.Fla.1999); *Lipcon v. Underwriters at Lloyd's, London,* 148 F.3d 1285, 1290 (11th Cir.1998). This is an additional factor supporting the conclusion that Statham should reasonably anticipate being haled into court in Florida.

6 On or about August 23, 2006, Statham executed the Selling Agreement as Managing Partner of White Oak in Georgia. (Declaration of Ross Statham, DE 7–2 at ¶ 31).

7 The decisions of the United States Court of Appeals for the Fifth Circuit, as that court existed on September 30, 1981, handed down by that court prior to the close of business on that date, shall be binding as precedent in the Eleventh Circuit, for this court, the district courts, and the bankruptcy courts in the circuit. *See Bonner v. Prichard,* 661 F.2d 1206, 1207 (11th Cir.1981) (en banc).

8 The Eleventh Circuit has held:

> Rule 9(b) is satisfied if the complaint sets forth (1) precisely what ... oral representations or what omissions were made, and (2) the time and place of each such statement and the person responsible for making (or, in the case of omissions, not making) same, and (3) the content of such statements and the manner in which they misled the plaintiff, and (4) what the defendants obtained as a consequence of the fraud.

Ziemba v. Cascade Intl., 256 F.3d 1194, 1202 (11th Cir.2001).

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-30

2002 WL 31894720
Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of Connecticut.

Douglas SPINGOLA,
v.
WHITEWATER MOUNTAIN RESORTS OF CONNECTICUT, INC. d/b/a Powder Ridge Ski Area et al.

No. CV010094538S.
|
Dec. 10, 2002.

Attorneys and Law Firms

Averum Sprecher, Middletown, for Douglas Spingola.

Howd & Ludorf, Hartford, for White Water Mountain Resorts of Connecticut, Inc. and White Water Mountain Resorts, Inc.

Opinion

RICHARD A. ROBINSON, J.

***1** The instant action was brought in a two Count Amended Complaint. The Plaintiff Douglas Spingola (hereinafter "Spingola") alleges that the Defendant White Water Mountain Resorts of Connecticut, Inc. (hereinafter "Whitewater") is a corporation duly organized and existing under the laws of the state of Connecticut and doing business as Powder Ridge Ski Area in Middlefield, Middlesex County, Connecticut.

The Plaintiff further alleges that on February 27, 1999, he and his family went to Powder Ridge Ski Area to go snow tubing. When he finished snow tubing he used a walkway from the tubing area when he was caused to slide and fall and become injured.

The Plaintiff alleges that at the time that he was injured, he was an invitee on the Defendants' premises.

On April 4, 2002, the Defendants filed a Motion for Summary Judgment. The Defendants assert that at the time that the Plaintiff was injured he was not an "invitee" but a "licensee." The Defendants further assert that even assuming that the Plaintiff enjoyed the status of an invitee, there is no evidence that a defect existed and/or that the Defendants had actual or constructive notice of the same for such a period of time that they could have corrected it.

Before addressing the merits of Defendants' motion, a brief review of the standards for the granting of a Motion for Summary Judgment is warranted:
"Practice Book [§ 17-49] provides that summary judgment shall be rendered forthwith if the pleadings, affidavits and any other proof submitted show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law ... In deciding a motion for summary judgment, the trial court must view the evidence in the light most favorable to the nonmoving party ...

"A material fact is a fact that will make a difference in the outcome of the case ... Once the moving party has presented evidence in support of the motion for summary judgment, the opposing party must present evidence that demonstrates the existence of some disputed factual issue ... It is not enough, however, for the opposing party merely to assert the existence of such a disputed issue. Mere assertions of fact ... are insufficient to establish the existence of a material fact and, therefore, cannot refute evidence properly presented to the court ..." (Citations omitted; internal quotation marks omitted.) *Yancey v. Connecticut Life & Casualty Ins. Co.,* 68 Conn.App. 556, 558-59, 791 A.2d 719 (2002).

Christian v. Gouldin, 72 Conn.App. 14, 18 (2002).

Section 17-45 of the Connecticut Practice Book concerns the proceedings for motions for summary judgment. It provides that:

> A motion for summary judgment shall be supported by such documents as may be appropriate, including but not limited to affidavits, certified transcripts of testimony under oath, disclosures, written admissions and the like. The motion shall be placed on the short calendar to be held not less than fifteen days following the filing of the motion and the supporting materials, unless the judicial authority otherwise directs. The adverse party [prior to the day the case is set down for short calendar] shall at least

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> five days before the date the motion is to be considered on the short calendar file opposing affidavits and other available documentary evidence. Affidavits, and other documentary proof not already a part of the file, shall be filed and served as are pleadings.

***2** The Plaintiff alleges in his Complaint that at the time that he was injured he was a business invitee of the Defendants and as such they owed him a duty of care.

The law in our state is well settled as to the duty owed by a property owner when an individual enters upon their land as an invitee:

"Invitees fall into certain general categories. A public invitee is a person who is invited to enter or remain on land as a member of the public for a purpose for which the land is held open to the public ... A business invitee is a person who is invited to enter or remain on land for a purpose directly or indirectly connected with business dealing with the possessor of land ... General Statutes § 52-557a, which provides that [t]he standard of care owed to a social invitee shall be the same as the standard of care owed to a business invitee, in effect recognizes a third kind of invitee, namely, the social invitee. The distinction between one who is an invitee and one who is merely a licensee turns largely on whether the visitor has received an invitation, as opposed to permission, from the possessor of land, to enter the land or remain on the land. Although an invitation itself does not establish the status of an invitee, it is essential to it. Mere permission, as distinguished from invitation, is sufficient to make the visitor a licensee but it does not make him an invitee." (Citations omitted; internal quotation marks omitted). *Corcoran v. Jacovino,* 161 Conn. 462, 465-66, 290 A.2d 225 (1971).

Kurti v. Becker, 54 Conn.App. 335, 338 (1999).

Plaintiff in his complaint specifically pleads that he is a business invitee.

Typically, "[f]or the plaintiff to recover for the breach of a duty owed to her as a business invitee, she ha[s] to allege and prove that the defendant had actual or constructive notice of the presence of the specific unsafe condition that caused her [injury] ... Either type of notice must be notice of the very defect which occasioned the injury and not merely of conditions naturally productive of that defect even though subsequently in fact producing it ... If the plaintiff, however, alleges an affirmative act of negligence, i.e., that the defendant's conduct created the unsafe condition, proof of notice is not necessary." (Citations omitted)

Meek v. Wal-Mart Stores, Inc., 72 Conn.App. 467, 474 (2002). [A] defendant owe[s] the plaintiff the duty to maintain its premises in a reasonably safe condition. *Gulycz v. Stop & Shop Cos.,* 29 Conn.App. 519, 521, 615 A.2d 1087, cert. denied, 224 Conn. 923, 618 A.2d 527 (1992). To hold the defendant liable for her personal injuries, the plaintiff must prove (1) the existence of a defect, (2) that the defendant knew or in the exercise of reasonable care should have known about the defect and (3) that such defect had "existed for such a length of time that the [defendant] should, in the exercise of reasonable care, have discovered it in time to remedy it." *Cruz v. Drezek,* 175 Conn. 230, 238-39, 397 A.2d 1335 (1978).

***3** *Martin v. Stop & Shop Supermarket Cos.,* 70 Conn.App. 250, 251 (2002).

The Defendants, in their Motion for Summary Judgment assert that the Plaintiff was not a business invitee, but a licensee.

"In general, there is an ascending degree of duty owed by the possessor of land to persons on the land based on their entrant status, i.e., trespasser, licensee or invitee." ... [I]n premises liability actions, the standard of care depends on the status of the visitor once the ownership status is determined.

Monterose v. Cross, 60 Conn.App. 655, 663 (2000).

Whereas the Defendants assert that the Plaintiff was a licensee, a discussion of a property owner's duty to a licensee is warranted.

"A licensee is a person who is privileged to enter or remain upon land by virtue of the possessor's consent, whether given by invitation or permission." (Internal quotation marks omitted.) *Laube v. Stevenson,* 137 Conn. 469, 473, 78 A.2d 693 (1951). The duty that a landowner "owes to a licensee ... does not ordinarily encompass the responsibility to keep the property in a reasonably safe condition, because the licensee must take the premises as he [or she] finds them ... If the licensor actually or constructively knows of the licensee's presence on the premises, however, the licensor must use reasonable care both to refrain from actively

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

subjecting him [or her] to danger and to warn him [or her] of dangerous conditions which the possessor knows of but which he [or she] cannot reasonably assume that the licensee knows of or by reasonable use of his [or her] faculties would observe." (Citations omitted; internal quotation marks omitted.) *Morin v. Bell Court Condominium Assn., Inc., supra,* 223 Conn. at 327-29.

Salaman v. City of Waterbury, 246 Conn. 298, 305 (1998).

The Plaintiff asserts that he was invited to the subject premises. In support of his Objection to the Motion for Summary Judgment the Plaintiff submitted excerpts of his deposition that was taken on January 31, 2002. The excerpts provide in pertinent part as follows:

A. I had heard an advertisement on the radio several times promoting the snow tubing.

B. Do you recall what the substance of the advertisement was?

C. Well, it was a family tubing fun. I heard it several times on the radio, bring your family to Powder Ridge for snow tubing activities, great family thing, fun thing to do.

(See deposition at page 14.)

It is the Plaintiff's contention that the aforementioned advertisement was an invitation for him to enter upon the Defendants' property for the purposes of snow tubing, which is what he alleges to have done and therefore he is a business invitee. However, the Defendants assert that Powder Ridge charges a fee and requires customers to sign a waiver and release form in exchange for the benefit of using its snow park, lift and tubes. (See Defendant's Exhibit B, Affidavit of Chad Johnson at paragraph 5.)

It is undisputed that the Plaintiff did not purchase any tickets or sign any waiver and release forms upon entering the park. Instead, he received tickets from an unidentified woman, who gave him her tickets without receiving any compensation. (See Memorandum in Support of Motion for Summary Judgment at Page 2, and Defendants' Exhibit A, Page 20, lines 12-22, inclusive.)

***4** The Defendants assert that while the Plaintiff may have been an invitee when he arrived on their premises, since he did not follow their procedures of purchasing a ticket and signing the waiver and release forms before entering into the snow tubing park he was not an invitee, but at best a licensee in that area of their premises.

> [A]n invitee who exceeds the limits of his invitation loses his status as an invitee ...

Frankovitch v. Burton, 185 Conn. 14, 21 (1981).

The Defendants assert that the tickets that were given to the Plaintiff by the unidentified are not transferable. Exhibit "B" the Defendants' Reply Memorandum in Support of the Motion for Summary Judgments is a copy of a Powder Ridge ticket that the Defendants purport to be similar to the tickets that the unidentified woman gave to the Plaintiff. The copy of the ticket provides in pertinent part that it is "NOT TRANSFERABLE." It also states that it is "NON REFUNDABLE" and contains a price, date, time of expiration and language concerning the bearer's assumption of risk.

The Plaintiff asserts that Connecticut has adopted the modern view of antiassignment provisions in contracts:

Our analysis of the effect of the antiassignment provision begins by emphasizing that the modern approach to contracts rejects traditional common-law restrictions on the alienability of contract rights in favor of free assignability of contracts. See 3 Restatement (Second), Contracts § 317, p. 15 (1981) ("[a] contractual right can be assigned"); J. Murray, Jr., Contracts (3d Ed.1990) ("the modern view is that contract rights should be freely assignable"); 3 E. Farnsworth, Contracts (2d Ed.1998) § 11.2, p. 61 ("[t]oday most contract rights are freely transferable"). Common-law restrictions on assignment were abandoned when courts recognized the necessity of permitting the transfer of contract rights. "The force[s] of human convenience and business practice [were] too strong for the common-law doctrine that [intangible contract rights] are not assignable." (Internal quotation marks omitted.) J. Murray, Jr., *supra,* § 135, p. 791. "If the law were otherwise, our modern credit economy could not exist." 3 E. Farnsworth, *supra,* § 11.2, p. 61. As a result, an assignor typically can transfer his contractual right to receive future payments to an assignee. See *Western United Life Assurance Co. v. Hayden,* 64 F.3d 833, 841 (3d Cir.1995); 3 E. Farnsworth, *supra,* § 11.2, pp. 61, 66.

The parties to a contract can include express language to limit assignment and courts generally uphold these contractual

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

antiassignment clauses. See 3 Restatement (Second), *supra,* § 317, p. 15 ("[a] contractual right can be assigned unless ... assignment is validly precluded by contract"); 3 E. Farnsworth, *supra,* § 11.4, pp. 82 ("most courts have upheld [terms prohibiting assignment] as precluding effective assignment"). Given the importance of free assignability, however, antiassignment clauses are construed narrowly whenever possible. See 3 E. Farnsworth, *supra,* § 11.4, pp. 82-83.

***5** In interpreting antiassignment clauses, the majority of jurisdictions now distinguish between the assignor's "right" to assign and the "power" to assign (modern approach).

Rumbin v. Utica Mutual Ins., 254 Conn. 259, 267 (2000).

The Court reasoned that:

> The modern approach thus serves the dual objectives of free assignability of contracts together with full compensation for any actual damages that might result from an assignment made in breach of an antiassignment provision.

Rumbin, Id. at 278.

It is clear that the Courts of this state have adopted the modern approach to antiassignment of contracts, an approach that includes the power to contract away prohibitions against assignment.

> The modern approach, however, is not adopted by some courts, which uphold antiassignment clauses regardless of whether the parties have included contractual language that expressly limits the power to assign or expressly invalidates the assignment itself. We agree with these courts that contracting parties can exercise their freedom to contract to overcome free alienability when they include the appropriate contractual language.

Rumbin, Id. at 272.

Although *Rumbin* concerned annuity contracts, its dicta indicates that the issues concerning antiassignment provisions are applicable to all contracts.

The antiassignment provision in the instant action provides that the Powder Ridge ticket is not transferable. This limited the unidentified woman's right to transfer the ticket to the Plaintiff, but not her power to do so. The ticket does not contain any express language to limit the power to assign or to void the assignment itself.

The Defendant's argument concerning the Plaintiff's entrant status was based on the issue concerning the transfer of the ticket and this Court's holding on the Plaintiff's entrant status is limited to said issue. While the Court does come to the conclusion that the transfer of the ticket does not convert the Plaintiff's entrant status from a invitee to a licensee, its holding is narrow as to this issue alone. In light of the foregoing, there is a genuine issue of material fact as to what the Plaintiff's entrant status was at the time of the incident in question.

The Defendants further assert that even assuming that the Plaintiff enjoyed the status of an invitee, there is no evidence that a defendant existed, and/or that the Defendants had actual or constructive notice of same for such a period of time what they could have corrected it.

The Plaintiff filed an affidavit in support of his Objection to the Motion for Summary Judgment. It provides in pertinent part that:
16. That, when we finished tubing we gathered up our tubes and placed them at a return area, and then followed a neon-like rope which lead toward the bottom of the hill on a path of packed-like snow. This path cumulated in a downward sloping ramp with a grade of about 20 degrees-30 degrees; this ramp had a dark, carpet-like material covering it, was constructed of a hard material under the carpet, and was about ten (10) to fifteen (15) feed in length. This ramp did not have a solidly fixed side railing(s), and in, contrast to the artificial illumination on the hill where the actual tubing activity took place, the lighting at the ramp was very dim ...

***6** 20 ... I had not been able to tell whether the carpet was wet before I stepped onto it and started sliding, I could now tell it was wet and "slick." I could not see or feel any sand or

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

any abrasive material on this carpet-like covering even while sitting right down on it.

21. That a couple of men who appeared to be Whitewater employees, because they were putting snow tubes into a large container located at that site, finally came over and helped me move to a nearby wooden box.

22. That, at that point I noticed a fifty-five (55) gallon drum containing sand. The drum had an opening in to put a shovel in to get sand out, was within the immediate proximity of the bottom of the ramp where I was injured.

Whereas the Defendants in this matter are seeking Summary Judgment, they have the burden of proving that there are no genuine issues of material fact.

> ... Practice Book [§ 17-49] provides that summary judgment shall be rendered forthwith if the pleadings, affidavits and any other proof submitted show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law ... In deciding a motion for summary judgment, the trial court must view the evidence in the light most favorable to the nonmoving party ... The party seeking summary judgment has the burden of showing the absence of any genuine issue [of] material facts which, under applicable principles of substantive law, entitle him to a judgment as a matter of law ... and the party opposing such a motion must provide an evidentiary foundation to demonstrate the existence of a genuine issue of material fact. (Citations omitted; internal quotation marks omitted.) *Kronberg v. Peacock,* 67 Conn.App. 668, 671, 789 A.2d 510, cert. denied, 260 Conn. 902, 793 A.2d 1089 (2002).

Billerback v. Cerminara, 72 Conn.App. 302, 305 (2002).

The Plaintiff's affidavit shows that there are genuine issue of material fact as to whether the Defendants knew or "should" have known about the alleged condition of the ramp in question. The Plaintiff's affidavit indicates that the subject ramp was a highly traveled source of egress from the snow tubing area. The Defendants had placed sand containers near the site of the alleged accident, but allegedly had not placed any sand on the ramp. The lighting of the ramp was allegedly dimmer than the surrounding area.

The Defendants have failed to meet their burden of proving that there are not any genuine issues of material fact remaining, the Motion for Summary Judgment is therefore denied.

For all of the reasons cited herein, the Defendants' Motion for Summary Judgment is denied.

All Citations

Not Reported in A.2d, 2002 WL 31894720

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-31

44 Or.App. 133
Court of Appeals of Oregon.

SPRINGFIELD INTERNATIONAL RESTAURANT, INC., an Oregon Corporation, d/b/a International Restaurant and Bernard E. Cooke, Appellants,
v.
Larry C. SHARLEY, M & L Enterprises, Inc., an Oregon Corporation and David N. Burks, Respondents.

No. 75-0125; CA 11467.
|
Argued and Submitted Sept. 10, 1979.
|
Decided Jan. 28, 1980.

Synopsis
Action was brought for conversion by wrongful execution and for tortious interference with contract and for tortious interference with business relationship. The Circuit Court, Lane County, Roland K. Rodman, J., awarded nominal damages of $25 and punitive damages of $1,500 and plaintiffs appealed. The Court of Appeals, Schwab, C. J., held that: (1) plaintiffs' right to possession and control of property would not give them right to maintain action for conversion by wrongful execution; (2) evidence supported implied findings that plaintiffs had not owned all of the property seized and that there was no basis in record to determine value of plaintiffs' property that had been seized; (3) where one plaintiff contended that any execution was wrongful because underlying judgment had been assigned to him, trial court was entitled to find that permitting that plaintiff to review assignment form before it was placed in escrow was not a formal delivery of the assignment to him and that there had been no assignments in legal sense of immediate, unconditional transfer of rights; and (4) with respect to causes of action for tortious interference with contract and tortious interference with business relationship, substantial evidence supported conclusion that motives for the alleged interference were not improper.

Affirmed.

Procedural Posture(s): On Appeal.

Attorneys and Law Firms

***134** ****1189** Michael L. Williams, Eugene, argued the cause for appellants. With him on the briefs were Arthur C. Johnson, Timothy J. Sercombe, Martha W. Reidy, Donald K. Armstrong, and Johnson, Harrang & Mercer, Eugene.

Scott M. Galenbeck, Springfield, argued the cause for respondents. With him on the brief was Lively & Wiswall, Springfield.

Before SCHWAB, C. J., and LEE and RICHARDSON, JJ.

Opinion

***135** SCHWAB, Chief Judge.

This is primarily an action for conversion by wrongful execution. The trial court, sitting without a jury, awarded plaintiffs' nominal damages of $25 and punitive damages of $1500. Plaintiffs appeal, urging their entitlement to far greater damages.

The facts involve a series of complex, multi-sided financial transactions that all relate to a restaurant located in a large motel-restaurant complex at an interstate highway interchange in Springfield. Over about a year-and-a-half period several different persons had a variety of interests in the restaurant. The execution alleged to have been wrongful consisted of the seizure of the cash, checks, credit card receipts, food and liquor located at the restaurant. The basic issue is whether these items were the property of plaintiffs, or, instead, the property of the judgment debtor, William Brenner, as claimed by defendants.

Brenner leased the restaurant facilities when the motel-restaurant first opened in ****1190** early 1973. He began operating the "International Restaurant" therein. A liquor license for the restaurant was taken out under the names of Brenner and his wife.

Larry Sharley is the sole stockholder in M & L Enterprises, Inc. In mid-1973, Brenner agreed to sell the restaurant operation to M & L Enterprises, one of the conditions being that M & L obtain a transfer of the liquor license. Sharley, through M & L Enterprises, then took possession of the restaurant and operated it for several months. When complications arose regarding the liquor license transfer, Brenner cancelled his agreement to sell to M & L, and resumed operation of the restaurant. M & L then sued Brenner

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

and obtained judgment against him for $38,150. The terms of that judgment permitted it to be paid in installments. The first installment was due November 10, 1974.

Bernard Cooke, one of the plaintiffs, worked intermittently ***136** for Brenner, on a rather informal basis, as the manager of the International Restaurant both before and after the months that Sharley had possession of and operated the restaurant.

John Rapolla and Rita Squier worked intermittently at the restaurant during the times Cooke managed it. Seemingly, like everybody involved in this controversy, they were interested in buying the restaurant.

On October 1, 1974, Brenner executed a bill of sale that purported to transfer all the restaurant assets except the inventory to Cooke. Cooke then proceeded to organize Springfield International Restaurant, Inc., in which he was the sole stockholder, and transferred those restaurant assets covered by the bill of sale to the corporation. About the same time, Cooke, as seller, and Rapolla and Squier, as buyers, entered into an agreement whereby Cooke was to sell them all of the outstanding shares in Springfield International Restaurant, Inc. As part of the purchase price, Rapolla and Squier were required to get Sharley to assign to Cooke the judgment that M & L Enterprises had against Brenner.

Sharley, as president of M & L, and the corporate secretary both executed such an assignment on November 7, 1974. It was taken to Cooke, apparently to be reviewed for form, and then placed in escrow with M & L's attorney pending closing of the sale of the restaurant from Cooke to Rapolla and Squier.

The first installment of the M & L judgment against Brenner was not paid November 10 when due. Sharley, on behalf of M & L, obtained a writ of execution on that judgment. On November 26 the sheriff levied on that execution by going to the restaurant and seizing all of the cash, checks, credit card receipts, food and liquor.

I

In support of their wrongful-execution claim, plaintiffs, Cooke and Springfield International Restaurant, ***137** Inc., first claim that they need not prove they had legal title to the property seized, but only that they had the right to possession and control. This contention is based on Mustola v. Toddy, 253 Or. 658, 662-63, 456 P.2d 1004 (1969), in which the court adopted the definition of conversion found in s 222A of the Restatement (Second) of Torts (1965). That section provides in part:

> "Conversion is an intentional exercise of dominion or control over a chattel which so seriously interferes with the Right of another to control it that the actor may justly be required to pay the other the full value of the chattel." (Emphasis supplied.)

Regardless of who would have sufficient right of control of a chattel to sue for conversion in other contexts, in the context of conversion by wrongful execution we conclude that legal title is controlling. ORS 23.040(1) permits execution "(a)gainst the property of the judgment debtor." It would render this statute meaningless if a judgment debtor could transfer to another some right of control over property he had title to and thereby insulate it from execution.

The extreme nature of plaintiffs' reliance on Restatement (Second) of Torts, s 222A (1965), is illustrated by their argument: ****1191** "Even if (Springfield International Restaurant, Inc.) is viewed as a bailee holding Mr. Brenner's goods in a bailor-bailee relationship the corporation still has the right to bring an action (for conversion for) the total value of the goods seized * * *." Writs of execution are often served on banks. It would be preposterous to conclude that, when a judgment creditor executes on the property of a judgment debtor that is in the possession of a bank, the bank then has a cause of action against the judgment creditor for conversion. See Restatement (Second) of Torts, s 266 (1965).

Plaintiffs seem to claim alternatively that they, not Brenner, had title to the property seized. Plaintiff Cooke also contends that any execution was wrongful because the underlying judgment had been assigned to him. The persons involved structured their various ***138** transactions in such ways that we cannot say as a matter of law that plaintiffs are entitled to prevail on either theory.

The October 1 bill of sale from Brenner to Cooke covering the restaurant assets states "except that the transfer does not include any inventory." This document indicates that title to the inventory remained in Brenner. Cooke then formed his wholly-owned corporation, Springfield International, and transferred to it "all personal property, assets, tangible and intangible, except inventory * * *." Cooke's agreement to sell the stock in his corporation to Rapolla and Squier included the following: "The Seller represents and warrants

that Springfield International Restaurant, Inc. has purchased all of the assets of the (restaurant) except inventory."

The sale agreement between Cooke and Rapolla/Squier also stated:

> "Business of the corporation (i. e., Springfield International Restaurant, Inc.) shall be conducted by William F. Brenner up to the date of closing in the normal and regular manner and will not enter into any contract except as may be required in the regular course of business without the approval of the Purchasers herein."

The sale was never closed. If, as contended by plaintiffs, Brenner had no interest in the restaurant after the October 1 bill of sale to Cooke, this provision is inexplicable.

Equally mysterious is the parties' treatment of the liquor license. It remained in Brenner's name up to the day of execution. Cooke, who claims he received all of Brenner's interest in the restaurant almost two months before the execution, never applied for a transfer of the liquor license to his name or the name of his corporation. All of the parties involved were experienced business people. More specifically, all of them knew that the Oregon Liquor Control Commission had previously fined Brenner for permitting ***139** Sharley, through M & L Enterprises, to operate the restaurant under Brenner's license the prior year. Under these circumstances, the lack of any effort to transfer the license to Cooke or his corporation at least supports a strong inference that Brenner retained some interest in some of the restaurant assets up until the time of execution.

We interpret the trial court's award of nominal damages to be based on a finding that plaintiffs had not proven they owned all of the property seized, and the further finding that there was no basis in this record to determine the value of plaintiffs' property that was seized. There is substantial evidence to support such findings. In fact, had defendants cross-appealed, the closer question would be whether there was evidence that plaintiffs owned any of the property.

Turning to the question of the assignment of the underlying judgment from Sharley and M & L to Cooke, we again confront curious provisions in the various transactions. Cooke's agreement to sell to Rappola and Squier refers to the assignment of that judgment and then states:

> All payments made on this judgment prior to closing shall go to the judgment holder (i. e., M & L Enterprises) and the Seller herein (i. e., Cooke) is to receive a commensurate amount added to the (sale price)."

****1192** It thus appears that the parties to that agreement, including Cooke, intended that the contemplated assignment of the judgment did not affect Brenner's obligation to make payments to Sharley through M & L between the date of the agreement and the closing of the restaurant sale.

Plaintiffs now make a variety of arguments for a contrary conclusion:

> " * * * (T)he assignment of the judgment to Cooke removed all rights to execute upon it. The placing of the assignment into escrow did not somehow mean ***140** that Sharley could act as if the assignment had never taken place. The very nature of an escrow places the subject of the escrow beyond the control of the grantor * * *."

Plaintiffs seemingly confuse an assignment in the sense of a present, immediate transfer of rights, I. e., an executed transaction, and promise to assign in the future or conditional promise to assign, I. e., an executory transaction. "An 'assignment' of a right is a manifestation to another person by the owner of the right indicating his intention to transfer, without further action or manifestation of intention, the right to such other person or to a third person." Restatement, Contracts, s 149(1). (1932). "A contract to assign a right in the future is not an assignment * * *." Restatement, Contracts, s 166(1) (1932).

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

All of the evidence at trial was to the effect that M & L's November 7 assignment to Cooke of its judgment against Brenner was only one part of the larger transaction whereby Cooke intended to sell Springfield International Restaurant, Inc. to Rapolla and Squier; with the formal delivery of the assignment to Cooke actually effectuating the assignment not intended until that transaction closed in escrow; and with closing dependent on numerous conditions that had not yet occurred at the time of execution of the assignment. The trial court was entitled to find that permitting Cooke to review the assignment for form before it was placed in escrow was not a formal delivery of the assignment to Cooke. Under all these circumstances, the trial court was entitled to conclude that there was no assignment in the legal sense of an immediate, unconditional transfer of rights.

Plaintiffs also overstate the law in the claim that "the very nature of an escrow" terminated M & L's rights to execute on its judgment. The effect of placing an assignment of judgment in escrow depends primarily on the parties' instructions to the escrow agent. See Vendeventer v. Dale Construction, 277 Or. 817, 562 P.2d 196 (1977); ***141** Hays v. Hug, 243 Or. 175, 412 P.2d 373 (1966); Kinney v. Schlussel et al., 116 Or. 376, 239 P. 818 (1925). There is no evidence in this record of the instructions to the escrow agent other than inferences that might be drawn from the Cooke-Rappola/ Squier agreement to convey the restaurant. And, as stated above, that agreement provided that all payments made on the judgment prior to closing shall go to the judgment holder, M & L Enterprises. Under these circumstances, there is no basis in this record for saying that as a matter of law the mere act of placing an assignment of judgment in escrow pursuant to unknown instructions terminated M & L's right to execute on the judgment.

II

In addition to the wrongful-execution claim, Cooke pleaded two causes of action against M & L Enterprises and two causes of action against Sharley: tortious interference with contract and tortious interference with a business relationship. See generally, Top Service Body Shop v. Allstate Ins. Co., 283 Or. 201, 582 P.2d 1365 (1978). All of these causes of action are based on the fact that after the seizure of the restaurant's assets the existing relationship and contemplated sale between Cooke and Rapolla/Squier collapsed.

The trial court entered judgment for defendants on all of these causes of action. Plaintiff Cooke claims some error was thus committed, although the scope of the assignment of error is unclear. His brief states:

> ****1193** "The court erred in finding for the Defendants on Plaintiff Bernard E. Cooke's cause of action for interference with his prospective sale of the restaurant.
>
> "* * *
>
> "The (complaint) should be construed to assert a cause of action stating a general tort for interference with economic and business relations or loss of prospective advantage rather than only the narrower tort of interference with a specific contract * * *."

This may mean that plaintiff is abandoning his claim for interference with contract although on the facts ***142** of this case in which the business relationship claimed to have been interfered with was the contemplated sale to Rapolla and Squier, which was already the subject of a signed agreement, plaintiff apparently finds more significance than we do in how his claim should be labeled.

Aside from the issue plaintiff has preserved, the precise nature of the error he claims was committed is unclear. Plaintiff's brief states:

> "* * * the evidence also established that one result of the wrongful execution was to destroy Cooke's ability to sell (the restaurant) because (the owner of the motel-restaurant complex) defaulted Cooke and Brenner on their lease * * *."

This statement is not supported by the record. All of the evidence is that one or two days after the execution, the owner of the restaurant facility, Cooke and Brenner met and all signed a lease cancellation agreement. There is no evidence that Cooke's participation in the lease cancellation was other than voluntary. So as a matter of causation, Cooke's inability to sell the business could have been due to his own conduct.

Plaintiff's brief also states:

> " * * * Since the trial court found the purpose of Sharley was to harm Cooke's business, and since execution on the escrowed and assigned judgment obviously blew apart the prospective sale to Rapolla and Squier, Plaintiff is entitled to recover as a matter of law."

We have already concluded that the placing of an assignment of the judgment in escrow did not, on this record, have the legal effect plaintiffs claim; to the extent that the tortious interference claim is based on these same acts, it fails for the same reasons. The trial court did not find that Sharley had a purpose to harm Cooke's business. Its award of punitive damages on the wrongful-execution claim was necessarily based on the finding that the seizure of some nominal or undetermined amount of Cooke's (or his corporation's) property was with wanton and reckless disregard for ***143** Cooke's (or his corporation's) rights; but this is not synonymous with a deliberate purpose to harm the business.

"Defendant's liability may arise from improper motives or from the use of improper means." Top Service Body Shop, supra, 283 Or. at 209, 582 P.2d at 1371. The "means" employed here alleged to be a tortious interference are the acts of executing on a judgment. That is not per se improper for the simple reason that it is permitted by statute. ORS 23.040(1). The Scope of the execution was found to be improper to some nominal or undetermined degree. But that minor impropriety seems far less extreme than the conduct held not actionable in Top Service Body Shop, supra, 283 Or. at 210-12, 582 P.2d 1365. Moreover, plaintiffs have been awarded damages for that impropriety in their wrongful-execution claim; awarding additional damages for the same injury under the heading of tortious interference would appear to be double recovery.

As for the possibility of improper motives, the most that can be said is that there was conflicting evidence. Plaintiff Cooke urges that we disregard Sharley's testimony to the effect that he executed only to obtain money that he was entitled to as "self-serving and unbelievable." The question of the credibility of the testimony was for the trial court; it is not for this court.

The means of supposed interference were not improper as a matter of law. ****1194** There is substantial evidence to support the conclusion that the motives for supposed interference were not improper. Plaintiff's tortious-interference claims thus fail.

III

Plaintiffs make numerous other assignments of error which we will briefly note.

Plaintiffs complain about the form of the trial court's judgment. Citing constitutional provisions, articles and the law of other states, plaintiffs claim the ***144** trial court should have orally explained its decision on the record and/or sent a letter of explanation and/or stated more detailed findings in its judgment. We hold the form of the judgment sufficient. Had plaintiffs made a timely request for special findings pursuant to ORS 17.431, as they had the right to do, all of the problems they now complain of at great length could have been avoided.

Plaintiffs ask that we increase the trial court's award of punitive damages. However, plaintiffs cite no cases in which an Oregon appellate court has said it has authority to increase punitive damages or has increased punitive damages. We seriously doubt that such authority exists. See Or.Const., Amended Art. VII, s 3. If such authority exists, we decline to exercise it on the facts of this case.

Plaintiffs make three assignments of error addressed to evidentiary rulings of the trial court. We conclude that any error committed on the evidentiary rulings was not prejudicial.

Affirmed.

All Citations

44 Or.App. 133, 605 P.2d 1188

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-32

896 F.Supp.2d 364
United States District Court,
W.D. Pennsylvania.

STS REFILLS, LLC, Plaintiff,
v.
RIVERS PRINTING SOLUTIONS, INC., Thomas E. Rivers, and Cathy Rivers, Defendants.

Civil Action No. 3:10–CV–43.
|
Sept. 13, 2012.

Synopsis
Background: Franchisor sued franchisees, seeking to arbitrate disputes stemming from two agreements granting franchises to operate retail stores in North Carolina. Franchisor moved for summary judgment.

Holdings: The District Court, Gibson, J., held that:

venue was proper;

under North Carolina law, where contractual language restricts or prohibits assignment, any assignment made contrary to that language is ineffective and void;

genuine issues of material fact existed as to whether the franchisor, at the time of an assignment from a master franchisor, had sufficient financial resources to fulfill its obligations under the franchise agreement;

franchisees were not estopped from challenging the validity of the assignment;

franchisor's breach of contract claims fell within the scope of an arbitration provision of the second franchise agreement; and

personal guarantees of franchisee's principals accompanied the second franchise agreement.

Motion granted in part and denied in part.

Procedural Posture(s): Motion for Summary Judgment.

Attorneys and Law Firms

***366** Brian P. Litzinger, John M. Haschak, Leventry, Haschak, and Rodkey, LLC, Johnstown, PA, for Plaintiff.

Maurice A. Nernberg, Jr., Maurice A. Nernberg & Associates, Pittsburgh, PA, for Defendants.

MEMORANDUM AND ORDER OF COURT

GIBSON, District Judge.

I. SYNOPSIS
This matter comes before the Court on Plaintiff STS Refills, LLC's Motion for Summary Judgment (Doc. No. 20) pursuant to Federal Rule of Civil Procedure 56. Plaintiff asks this Court for an order compelling Rivers Printing Solutions, Inc., Thomas E. Rivers, and Cathy Rivers to arbitrate disputes related to the alleged breach of two agreements, allegedly between STS Refills, Inc., Rivers Printing Solutions, Inc., Thomas E. Rivers, and Cathy Rivers. (Doc. No. 20 at 2; Doc. No. 1 at 1.) For the reasons that follow, Plaintiff's Motion for Summary Judgment is **GRANTED IN PART AND DENIED IN PART.**

***367 II. JURISDICTION AND VENUE**
This Court has jurisdiction pursuant to 28 U.S.C. § 1332(a)(1).[1] Venue is proper in this case pursuant to 28 U.S.C. § 1391(a)(2) because a substantial part of the events giving rise to this action occurred in this district. However, in light of Plaintiff's assertion that venue is proper pursuant to 9 U.S.C. § 4 and the terms of the agreements (*see* Doc. No. 1 at 3) and Defendants' assertions that venue is improper in this district (*see* Doc. No. 7; Doc. No. 18 at 1–2), the Court finds that the issue of venue merits a brief discussion.

Plaintiff states in its complaint that venue in this Court is appropriate pursuant to 9 U.S.C. § 4. (*See* Doc. No. 1 at 3.) Section 4 of the Federal Arbitration Act (hereinafter the "FAA"), codified at 9 U.S.C. § 1 *et seq.,* has indeed been interpreted to contain a venue provision.[2] *See, e.g., Econo–Car Int'l, Inc. v. Antilles Car Rentals, Inc.,* 499 F.2d 1391, 1394 (3d Cir.1974); *Image Software, Inc. v. Reynolds & Reynolds Co.,* 459 F.3d 1044, 1052–52 (10th Cir.2006) (citing *Econo–Car Int'l,* 499 F.2d at 1394); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Lauer,* 49 F.3d 323, 327 (7th Cir.1995); *Argonaut Ins. Co. v. Century Indem. Co.,* No. 05–

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

5355, 2006 U.S. Dist. LEXIS 60765, at *8–9 (E.D.Pa. Aug. 5, 2006). While some Courts have suggested that section 4 might be a restrictive venue provision that controls over general venue statutes, *see Image Software, Inc.,* 459 F.3d at 1054, courts in this Circuit have not, *see, e.g., Econo–Car Int'l,* 499 F.2d at 1394 (noting that, because a district court may not order arbitration outside its district pursuant to the text of 9 U.S.C. § 4, a restrictive reading section 4's language permitting a party to request an order "directing that ... arbitration proceed in the manner provided for in [the arbitration] agreement" might prevent a district court from ordering arbitration even where venue is otherwise proper); *Jumara v. State Farm Ins. Co.,* 55 F.3d 873, 877–79 (3d Cir.1995); *Argonaut Ins. Co.,* 2006 U.S. Dist. LEXIS 60765, at *8–9 (relying on the United States Supreme ***368** Court's opinion in *Cortez Byrd Chips, Inc. v. Bill Harbert Constr. Co.,* 529 U.S. 193, 120 S.Ct. 1331, 146 L.Ed.2d 171 (2000) in holding that section 4 of the FAA does not foreclose the general venue statute of 28 U.S.C. § 1391). Indeed, in *Jumara v. State Farm Ins. Co.,* 55 F.3d 873, 877–79 (3d Cir.1995), the Third Circuit's decision to transfer a matter under 28 U.S.C. § 1404(a) demonstrated that a valid forum selection clause in an arbitration agreement selecting a location in a particular district as the forum for arbitration does not foreclose the possibility that venue will be proper in another judicial district. There, Plaintiffs brought an action in the Eastern District of Pennsylvania seeking to compel arbitration pursuant to an agreement that selected a county in the Middle District of Pennsylvania as the forum for arbitration. *Id.* at 875, 881. After concluding that transfer to the Middle District was the appropriate course of action, the Court inquired into the proper statutory basis for transfer. *Id.* at 877–79. The Court held that the action should be transferred pursuant to 28 U.S.C. § 1404(a), which permits a district court to transfer a civil action from one proper venue to another proper venue, rather than 28 U.S.C. § 1406(a), which permits a district court to transfer a civil action that has been brought in an improper forum to a forum where venue is proper. *Jumara,* 55 F.3d at 877–79. The Court so held because, notwithstanding the forum selection clause selecting the Middle District as the forum for arbitration, venue was also proper in the Eastern District under 28 U.S.C. § 1391. *Id.* at 878–79. *See also Lester v. Gene Express, Inc.,* No. 09–0403, 2009 WL 3757155, at *4, 2009 U.S. Dist. LEXIS 105029, at *12–13 (D.N.J. Nov. 10, 2009) (same). Thus, notwithstanding the forum selection clauses in the Agreements at issue in this case,[3] venue is proper in this district under 28 U.S.C. § 1391(a)(2) because Plaintiff is a Pennsylvania Limited Liability Company with its principal place of business in this district (*see* Doc. No. 1 at 3; Doc. No. 18 at 1) and a substantial part of the events or omissions giving rise to this claim occurred in this district.

III. FACTUAL AND PROCEDURAL BACKGROUND

On February 10, 2010, STS Refills, LLC, (hereinafter "STS"), a franchisor of master franchisor Cartridge World North America, LLC (hereinafter "Cartridge World"), brought suit in this Court to compel Defendants, Rivers Printing Solutions, Inc. (hereinafter "Rivers Printing"), Thomas E. Rivers, and Cathy Rivers, franchisees, to arbitrate disputes stemming from two contractual franchise agreements. (Doc. No. 1 at 1, 3.) Although similar in many respects, the two agreements contain different choice of law provisions and raise different legal issues, and therefore will be discussed separately in this memorandum.

The first agreement, dated February 7, 2005, was entered into by Cartridge World and Rivers Printing, a North Carolina Corporation with its principal place of business in Wilmington, North Carolina. (*See* Doc. No. 18 at 1; Doc No. 22 at 1; Doc. No. 24 at 1.) The Agreement (hereinafter the "Wilmington Agreement") granted Rivers Printing a franchise to operate a Cartridge World retail store in Wilmington, North Carolina (hereinafter the "Wilmington ***369** franchise location"). (*See* Doc. No. 22 at 1; Doc. No. 24 at 1; *see generally* Doc. No. 1–4; Doc. No. 1–5; Doc. No. 1–6.) Thomas E. Rivers and Cathy Rivers personally guaranteed the Wilmington Agreement. (Doc. No. 24 at 2.) On March 30, 2006, the Wilmington Agreement was allegedly assigned by Cartridge World to Plaintiff, STS, a Pennsylvania Limited Liability Company with its principal place of business in Altoona, Pennsylvania (*see* Doc. No. 7–3; Doc. No. 22 at 1), after which date Rivers Printing and STS engaged in business pursuant to the Wilmington Agreement (*see* Doc. No. 22 at 1; Doc. No. 24 at 1). The assignment purports to transfer the Wilmington Agreement in full, with assignee accepting all rights and agreeing to assume, perform, and observe "all of the terms, provisions and conditions that are on the part of the Assignor to be performed and observed under the terms of the Franchise Agreement...." (Doc. No. 7–3.) As further discussed below, Defendants challenge the validity of this assignment. (*See* Doc. No. 24 at 1, 3; Doc. No. 25.)

The Wilmington Agreement contains a choice of law clause and an arbitration clause. (*See* Doc. No. 1–5 at 43–50.) The choice of law clause provides, in relevant part:

> Therefore, you and we ... agree that, except with respect to the applicability of the Federal Arbitration Act, 9 U.S.C. § 1 et. seq. and the effect of federal preemption of state law by such Act, and except to the extent governed by the United States Trademark Act and other federal laws and as otherwise expressly provided in this Agreement, this Agreement and all other matters, including, but not limited to respective rights and obligations, concerning you and us, will be governed by, and construed and enforced in accordance with, the laws of North Carolina.

(Doc. No. 1–5 at 49.) The arbitration clause, in addition to providing for disputes to be resolved through ADR and arbitration, contains provisions on both the scope of the disputes to be arbitrated and the location of arbitration. (*See* Doc. No. 1–5 at 43–44.) Regarding the disputes to be arbitrated, the Agreement provides:

> Any litigation, claim, dispute, suit, action, controversy, or proceeding *of any type whatsoever* including any claim for equitable relief and/or where you are acting as a "private attorney general," suing pursuant to a statutory claim or otherwise, between or involving you and us on whatever theory and/or facts based, and whether or not arising out of this Agreement, ("Claim") will be processed in the following manner, you and we each expressly waiving all rights to *any* court proceeding, except as expressly provided below at Section 19.1 H.

(Doc. No. 1–5 at 43.) Regarding the location of arbitration, the Agreement provides:

> Any mediation/arbitration (and any appeal) will be conducted exclusively at neutral location [sic] in the county in which our then current headquarters is located, which may change from time to time, and be attended by you and us, and/or designees authorized to make binding commitments on each of our respective behalfs; provided that if any court determines that this provision is unenforceable for any reason, mediation/arbitration (and any appeal) will be conducted at a location near your unit.

(Doc. No. 1–5 at 44.)

The second agreement, dated November, 14, 2007, was entered into by STS and Rivers Printing. (*See* Doc. No. 22 at 2; Doc. No. 24 at 2.) The Agreement (hereinafter the "Belleville Agreement") granted Rivers Printing a franchise to operate a ***370** Cartridge World retail store in Belleville, North Carolina (hereinafter the "Belleville franchise location"). (*See* Doc No. 22 at 2; Doc. No. 24 at 2; *see generally* Doc. No. 1–7; Doc. No. 1–8; Doc. No. 1–9.) Plaintiff contends, but Defendants dispute, that Thomas E. Rivers and Cathy Rivers personally guaranteed the Belleville Agreement. (*See* Doc. No. 22 at 2; Doc. No. 24 at 2.) Like the Wilmington Agreement, the Belleville Agreement also contains a choice of law clause and an arbitration clause. (*See* Doc. No. 1–8 at 40–48.) The choice of law provision in the Belleville Agreement is identical to that in the Wilmington Agreement with the exception that is selects Pennsylvania law as the law to govern all matters, rights, and obligations under the Belleville Agreement. (*Compare* Doc. No. 1–8 at 47 *with* Doc. No. 1–5 at 49.) The excerpted portions of the arbitration clause of the Wilmington Agreement are identical in all material ways to that of Belleville Agreement with two exceptions. (*Compare* Doc. No. 1–5 at 43 *with* Doc. No. 1–8 at 41 *and* Doc. No. 1–5 at 44 *with* Doc. No. 1–8 at 42.) First, when addressing the disputes to be arbitrated, the emphasis beneath the words "of any type whatsoever" and "any" that appears in the Wilmington Agreement is omitted in the Belleville Agreement; and second, when addressing the location of arbitration, the Belleville Agreement replaces the words "in the county in which our then current headquarters

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

is located" that appear in the Wilmington Agreement with the words "in the county for our then-current principal business address." [4] (*Compare* Doc. No. 1–5 at 43 *with* Doc. No. 1–8 at 41 *and* Doc. No. 1–5 at 44 *with* Doc. No. 1–8 at 42.)

On April 20, 2010, Defendants moved to dismiss this action for improper venue pursuant to Federal Rule of Civil Procedure 12(b)(3) (the "Motion to Dismiss"). (Doc. No. 7.) This Court denied that motion through a Memorandum and Order dated March 29, 2011. (Doc. No. 17.) Defendants submitted an Answer entitled Answer and Affirmative Defenses to Complaint in the Nature of a Petition to Compel Arbitration (the "Answer") (Doc. No. 18) on April 12, 2011. On January 5, 2012, Plaintiff filed the instant motion for summary judgment. (Doc. No. 20.) In support of the motion, Plaintiff contemporaneously filed a brief (Doc. No. 21) and a concise statement of material facts (the "CSMF") (Doc. No. 22) with an appendix of supporting exhibits (Doc. No. 22–1; Doc. No. 22–2; Doc. No. 22–3; Doc. No. 22–4), as required by the Local Rules of the United States District Court for the Western District of Pennsylvania (the "Local Rules"). Defendants filed a Responsive Concise Statement entitled "Reply and New Matter to Concise Statement of Material Facts" (the "Responsive Concise Statement") (Doc. No. 24) on February 3, 2012, as required by Local Rule 56.C.1. In support of their Responsive Concise Statement, Defendants contemporaneously filed a Brief in Opposition to Plaintiff's Motion for Summary Judgment (Doc. No. 25) with supporting exhibits (the "Brief in Opposition"), as required by Local Rule 56.C.2–3. (Doc. No. 25–1; Doc. No. 25–2; Doc. No. 25–3.)

IV. STANDARD OF REVIEW

"Summary judgment is appropriate only where, drawing all reasonable inferences in favor of the nonmoving party, there is no genuine issue as to any material fact ... and the moving party is entitled to judgment as a matter of law." ***371** *Melrose, Inc. v. Pittsburgh,* 613 F.3d 380, 387 (3d Cir.2010) (quoting *Ruehl v. Viacom, Inc.,* 500 F.3d 375, 380 n. 6 (3d Cir.2007)); *see also Celotex Corp. v. Catrett,* 477 U.S. 317, 322, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986); Fed.R.Civ.P. 56(a). [5] Issues of fact are genuine "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986); *see also McGreevy v. Stroup,* 413 F.3d 359, 363 (3d Cir.2005). Material facts are those which will affect the outcome of the trial under governing law. *Anderson,* 477 U.S. at 248, 106 S.Ct. 2505.

The moving party bears the initial responsibility of stating the basis for its motion and identifying those portions of the record which demonstrate the absence of a genuine issue of material fact. *Celotex,* 477 U.S. at 323, 106 S.Ct. 2548. If the moving party meets this burden, the party opposing summary judgment "may not rest upon the mere allegations or denials of the ... pleading," but "must set forth specific facts showing that there is a genuine issue for trial." *Saldana v. Kmart Corp.,* 260 F.3d 228, 232 (3d Cir.2001) (internal citations omitted); *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.,* 475 U.S. 574, 587, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986); *see also Podobnik v. U.S. Postal Serv.,* 409 F.3d 584, 594 (3d Cir.2005) (noting that a party opposing summary judgment "must present more than just bare assertions, conclusory allegations or suspicions to show the existence of a genuine issue" (internal quotation marks omitted)).

V. DISCUSSION

Plaintiff contends that the Court should grant summary judgment against Defendants as to both contracts because (1) both the Wilmington Agreement and the Belleville Agreement contain an agreement to arbitrate disputes and (2) the issues in dispute are within the scope of the arbitration agreements. (*See* Doc. No. 20 at 1–2; Doc. No. 21 at 2; Doc. No. 22 at 2.) Defendants disagree. Defendants contend that Cartridge World's assignment of the Wilmington Agreement to STS contravened the terms of the Wilmington Agreement, rendering the assignment void (*see* Doc. No. 24 at 1) and therefore that STS "lacks standing to enforce the [Wilmington Agreement]," (*see* Doc. No. 24 at 3). Additionally, Defendants contend a personal guaranty of Thomas E. Rivers and Cathy Rivers did not accompany the Belleville Agreement. (Doc. No. 24 at 2.)

In response, Plaintiff alleges that this Court "specifically rejected" Defendants' argument that the assignment of the Wilmington Agreement was not effective in this Court's March 29, 2011 Memorandum and Order (Doc. No. 17) denying Defendants' Motion to Dismiss for Improper Venue (Doc. No. 7). Further, Plaintiff appears to contend that Defendants should be estopped from challenging the validity of the assignment through its assertion that Defendants did not object to the assignment at the time the Agreement was allegedly assigned and that Defendants continued to operate and conducted business with STS pursuant to the terms in the Wilmington Agreement after the alleged assignment. (*See* Doc. No. 21 at 1; Doc. No. 22 at 1.) The Court will address each of these issues in turn. Because

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

each Agreement raises different factual and legal issues, in addressing these issues, the Court will discuss the Wilmington and ***372** Belleville Agreements separately, beginning with the Wilmington Agreement.

A. The Wilmington Agreement

Prior to compelling arbitration pursuant to the FAA, a court must determine that "(1) there is an agreement to arbitrate and (2) the dispute at issue falls within the scope of that agreement." *Century Indem. Co. v. Certain Underwriters at Lloyd's,* 584 F.3d 513, 523 (3d Cir.Pa.2009). Defendants admit that the Wilmington Agreement contains an arbitration clause. (*See* Doc. No. 24 at 2). Defendants further do not specifically challenge Plaintiff's contention that the disputes at issue fall within the scope of the arbitration clause. (*See* Doc. No. 24; Doc. No. 25).[6] However, Defendants challenge a more preliminary matter; Defendants deny the existence of any agreement between STS and the Defendants relating to the Wilmington franchise location. Specifically, Defendants contend that the assignment to STS violated the terms of the Wilmington Agreement and is therefore void. (*See* Doc. No. 24 at 1; Doc. No. 25 at 2, 3.) Although Defendants assert that the assignment's failure to satisfy the terms of the Wilmington Agreement renders the assignment invalid and void (*see* Doc. No. 24 at 1; Doc. No. 25 at 2, 3), Defendants cite no caselaw for this proposition (*see* Doc. No. 25 at 3). As stated above, the parties have selected North Carolina law to govern the Wilmington Agreement. (Doc. No. 1–5 at 49.) Therefore, before inquiring into the existence of a genuine dispute as to a material fact with respect to the existence of an agreement between STS and Defendants, as a preliminary matter, this Court must determine the effect of an assignment that occurs in violation of the terms of a written agreement under North Carolina law.

Courts have taken differing approaches to anti-assignment clauses. Depending on the language used, courts have found that contractual clauses restricting or prohibiting assignment either render the assignment void or result in a valid assignment and simply entitle the obligor to damages for breach of contract. *Dean v. Symetra Assigned Benefits Serv. Co. (In re Application for Approval of Structured Settlement Payment Rights),* 133 Wash.App. 350, 136 P.3d 765, 775 (2006) (discussing different approaches used in addressing anti-assignment clauses in structured settlement agreements, applying North Carolina law). For example, the Restatement (Second) of Contracts § 322 (1981) provides:

> (1) Unless the circumstances indicate the contrary, a contract term prohibiting assignment of "the contract" bars only the delegation to an assignee of the performance by the assignor of a duty or condition.
>
> (2) A contract term prohibiting assignment of rights under the contract, unless a different intention is manifested,
>
> ...
>
> (b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective....

While under the latter approach the assignment to STS would be effective and, ***373** irrespective of a contractual term restricting or prohibiting assignment, as a party to the agreement STS could enforce an arbitration agreement contained therein, *cf. CTF Hotel Holdings v. Marriott Int'l,* 381 F.3d 131, 137 (3d Cir.2004); *Collie v. Wehr Dissolution Corp.,* 345 F.Supp.2d 555, 561 (M.D.N.C.2004) (applying North Carolina law to the arbitration agreement), under the former approach STS may be barred from enforcing the arbitration clause absent a common law principle creating an exception to the general rule that "one who is not a party to an arbitration agreement lacks standing to compel arbitration," *Collie,* 345 F.Supp.2d at 561; *see also Cost Bros. Inc. v. Travelers Indem. Co.,* 760 F.2d 58, 60 (3d Cir.1985).

Under North Carolina Law, contract rights are assignable unless prohibited by statute, public policy or the terms of the contract, or the contract is one for personal services or is entered into out of personal confidence in the other party to the contract. *Kraft Foodservice v. Hardee,* 340 N.C. 344, 457 S.E.2d 596, 598 (1995). "Assignments are governed by the general principals of contract law, and 'provisions in bilateral contracts that forbid or restrict assignment of the contract without the consent of the obligor are generally valid and enforceable.' " *Parkersmith Props. v. Johnson,* 136 N.C.App. 626, 525 S.E.2d 491, 495 (2000) (quoting 6 Am.Jur.2d *Assignments* § 21 (1999)) (some citations omitted). Neither STS nor this Court's survey of relevant caselaw has shown that North Carolina has adopted the Restatement approach. At least one state appellate court applying North Carolina law has come to the same conclusion. *See Dean,* 136 P.3d at 774–76. In so concluding, that Court held that "anti-assignment clauses in contracts are enforceable in North Carolina at the insistence of an obligor, and that an assignment without the obligor's consent is ineffective." *Id.* at 776. This Court agrees and finds no difference between a contractual

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

prohibition of assignment and a contractual restriction on assignment. Therefore, the Court concludes that, under North Carolina law, where contractual language restricts or prohibits assignment, any assignment made contrary to that language is ineffective and void.

The Wilmington Agreement generally permits transfer of the Agreement by Cartridge World with the narrow restriction that the transferee must have sufficient resources to fulfill its obligations. (*See* Doc. No. 1–5 at 27; Doc. No. 25 at 2.) It provides, in relevant part:

> This Agreement, and any or all of our rights and/or obligations under it, are fully transferable by us in our Business Judgment, in whole or in part, without your consent, provided that any such transferee shall appear at the time of the transfer to have financial resources reasonably appropriate to fulfill its obligations under this Agreement.

(Doc. No. 1–5 at 27.) Defendants contend that, at the time Cartridge World assigned the Wilmington Agreement to STS, STS did not have "sufficient financial resources to fulfill its obligations under the agreement ...." (Doc. No. 25 at 3.) Because this Court finds that assignments made in violation of a contractual term restricting assignment renders the assignment void under North Carolina law, whether Plaintiff may enforce the arbitration clause as a party to the Wilmington Agreement under 9 U.S.C. § 4,[7] turns on the validity of the ***374** assignment. This fact will affect the outcome of the proceedings. Therefore this fact is material.

Defendants, in support of their claim that STS did not have the financial resources necessary to fulfill their obligations under the Wilmington Agreement cite to materials purporting to demonstrate that at and around the time of the alleged assignment STS had negative equity (*see* Doc. No. 25–1; Doc. No. 25–3) as well as to an account statement displaying several overdraft charges (*see* Doc. No. 25–2). After drawing all reasonable inferences in favor of the Defendants as the nonmoving party, the Court finds that with respect to the validity of the assignment under the Wilmington Agreement "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *See Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986). Therefore, the dispute as to whether the assignment of the Wilmington Agreement to STS was valid and effective is also genuine, and a genuine dispute as to a material fact exists.

Finding a genuine dispute as to a material fact, the Court next addresses whether, despite this dispute, Defendants are estopped from challenging the validity of the assignment. Judicial estoppel is an equitable doctrine that prevents a party from asserting inconsistent claims or arguments in different legal proceedings or different phases of litigation. *See Mintze v. Am. Fin. Servs., Inc. (In re Mintze),* 434 F.3d 222, 232 (3d Cir.2006); *Pegram v. Herdrich,* 530 U.S. 211, 228 n. 8, 120 S.Ct. 2143, 147 L.Ed.2d 164 (2000). "Its purpose is to protect the judicial process by preventing parties from 'deliberately changing positions according to the exigencies of the moment.' " *In re Armstrong World Indus. Inc.,* 432 F.3d 507, 517 (3d Cir.2005) (quoting *New Hampshire v. Maine,* 532 U.S. 742, 750, 121 S.Ct. 1808, 149 L.Ed.2d 968 (2001)). The Third Circuit has held that "[t]hree requirements must be met before a district court may properly apply judicial estoppel." *Montrose Med. Group Participating Sav. Plan v. Bulger,* 243 F.3d 773, 779–80 (3d Cir.2001).

> First, the party to be estopped must have taken two positions that are irreconcilably inconsistent. Second, judicial estoppel is unwarranted unless the party changed his or her position in bad faith—i.e., with intent to play fast and loose with the court. Finally, a district court may not employ judicial estoppel unless it is tailored to address the harm identified and no lesser sanction would adequately remedy the damage done by the litigant's misconduct.

Id. at 779–80 (quotation marks and citations omitted).

Plaintiff does not cite to, nor is this Court aware of, any prior legal proceedings related to this dispute. Therefore, Plaintiff has failed to show that Defendants have asserted inconsistent claims in different legal proceedings. Defendants' challenge to the validity of the assignment of the Wilmington Agreement to STS is not limited to Defendants' Responsive Concise Statement and Brief in Opposition. Defendants raised

this issue in their Answer and Motion to Dismiss. (*See* Doc. No. 18 at 5; Doc. No. 7 at 2, n. 1, 2–3.) Thus, Defendants also have not asserted inconsistent claims in different phases of this litigation. Additionally, Defendants assert that they obtained information demonstrating STS' financial difficulties through discovery. (Doc. No. 25 at 2.) This Court finds that Defendants' doing business with STS pursuant to an alleged ***375** assignment is not "irreconcilably inconsistent" with later challenging the validity of that assignment following the disclosure of financial information during discovery. Furthermore, there is insufficient evidence before the Court to conclude that any change in Defendants' position was done in bad faith. Therefore, the Court concludes that Defendants are not estopped from challenging the validity of the assignment.

Finally, the Court briefly addresses Plaintiff's assertion that this Court found that the assignment of the Wilmington Agreement was valid in its March 29, 2011 Memorandum and Order. (*See* Doc. No. 22 at 2 (citing Doc. No. 17).) In ruling on Defendants' Motion to Dismiss (Doc. No. 7) this Court stated that "On March 30, 2006, Carolina Cartridges, Inc. assigned its franchise agreements to STS Refills, LLC ..." and rejected Defendants' assertion that the assignment was invalid (Doc. No. 17 at 3, 4). In so doing, the Court did not inquire into or render an opinion on the validity of the alleged assignment. Rather, the Court stated the facts after accepting as true the allegations contained in Plaintiff's complaint. *See Phillips v. County of Allegheny,* 515 F.3d 224, 231 (3d Cir.2008) (stating standard for deciding a motion to dismiss pursuant to Fed R. Civ. Pro. 12(b)(3)). Therefore, Plaintiff's assertion that this issue has already been decided by this Court is incorrect.

In conclusion, the Court finds that there is a genuine dispute as to a material fact that is not barred by judicial estoppel and that has not previously been decided by this Court. Therefore, Plaintiff's motion for summary judgment with respect to the Wilmington Agreement is denied.

B. The Belleville Agreement

Finding a genuine dispute as to a material fact exists with respect to the Wilmington Agreement, this Court next turns its attention to the Belleville Agreement. Defendants do not challenge the existence of an agreement between Rivers Printing and STS with respect to the Belleville franchise location. (*See* Doc. No. 24 at 2). Thus, the Court begins with the legal standard for issuing an order compelling arbitration. "Before compelling a party to arbitrate pursuant to the FAA, a court must determine that (1) there is an agreement to arbitrate and (2) the dispute at issue falls within the scope of that agreement." *Century Indem. Co. v. Certain Underwriters at Lloyd's,* 584 F.3d 513, 523 (3d Cir.2009). "Absent language in the parties' agreement clearly providing otherwise, the arbitrability of a dispute is a question of law for the court to determine." *Gedid v. Huntington Nat'l Bank,* No. 11–1000, 2012 WL 691637, at *4, 2012 U.S. Dist. LEXIS 27715, at *11 (E.D.Pa. Feb. 10, 2012) (citing *U.S. Small Bus. Admin. v. Chimicles,* 447 F.3d 207, 209 (3d Cir.2006); *Gen. Elec. Co. v. Deutz AG,* 270 F.3d 144, 154 (3d Cir.2001)). "For a court to compel arbitration, it initially must find that there is a valid agreement to arbitrate because the basis for contractual arbitration is consent, not coercion." *Century Indem. Co.,* 584 F.3d at 523 (3d Cir.2009). Furthermore, because parties may agree to arbitrate some, but not all, disputes arising out of a contract or relationship, even where an agreement to arbitrate exits a court must also find that the parties have agreed to arbitrate the dispute or disputes in issue. *Id.*

When a valid agreement to arbitrate exists, "the determination of whether 'a particular dispute is within the class of those disputes governed by the arbitration clause ... is a matter of federal law.' " *Id.* at 524 (quoting *China Minmetals Materials Imp. & Exp. Co. v. Chi Mei Corp.,* 334 F.3d 274, 290 (3d Cir.2003)). "When a dispute consists of several claims, the ***376** court must determine on an issue-by-issue basis whether a party bears a duty to arbitrate." *Trippe Mfg. Co. v. Niles Audio Corp.,* 401 F.3d 529, 532 (3d Cir.2005). "In determining whether the particular dispute falls within a valid arbitration agreement's scope, 'there is a presumption of arbitrability[:] an order to arbitrate the particular grievance should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute.' " *Century Indem. Co.,* 584 F.3d at 524 (quoting *AT & T Techs., Inc. v. Commc'ns. Workers of Am.,* 475 U.S. 643, 650, 106 S.Ct. 1415, 89 L.Ed.2d 648 (1986)).

Similar to the Wilmington Agreement, Defendants admit that the Belleville Agreement contains an arbitration clause. (*See* Doc. No. 24 at 2.) Therefore, the existence of an agreement to arbitrate is not in question and the Court turns to the question of whether the disputes at issue fall within the scope of the arbitration agreement. Plaintiff describes the nature of the disputes in its Complaint and Memorandum In Support of Motion for Summary Judgment. (*See* Doc. No. 1 at 5–6; Doc. No. 21 at 2.) Specifically, Plaintiff alleges that Defendants committed the following breaches of contract: (1) Defendants removed all Cartridge World

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

signage, logos, uniforms, and other identifying items from the Belleville franchise location but continued to substantially operate as a Cartridge World store, (2) Defendants continued to utilize equipment and proprietary information provided by STS and/or Cartridge World after removing information identifying the Belleville franchise location as a Cartridge World store, (3) Defendants stopped remitting franchise fees to STS as required by the Belleville Agreement and (4) Defendants continued to use the Cartridge World brand or trademark in telephone directories and advertisements after having removed information identifying the Belleville franchise location as a Cartridge World store. (Doc. No. 1 at 5–6.) Plaintiff further sets forth the text of the Belleville Agreement regarding the scope of the disputes to be arbitrated in its CSMF with a citation to the record, as required by Local Rule 56.B.1. (*See* Doc. No. 22 at 2.)

Defendants, in their Responsive Concise Statement, state that the Agreement "is a thing which speaks for itself" and deny any attempt to interpret, construe, or modify the terms of the document. (Doc. No. 24 at 2.) However, beyond this, Defendants do not advance any specific arguments contending that or explaining how disputes between the parties fall outside the scope of the arbitration agreement, which, by its terms broadly includes "any litigation, claim, dispute, suit, action, controversy, or proceeding of any type whatsoever ... between or involving you and us on whatever theory and/or facts based, and whether or not arising out of this Agreement ...."[8] (Doc. No. 1–8 at 41). Indeed, the "New Matter" in Defendants' Responsive Concise Statement is limited to issues related to the Wilmington Agreement. (*See* Doc. No. 24 at 3.) Each dispute identified by Plaintiff is a dispute between STS and Defendants relating to the operation of the Belleville franchise location, thereby satisfying the clause's requirement that the dispute be "between or involving" STS and Defendants. Further, although the arbitration clause does not limit its breadth to disputes arising out of the Belleville Agreement, the type of disputes at issue appear to be of the precise nature that the clause appears to be designed to address: disputes between the parties related to the ***377** operation of a franchise pursuant to the franchise agreement. Therefore, in light of the arbitration clause's breadth, the fact that Defendants have not advanced any arguments as to whether or why the disputes at issue fall outside the scope of the arbitration clause, and the "presumption of arbitrability," *see Century Indem. Co.,* 584 F.3d at 524, Defendants have failed to demonstrate the existence of a genuine dispute as to the scope of the arbitration clause.

Defendants do challenge Plaintiff's assertion that personal guarantees of Thomas E. Rivers and Cathy Rivers accompanied the Belleville Agreement. (*See* Doc. No. 24 at 2.) Plaintiff, in support of its assertion, cites to pages 53–54 of Exhibit 2 to the Complaint (*see* Doc. No. 22 at 2), as required by Local Rule 56.B.1, which consist of an exhibit to the Belleville Agreement (hereinafter the "Belleville Exhibit") entitled "Continuing Personal Guarantee" (*see* Doc. No. 1–8 at 53–54). The "Continuing Personal Guarantee" is signed by "Tom Rivers" and "Cathy Rivers." (Doc. No. 1–8 at 54). A comparison between the text in the purported personal guarantee of the Belleville Agreement and the text of the corresponding exhibit in the Wilmington Agreement entitled "Owners Guarantee and Assumption of Corporate Franchisee's Obligations" (Doc. No. 1–5 at 54–55), which Defendants admit constitutes a personal guarantee of the Wilmington Agreement by Thomas E. Rivers and Cathy Rivers, (*see* Doc. No. 24 at 2) reveals only limited changes in phrasing. Defendants have not asserted that any of these changes affect the substance of the Belleville Exhibit nor have they explained how any of these changes may affect the substance of the Belleville Exhibit. Additionally, although Defendants have supplemented their denial of Plaintiff's assertion that a personal guarantee accompanied the Belleville Agreement with a citation to a pleading, (specifically, the Answer) (*see* Doc. No. 24 at 2) as required by Local Rule 56.C.1.b, Defendants have failed to set forth a basis for the denial in both their Responsive Concise Statement and the Answer to which they cite (*see* Doc. No. 24 at 2; Doc. No. 18 at 3), as is also required by Local Rule 56.C.1.b. Because a party opposing summary judgment must set forth more than a mere denial of the pleading to create a genuine issue as to any material fact, *Saldana v. Kmart Corp.,* 260 F.3d 228, 232 (3d Cir.2001); *see also* Local Rule 56.C.1.b., the Court finds Defendants have also failed to demonstrate the existence of a genuine dispute as to the existence of a personal guarantee of the Belleville Agreement by Thomas E. Rivers and Cathy Rivers. Therefore, Defendants have failed to demonstrate that a genuine dispute as to an issue of material fact exists with respect to the Belleville Agreement and Plaintiff's motion for summary judgment with respect to the Belleville Agreement is granted.

VI. CONCLUSION

For the reasons stated above, Defendants have demonstrated that a genuine dispute of material fact exists as to whether the assignment of the Wilmington Agreement to STS was valid and effective, and therefore whether Plaintiff may

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

enforce the arbitration clause of the Wilmington Agreement under 9 U.S.C. § 4. However, Defendants have failed to demonstrate the existence of a genuine dispute as to a material fact with respect to the scope of the arbitration clause in the Belleville Agreement or the existence of a personal guarantee of the Belleville Agreement by Thomas E. Rivers and Cathy Rivers. Accordingly, the Court will **DENY** Plaintiff's Motion for Summary Judgment with respect to the Wilmington Agreement and **GRANT** Plaintiff's Motion ***378** for Summary Judgment with respect to the Belleville Agreement. An appropriate order follows.

ORDER

AND NOW, this 13th day of September, 2012, in accordance with the Memorandum, **IT IS HEREBY ORDERED** that the Motion for Summary Judgment (Doc. No. 20) filed by Plaintiff STS Refills, LLC is **GRANTED IN PART AND DENIED IN PART.** STS Refills, LLC is directed to file a demand for arbitration for disputes related to the Belleville Agreement with Franchise Arbitration and Mediation Services (FAM) within ten (10) days hereof. The parties are ORDERED to pay the costs of such arbitration as provided by FAM Arbitration Guidelines, effective May 17, 2011.

All Citations

896 F.Supp.2d 364

Footnotes

1 Defendants acknowledge that complete diversity exists, however, Defendants deny that the amount in controversy requirement is met. Although Plaintiff's requested relief is limited to an order compelling arbitration, "the amount in controversy in a petition to compel arbitration ... is determined by the underlying cause of action that would be arbitrated." *Jumara v. State Farm Ins. Co.,* 55 F.3d 873, 877 (3d Cir.1995). Because Plaintiff has plead that the amount in controversy in the underlying cause of action will exceed $75,000 (Doc. No. 1 at 3) and it is not clear "to a legal certainty that the claim is really for less than the jurisdictional amount," *Horton v. Liberty Mut. Ins. Co.,* 367 U.S. 348, 353, 81 S.Ct. 1570, 6 L.Ed.2d 890 (1961), the amount in controversy requirement is met and diversity jurisdiction exists.

2 9 U.S.C. § 4 states:

> A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28 [28 USCS §§ 1 et seq.], in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement ... The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed ....

The second portion of this statutory provision, which states that arbitration "shall be within the district in which the petition for an order directing such arbitration is filed" is relevant to venue.

3 Previously, this Court found that venue was proper in this forum pursuant to the terms of the arbitration agreement. (*See* Doc. No. 17 at 4.) Upon further consideration, and without revisiting the question of venue pursuant to the terms of the arbitration agreement, the Court now finds that 28 U.S.C. § 1391(a)(2) is a more appropriate ground upon which to hold that venue is proper in the Western District of Pennsylvania.

4 It is noted that both STS's principal business address and headquarters are located in Altoona, Blair County, Pennsylvania. (*See* Doc. No. 1 at 2; Doc. No. 9 at 3.)

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

5 Rule 56 was revised in 2010. The standard previously set forth in subsection (c) is now codified as subsection (a). The language of this subsection is unchanged, except for "one word—genuine 'issue' bec [ame] genuine 'dispute.' " Fed.R.Civ.P. 56 advisory committee's note, 2010 amend.

6 Defendants deny any attempt on behalf of Plaintiff to interpret, construe, or modify the terms of the arbitration clause. However, as discussed more thoroughly with respect to the Belleville Agreement, Defendants do not advance any specific arguments contending or explaining why the disputes at issue fall outside the scope of the arbitration clause in the Wilmington Agreement. For a further discussion regarding this matter, see section V.B below, as the discussion therein relating to the Belleville agreement is also true with respect to the Wilmington Agreement.

7 Title 9 U.S.C. section 4 permits "[a] *party* aggrieved" by another's alleged failure, neglect, or refusal to arbitrate pursuant to an agreement that provides for arbitration to petition a United States district court for an order directing arbitration. (Emphasis added.)

8 See Section III above for the full text of this clause of the Belleville Agreement.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-33

KeyCite Yellow Flag - Negative Treatment
Declined to Extend by Texas Spine & Joint Hospital, Ltd. v. Blue Cross and Blue Shield of Texas, a Division of Health Care Service Corporation, E.D.Tex., May 28, 2015

KeyCite Overruling Risk - Negative Treatment
Overruling Risk Illinois Tool Works Inc. v. Independent Ink, Inc., U.S., March 1, 2006

81 S.Ct. 623
Supreme Court of the United States

TAMPA ELECTRIC COMPANY, Petitioner,
v.
NASHVILLE COAL COMPANY et al.

No. 87.
|
Argued Dec. 15, 1960.
|
Decided Feb. 27, 1961.

Synopsis
Utility's suit for declaration that its requirements contract with coal company was valid and for enforcement according to its terms. The United States District Court for the Middle District of Tennessee, Nashville Division, 168 F.Supp. 456, rendered judgment adverse to the utility and it appealed. The United States Court of Appeals for the Sixth Circuit, 276 F.2d 766, affirmed and the Supreme Court granted certiorari. The Supreme Court, Mr. Justice Clark, held requirements contract between public utility and coal mining company covering all coal to be used by utility at a specified station for 20 years and pre-empting less than 1% of total relevant coal market did not substantially foreclose competition in relevant coal market, and contract did not violate Clayton Act provision proscribing certain sales agreements prohibiting use of competitor's goods.

Reversed and remanded to District Court for further proceedings.

Mr. Justice Black and Mr. Justice Douglas dissented.

Attorneys and Law Firms

****625** Mr. ***321** William C. Chanler, New York City, for petitioner.

Mr. Abe Fortas, Washington, D.C., for respondents.

Opinion

Mr. Justice CLARK delivered the opinion of the Court.

We granted certiorari to review a declaratory judgment holding illegal under s 3 of the Clayton Act [1] a requirements contract between the parties providing for the purchase by petitioner of all the coal it would require as boiler fuel at its Gannon Station in Tampa, Florida, over a 20-year period. 363 U.S. 836, 80 S.Ct. 1612, 4 L.Ed.2d 1723. Both the District court, 168 F.Supp. 456, and the Court of Appeals, 276 F.2d 766, Judge Weick dissenting, agreed with respondents that the contract fell within the proscription of s 3 and therefore was illegal and unenforceable. We cannot agree that the contract suffers the claimed anti-trust illegality [2] and, therefore, do not find it necessary to ***322** consider respondents' additional argument that such illegality is a defense to the action and a bar to enforceability.

The Facts.

Petitioner Tampa Electric Company is a public utility located in Tampa, Florida. It produces and sells electric energy to a service area, including the city, extending from Tampa Bay eastward 60 miles to the center of the State, and some 30 miles in width. As of 1954 petitioner operated two electrical generating plants comprising a total of 11 individual generating units, all of which consumed oil in their burners. In 1955 Tampa Electric decided to expand its facilities by the construction of an additional generating plant to be comprised ultimately of six generating units, and to be known as the 'Francis J. Gannon Station.' Although every electrical generating plant in peninsular Florida burned oil at that time, Tampa Electric decided to try coal as boiler fuel in the first two units constructed at the Gannon Station. Accordingly, it contracted with the respondents [3] to furnish the expected coal requirements for the units. The agreement, dated May 23, 1955, embraced Tampa Electric's 'total requirements of fuel * * * for the operation of its first two units to be installed at the Gannon Station * * * not less than 225,000 tons of coal per unit per year,' for a period of 20 years. The contract further provided that 'if during the first 10 years of the term * * * the Buyer constructs additional units (at Gannon) in which coal is used as the fuel, it shall give the Seller notice thereof two years prior to the completion of such unit or units and upon completion of same the fuel requirements thereof shall be added to this contract.' It was understood and agreed, however, that 'the Buyer has the option to be exercised two

WESTLAW © 2020 Thomson Reuters. No claim to original U.S. Government Works.

years prior ***323** to completion of said unit or units of determining whether coal or some other fuel ****626** shall be used in same.' Tampa Electric had the further option of reducing, up to 15%, the amount of its coal purchases covered by the contract after giving six months' notice of an intention to use as fuel a by-product of any of its local customers. The minimum price was set at $6.40 per ton delivered, subject to an escalation clause based on labor cost and other factors. Deliveries were originally expected to begin in March 1957, for the first unit, and for the second unit at the completion of its construction.

In April 1957, soon before the first coal was actually to be delivered and after Tampa Electric, in order to equip its first two Gannon units for the use of coal, had expended some $3,000,000 more than the cost of constructing oil-burning units, and after respondents had expended approximately $7,500,000 readying themselves to perform the contract, the latter advised petitioner that the contract was illegal under the antitrust laws, would therefore not be performed, and no coal would be delivered. This turn of events required Tampa Electric to look elsewhere for its coal requirements. The first unit at Gannon began operating August 1, 1957, using coal purchased on a temporary basis, but on December 23, 1957, a purchase order contract for the total coal requirements of the Gannon Station was made with Love and Amos Coal Company. It was for an indefinite period cancellable on 12 months' notice by either party, or immediately upon tender of performance by respondents under the contract sued upon here. The maximun price was $8.80 per ton, depending upon the freight rate. In its purchase order to the Love and Amos Company, Tampa estimated that its requirements at the Gannon Station would be 350,000 tons in 1958; 700,000 tons in 1959 and 1960; 1,000,000 tons in 1961; and would increase thereafter, as required, to 'about 2,250,000 tons per year.' The second unit at Gannon ***324** Station commenced operation 14 months after the first, i.e., October 1958. Construction of a third unit, the coal for which was to have been provided under the original contract, was also begun.

The record indicates that the total consumption of coal in peninsular Florida, as of 1958, aside from Gannon Station, was approximately 700,000 tons annually. It further shows that there were some 700 coal suppliers in the producing area where respondents operated, and that Tampa Electric's anticipated maximum requirements at Gannon Station, i.e., 2,250 tons annually, would approximate 1% of the total coal of the same type produced and marketed from respondents' producing area.

Petitioner brought this suit in the District Court pursuant to 28 U.S.C. s 2201, 28 U.S.C.A. s 2201, for a declaration that its contract with respondents was valid, and for enforcement according to its terms. In addition to its Clayton Act defense, respondents contended that the contract violated both ss 1 and 2 of the Sherman Act which, it claimed, likewise precluded its enforcement. The District Court, however, granted respondents' motion for summary judgment on the sole ground that the undisputed facts, recited above, showed the contract to be a violation of s 3 of the Clayton Act. The Court of Appeals agreed. Neither court found it necessary to consider the applicability of the Sherman Act.

Decisions of District Court and Court of Appeals.

Both courts admitted that the contract 'does not expressly contain the 'condition'' (276 F.2d 771) that Tampa Electric would not use or deal in the coal of respondents' competitors. Nonetheless, they reasoned, the 'total requirements' provision had the same practical effect, for it prevented Tampa Electric for a period of 20 years from buying coal from any other source for use at that station. Each court cast aside as 'irrelevant' arguments citing the ***325** use of oil as boiler fuel be Tampa Electric at its other stations, and by other utilities in peninsular ****627** Florida, because oil was not in fact used at Gannon Station, and the possibility of exercise by Tampa Electric of the option reserved to it to build oil-burning units at Gannon was too remote. Found to be equally remote was the possibility of Tampa's conversion of existing oil-burning units at its other stations to the use of coal which would not be covered by the contract with respondents. It followed, both courts found, that the 'line of commerce' (168 F.Supp. 460) on which the restraint was to be tested was coal —not boiler fuels. Both courts compared the estimated coal tonnage as to which the contract pre-empted competition for 20 years, namely, 1,000,000 tons a year by 1961, with the previous annual consumption of peninsular Florida, 700,000 tons. Emphasizing that fact as well as the contract value of the coal covered by the 20-year term, i.e., $128,000,000, they held that such volume was not 'insignificant or insubstantial' and that the effect of the contract would 'be to substantially lessen competition,' in violation of the Act. Both courts were of the opinion that in view of the executory nature of the contract, judicial enforcement of any portion of it could not be granted without directing a violation of the Act itself, and enforcement was, therefore, denied. [4]

Application of s 3 of the Clayton Act.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

In the almost half century since Congress adopted the Clayton Act, this Court has been called upon 10 times, [5] including the present, to pass upon questions arising under s 3. Standard Fashion Co. v. Magrane-Houston Co., 1922, 258 U.S. 346, at page 356, 42 S.Ct. 360, at page 362, 66 L.Ed. 653, the first of the cases, held that ***326** the Act 'sought to reach the agreements embraced within its sphere in their incipiency, and in the section under consideration to determine their legality by specific tests of its own * * *.' In sum, it was declared, s 3 condemned sales or agreements 'where the effect of such sale or contract * * * would under the circumstances disclosed probably lessen competition, or create an actual tendency to monopoly.' 258 U.S. at pages 356—357, 42 S.Ct. at page 362. This was not to say, the Court emphasized, that the Act was intended to reach every 'remote lessening' of competition—only those which were substantial—but the Court did not draw the line where 'remote' ended and 'substantial' began. There in evidence, however, was the fact that the activities of two-fifths of the Nation's 52,000 pattern agencies were affected by the challenged device. Then, one week later, followed United Shoe Machinery Corp. v. United States, 1922, 258 U.S. 451, 42 S.Ct. 363, 66 L.Ed. 708, which held that even though a contract does 'not contain specific agreements not to use the (goods) of a competitor,' if 'the practical effect * * * is to prevent such use,' it comes within the condition of the section as to exclusivity. 258 U.S. at page 457, 42 S.Ct. at page 365. The Court also held, as it had in Standard Fashion, supra, that a finding of domination of the relevant market by the lessor or seller was sufficient to support the inference that competition had or would be substantially lessened by the contracts involved there. As of that time it seemed clear that if 'the practical effect' of the contract was to prevent a lessee or buyer from using the products of a competitor of the lessor or seller and the contract would thereby probably substantially lessen competition in a line of commerce, it was proscribed. A quarter of a century later, in International Salt Co. v. United States, 1947, 332 U.S. 392, 68 S.Ct. 12, 92 L.Ed. 20, the Court held, at least in tying cases, that the necessity of direct proof of the economic impact of such a contract was not necessary where it was established that 'the volume of business ***327** affected' was not 'insignificant or insubstantial' and that the effect was ****628** 'to foreclose competitors from any substantial market.' 332 U.S. at page 396, 68 S.Ct. at page 15. It was only two years later, in Standard Oil Co. v. United States, 1949, 337 U.S. 293, 69 S.Ct. 1051, 93 L.Ed. 1371, that the Court again considered s 3 and its application to exclusive supply or, as they are commonly known, requirements contracts. It held that such contracts are proscribed by s 3 if their practical effect is to prevent lessees or purchasers from using or dealing in the goods, etc., of a competitor or competitors of the lessor or seller and thereby 'competition has been foreclosed in a substantial share of the line of commerce affected.' 337 U.S. at page 314, 69 S.Ct. at page 1602.

In practical application, even though a contract is found to be an exclusive-dealing arrangement, it does not violate the section unless the court believes it probable that performance of the contract will foreclose competition in a substantial share of the line of commerce affected. Following the guidelines of earlier decisions, certain considerations must be taken. First, the line of commerce, i.e., the type of goods, wares, or merchandise, etc., involved must be determined, where it is in controversy, on the basis of the facts peculiar to the case. [6] Second, the area of effective competition in the known line of commerce must be charted by careful selection of the market area in which the seller operates, and to which the purchaser can practicably turn for supplies. In short, the threatened foreclosure of competition must be in relation to the market affected. As was said in Standard Oil Co. v. United States, supra:

'It is clear, of course, that the 'line of commerce' affected need not be nationwide, at least where the purchasers cannot, as a practical matter, turn to suppliers outside their own area. Although the effect on ***328** competition will be quantitatively the same if a given volume of the industry's business is assumed to be covered, whether or not the affected sources of supply are those of the industry as a whole or only those of a particular region, a purely quantitative measure of this effect is inadequate because the narrower the area of competition, the greater the comparative effect on the area's competitors. Since it is the preservation of competition which is at stake, the significant proportion of coverage is that within the area of effective competition.' 337 U.S. at page 299, note 5, 69 S.Ct. at page 1055.

In the Standard Oil case, the area of effective competition—the relevant market—was found to be where the seller and some 75 of its competitors sold petroleum products. Conveniently identified as the Western Area, it included Arizona, California, Idaho, Nevada, Oregon, Utah and Washington. Similarly, in United States v. Columbia Steel Co., 1948, 334 U.S. 495, 68 S.Ct. 1107, 92 L.Ed. 1533, a s 1 Sherman Act case, this Court decided the relevant market to be the competitive area in which Consolidated marketed its products, i.e., 11 Western States. The Court found Consolidated's share of the nationwide market for the relevant line of commerce, rolled steel products, to be less

than 1/2 of 1%, an 'insignificant fraction of the total market,' 334 U.S. at page 508, 68 S.Ct. at page 1114; and its share of the more narrow but only relevant market, 3%, was described as 'a small part,' 334 U.S. at page 511, 68 S.Ct. at page 1116, not sufficient to injure any competitor of United States Steel in that area or elsewhere.

Third, and last, the competition foreclosed by the contract must be found to constitute a substantial share of the relevant market. That is to say, the opportunities for other traders to enter into or remain in that market must be significantly limited as was pointed out ****629** in Standard Oil Co. v. United States, supra. There the impact of the requirements contracts was studied in the setting of the large number of gasoline stations—5,937 or ***329** 16% of the retail outlets in the relevant market—and the large number of contracts, over 8,000, together with the great volume of products involved. This combination dictated a finding that 'Standard's use of the contracts (created) just such a potential clog on competition as it was the purpose of s 3 to remove' where, as there, the affected proportion of retail sales was substantial. 337 U.S. at page 314, 69 S.Ct. at page 1062. As we noted above, in United States v. Columbia Steel Co., supra, substantiality was judged on a comparative basis, i.e., Consolidated's use of rolled steel was 'a small part' when weighed against the total volume of that product in the relevant market.

To determine substantiality in a given case, it is necessary to weigh the probable effect of the contract on the relevant area of effective competition, taking into account the relative strength of the parties, the proportionate volume of commerce involved in relation to the total volume of commerce in the relevant market area, and the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein. It follows that a mere showing that the contract itself involves a substantial number of dollars is ordinarily of little consequence.

The Application of s 3 Here.

In applying these considerations to the facts of the case before us, it appears clear that both the Court of Appeals and the District Court have not given the required effect to a controlling factor in the case—the relevant competitive market area. This omission, by itself, requires reversal, for, as we have pointed out, the relevant market is the prime factor in relation to which the ultimate question, whether the contract forecloses competition in a substantial share of the line of commerce involved, must be decided. For the purposes of this case, therefore, we need not decide two threshold questions pressed by Tampa ***330** Electric. They are whether the contract in fact satisfies the initial requirement of s 3, i.e., whether it is truly an exclusive-dealing one, and, secondly, whether the line of commerce is boiler fuels, including coal, oil and gas, rather than coal alone.[7] We, therefore, for the purposes of this case, assume, but do not decide, that the contract is an exclusive-dealing arrangement within the compass of s 3, and that the line of commerce is bituminous coal.

Relevant Market of Effective Competition.

Neither the Court of Appeals nor the District Court considered in detail the question of the relevant market. They do seem, however, to have been satisfied with inquiring only as to competition within 'Peninsular Florida.' It was noted that the total consumption of peninsular Florida was 700,000 tons of coal per year, about equal to the estimated 1959 requirements of Tampa Electric. It was also pointed out that coal accounted for less than 6% of the fuel consumed in the entire State.[8] The District ****630** Court concluded that though the respondents were only one of 700 coal producers who could serve the same market, peninsular Florida, the contract for a period of 20 years excluded competitors from a substantial ***331** amount of trade. Respondents contend that the coal tonnage covered by the contract must be weighed against either the total consumption of coal in peninsular Florida, or all of Florida, or the Bituminous Coal Act area comprising peninsular Florida and the Georgia 'finger,' or, at most, all of Florida and Georgia. If the latter area were considered the relevant market, Tampa Electric's proposed requirements would be 18% of the tonnage sold therein. Tampa Electric says that both courts and respondents are in error, because the '700 coal producers who could serve' it, as recognized by the trial court and admitted by respondents, operated in the Appalachian coal area and that its contract requirements were less than 1% of the total marketed production of these producers; that the relevant effective area of competition was the area in which these producers operated, and in which they were willing to compete for the consumer potential.

We are persuaded that on the record in this case, neither peninsular Florida, nor the entire State of Florida, nor Florida and Georgia combined constituted the relevant market of effective competition. We do not believe that the pie will slice so thinly. By far the bulk of the overwhelming tonnage marketed from the same producing area as serves Tampa

is sold outside of Georgia and Florida, and the producers were 'eager' to sell more coal in those States. [9] While the relevant competitive market is not ordinarily susceptible to a 'metes and bounds' definition, cf. Times-Picayune Pub. Co. v. United States, 345 U.S. 594, 611, 73 S.Ct. 872, 881, 97 L.Ed. 1277, it is of course the area in which respondents ***332** and the other 700 producers effectively compete. Standard Oil Co. v. United States, supra. The record shows that, like the respondents, they sold bituminous coal 'suitable for (Tampa's) requirements,' mined in parts of Pennsylvania, Virginia, West Virginia, Kentucky, Tennessee, Alabama, Ohio and Illinois. We take notice of the fact that the approximate total bituminous coal (and lignite) product in the year 1954 from the districts in which these 700 producers are located was 359,289,000 tons, of which some 290,567,000 tons were sold on the open market. [10] Of the latter amount some 78,716,000 tons were sold to electric utilities. [11] We also note that in 1954 Florida and Georgia combined consumed at least 2,304,000 tons, 1,100,000 of which were used by electric utilities, and the sources of which were mines located in no less than seven States. [12] We take further notice that the production and marketing of bituminous coal (and lignite) from the same districts, and assumedly equally available to Tampa on a commercially feasible basis, is currently on a par with prior years. [13] In point of statistical fact, coal consumption in the combined Florida-Georgia area has increased significantly since 1954. In 1959 more than 3,775,000 were there consumed, 2,913,000 being used by electric utilities including, ****631** presumably, the coal used by the petitioner. [14] ***333** The coal continued to come from at least seven States. [15] From these statistics it clearly appears that the proportionate volume of the total relevant coal product as to which the challenged contract pre-empted competition, less than 1%, is, conservatively speaking, quite insubstantial. A more accurate figure, even assuming pre-emption to the extent of the maximum anticipated total requirements, 2,250,000 tons a year, would be .77%.

Effect on Competition in the Relevant Market.

It may well be that in the context of antitrust legislation protracted requirements contracts are suspect, but they have not been declared illegal per se. Even though a single contract between single traders may fall within the initial broad proscription of the section, it must also suffer the qualifying disability, tendency to work a substantial—not remote—lessening of competition in the relevant competitive market. It is urged that the present contract pre-empts competition to the extent of purchases worth perhaps $128,000,000, [16] and that this ***334** 'is, of course, not insignificant or insubstantial.' While $128,000,000 is a considerable sum of money, even in these days, the dollar volume, by itself, is not the test, as we have already pointed out.

The remaining determination, therefore, is whether the pre-emption of competition to the extent of the tonnage involved tends to substantially foreclose competition in the relevant coal market. We think not. That market sees an annual trade in excess of 250,000,000 tons of coal and over a billion dollars—multiplied by 20 years it runs into astronomical figures. There is here neither a seller with a dominant position in the market as in Standard Fashions, supra; nor myriad outlets with substantial sales volume, coupled with an industry-wide practice of relying upon exclusive contracts, as in Standard Oil, supra; nor a plainly restrictive tying arrangement as in International Salt, supra. On the contrary, we seem to have only that type of contract which 'may well be of economic advantage to buyers as well as to sellers.' Standard Oil Co. v. United States, supra, 337 U.S. at page 306, 69 S.Ct. at page 1058. In the case of the buyer it 'may assure supply,' while on the part of the seller it 'may make possible the substantial reduction of selling expenses, give protection against price fluctuations, and * * * offer the possibility of a predictable market.' Id., 337 U.S. at pages 306—307, 69 S.Ct. at page 1058. The 20-year period of the ****632** contract is singled out as the principal vice, but at least in the case of public utilities the assurance of a steady and ample supply of fuel is necessary in the public interest. Otherwise consumers are left unprotected against service failures owing to shutdowns; and increasingly unjustified costs might result in more burdensome rate structures eventually to be reflected in the consumer's bill. The compelling validity of such considerations has been recognized fully in the natural gas public utility field. This is not to say that utilities are immunized from Clayton Act proscriptions, but merely that, in judging the term ***335** of a requirements contract in relation to the substantiality of the foreclosure of competition, particularized considerations of the parties' operations are not irrelevant. In weighing the various factors, we have decided that in the competitive bituminous coal marketing area involved here the contract sued upon does not tend to foreclose a substantial volume of competition.

We need not discuss the respondents' further contention that the contract also violates s 1 and s 2 of the Sherman Act, for if it does not fall within the broader proscription of s 3 of the Clayton Act it follows that it is not forbidden by those of the

former. Times-Picayune Pub. Co. v. United States, supra, 345 U.S. at pages 608—609, 73 S.Ct. at page 880.

The judgment is reversed and the case remanded to the District Court for further proceedings not inconsistent with this opinion.

It is so ordered.

Judgment reversed and case remanded to the District Court for further proceedings.

Mr. Justice BLACK and Mr. Justice DOUGLAS are of the opinion that the District Court and the Court of Appeals correctly decided this case and would therefore affirm their judgments.

All Citations

365 U.S. 320, 81 S.Ct. 623, 5 L.Ed.2d 580

Footnotes

1 'It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods * * * for use, consumption, or resale within the United States * * * on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods * * * of a competitor or competitors of the * * * seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.' 15 U.S.C. s 14, 15 U.S.C.A. s 14.

2 In addition to their claim under s 3 of the Clayton Act, respondents argue the contract is illegal under the Sherman Act, 15 U.S.C. ss 1, 2, 15 U.S.C.A. ss 1, 2.

3 The original contract was with Potter Towing Company, and by subsequent agreements with Tampa Electric responsibility thereunder was assumed by respondent West Kentucky Coal Company.

4 Cf. Kelly v. Kosuga, 358 U.S. 516, 79 S.Ct. 429, 3 L.Ed.2d 475.

5 For discussion of previous cases, see Standard Oil Co. v. United States, 337 U.S. 293, 300—305, 69 S.Ct. 1051, 1055—1058, 93 L.Ed. 1371.

6 See International Boxing Club of New York, Inc. v. United States, 358 U.S. 242, 79 S.Ct. 245, 3 L.Ed.2d 270.

7 In support of these contentions petitioner urges us to consider that it remains free to convert existing oil-burning units at its other plants to coal-burning units, the fuel for which it would be free to purchase from any seller in the market; also that just as it is permitted to use oil at its other plants, so, too, it may construct all future Gannon units as oil burners; and that in any event it is free to draw a maximum of 15% of its Gannon fuel requirements from by-products of local customers. Petitioner further argues that its novel reliance upon coal in fact created new fuel competition in an area that theretofore relied almost exclusively upon oil and, to a lesser extent, upon natural gas.

8 Oil and, to a lesser extent, natural gas are the primary fuels consumed in Florida.

9 Peabody Coal Company offered to supply petitioner with coal from its mines in western Kentucky, for use in the units at another of its Florida stations, and that offer prompted a renegotiation of the price petitioner was paying for the oil then being consumed at that station.

10 U.S. Bureau of the Census. 1 U.S. Census of Mineral Industries: 1954, Series: MI-12B, p. 4 (1957).

11 Id., at 12B—6.

12 1,569,000 tons from counties in West Virginia, Virginia, Kentucky, Tennessee and North Carolina; 412,000 tons from counties in Alabama, Georgia and Tennessee; the balance was produced in other counties in West Virginia, Virginia and western Kentucky. Id., at 12B—10.

13 United States Dept. of Interior, Bureau of Mines, II Minerals Yearbook (Fuels), 1959.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

14 United States Dept. of Interior, Bureau of Mines, Mineral Market Report, M.M.S. No. 3035, p. 23 (1960). These statistics were taken from sources cited by respondents.

15 1,787,000 tons from certain counties in West Virginia, Virginia, Kentucky, Tennessee and North Carolina; 1,321,000 tons from counties in Alabama, Georgia and elsewhere in Tennessee; 665,000 tons from the western Kentucky fields; 2,000 tons from other counties in West Virginia and Virginia. Ibid.

16 In this connection we note incidentally that in Appalachian Coals, Inc., v. United States, 1933, 288 U.S. 344, 369, 53 S.Ct. 471, 477, 77 L.Ed. 825, cited by respondents, Chief Justice Hughes quoted testimony showing that in 1932 it was nothing those days 'for one interest or one concern to buy several million tons of coal.' At note 7. The findings of the District Court, 1 F.Supp. 339, showed that one utility consumed 2,485,000 tons of coal a year. Other concerns had requirements running from 30,000 to 250,000 tons annually, while a textile manufacturer used 600,000 tons. 288 U.S. at page 370, note 8, 53 S.Ct. at page 478. The Chief Justice also stated in his opinion that, within 24 counties in Kentucky, Tennessee (in both of which respondents operate) and their competitive States of Virginia and West Virginia, 'there are over 1,620,000 acres of coal bearing land, containing approximately 9,000,000,000 net tons of recoverable coal * * *.' 288 U.S. at page 369, 53 S.Ct. at page 477.

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-34

284 F. 377
District Court, S.D. Ohio, Western Division.

THOMAS-BONNER CO.
v.
HOOVEN, OWENS & RENTSCHLER CO.

No. 2557.
|
August 23, 1920.

Synopsis
At law. Action by the Thomas-Bonner Company against the Hooven, Owens & Rentschler Company. Judgment for defendant.

Attorneys and Law Firms

***378** Irving A. Fish, of Milwaukee, Wis., and Edw. P. Moulinier, of Cincinnati, Ohio, for plaintiff.

Floyd C. Williams and Stanley Shaffer, both of Cincinnati, Ohio, for defendant.

Opinion

SATER, District Judge.

At the conclusion of all of the evidence both parties moved for a directed verdict. Judge Hollister took the case under advisement. In due course, after his sudden death, it reached me for disposition as a part of his unfinished work.

For some time prior to April, 1915, the defendant had been endeavoring to construct for marketing a patented automatic typewriter. In the April issue of System, a magazine, the defendant advertised for 17 big caliber men as sales managers to introduce its new appliance, which managers were to measure up to the following standard:

'First. They must be experienced in the organizing and handling of a selling force. made up in turn of high-grade men.

'Second. They must have strong personality— be able to meet 'man to man' the biggest business men of this country and put our proposition before them.

'Third. They must be men of record— able to show results in the past. We don't want 'comers'— we want men of proved ability.

'Fourth. We want men who have some money— not that we need another dollar for the financing of our product, but simply that we consider men who have made money and saved money best suited for our work.'

Applicants were requested to communicate to Roberts, the defendant's sales manager, their financial ability and the whole story of their accomplishments in a business way. On April 3 a letter went forward to Roberts, signed 'The Thomas-Bonner Co., C. A. Bonner, President,' in which the belief was expressed that 'our firm' measures up to the four above-mentioned standard requirements, and gave the information that the firm's business was that of manufacturers' agents, that it represented in Wisconsin and the upper peninsula of Michigan two high-class articles, one an adding machine, and that it was prepared to take on the agency for another really meritorious article and put out high-class salesmen to market it successfully. On April 23, in a letter containing somewhat fulsome praise of the new device, Roberts stated the results obtainable by its use and that the machine would do the work of five typists. He announced that the defendant was conservative and would adhere to its usual method of selecting men; that it made the men selected a part of itself and of its permanent force, having made only one or two changes in its sales force in 20 years; that exceptional growing men of proven work, who are master salesmen, were wanted; that, instead of opening branch offices of its own, it would select proper men, furnish them with machines, allow them to open their own offices, and pay them a handsome commission; and that, if a desirable applicant of creditable record could show financial strength sufficient to open up and maintain an office, and ability to carry on business successfully, the defendant would be willing to enter into a contract with him. Able men, and not money, it was stated, was what the defendant desired.

On April 29 C. A. Bonner by letter informed Roberts that he had ***379** discussed the latter's proposition 'with our sales manager and with Mr. E. D. Thomas, my partner,' and asked for the form of contract proposed, on receipt of which he would then disclose 'of what the Thomas-Bonner Company is made.' Roberts' response was that, 'if you or your business associate can come down' to Hamilton, the terms to be embraced in a contract would be thoroughly considered. The Thomas-Bonner Company desired the agency for the Milwaukee district, if allowed 30 days to pay for the machines it would be required to buy for demonstration. On May 12 the defendant, as party of the first part, and 'the Thomas-Bonner Company, composed of C. A. Bonner, E. D. Thomas, and C. R. Thomas, of Milwaukee, Wisconsin, party of the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

second part,‘ executed a contract, the signatures to which are ‘The Hooven-Owens-Rentschler Company, by C. E. Hooven, Treas.,‘ and ‘The Thomas-Bonner Co. (party of the second part), C. A. Bonner, Pres't, E. D. Thomas, Secty.‘ The duties, in so far as need be noted, imposed on the Thomas-Bonner Company, were:

‘First. Diligent effort on the part of the party of the second part, in effecting sales of the Hooven automatic typewriter.

‘Second. Said second party agrees to devote his entire time to the work of and incidental to making sales of the Hooven automatic typewriter.

‘Third. The delivery and installation of said typewriters and accessories in the offices or place of business of the purchasers of same.

‘Fourth. The proper instruction of person or persons, designated by purchasers, to learn the operation and care of the Hooven automatic typewriter and its accessories.

‘Fifth. The taking care of and adjusting, also making repairs necessary when called upon to do so by purchasers, during the life of the guaranty, without charge to the purchaser.

‘Sixth. The handling of all detail and clerical work connected with and incident to the proper operation of the district office.‘

The company was further obligated to demonstrate the automatic typewriter and its accessories in a suitable office or salesroom; to employ a suitable person to make adjustments and repairs to such typewriter and accessories when called upon by purchasers or users in its district to do so, and to make no charge for such services or repairs made and parts furnished within such district during the period covered by the defendant's guaranty to purchasers or users, all necessary tools and parts required to maintain the required service to customers and to carry out the service guaranty to be furnished by the defendant; to abide by the selling rules or regulations of the defendant as issued from time to time, under penalty of forfeiture for violation on a 10-day written notice; to install in its office or salesroom two typewriters and their accessories for demonstration purposes and to pay for the same; to maintain the selling price of the typewriter as fixed by the defendant and to offer no discount, rebates, or other inducements that would affect the selling price, under penalty in case of violation, of forfeiture of the contract on 10 days' written notice; and to make at least six bona fide sales of typewriters each month, and on failure to do so the defendant might exercise the reserved privilege of canceling the contract on 60 days' written notice. The defendant agreed to do all advertising for the introduction of the device, furnishing the company, without charge, all pamphlets, catalogues, booklets, ***380** and other literature produced from time to time; to furnish without expense to the company all letter heads, envelopes, and other printed stationery necessary for the agency's business; to deliver to the company typewriters and accessories required by bona fide orders taken on sales order blanks furnished by defendant; to make all collections, ‘etc.,‘ in connection with sales of typewriters made by the company, the company, however, to assist whenever possible in effecting prompt collection on accounts made in its territory; to pay a 25 per cent. commission on all sales made by the company which were accepted by the defendant; to help the company in every possible manner in building up a profitable and satisfactory business; and to furnish the company with the names of inquirers about the machine and to make no sales within the company's district, except as a commission is paid to the company. In case of a disagreement between the parties, the company was to resell the two machines purchased by it to defendant at the price which the company paid defendant for the same. The contract was to remain in force from year to year, if the company complied with its terms.

From the foregoing it is clear that the defendant corporation knowingly contracted with the Thomas-Bonner Company as a partnership. The petition charges and the answer admits that the company was a partnership when the contract was made. Bonner's first letter apprised Roberts that he was writing for a ‘firm.‘ The word ‘firm‘ is synonymous with ‘partnership.‘ Bouvier's Law Dict. title ‘Firm‘; 3 Words and Phrases Jud. Def. 2820. His letter of April 29 told Roberts that Bonner and E. D. Thomas were partners. The mention in Roberts' letter of Bonner's ‘business associate‘ shows that he recognized that he was dealing with a partnership. The contract, when executed, brought to the defendant's knowledge the existence of a third partner. From examination of the handwriting of the signers and of the written portions of the contract, taken in connection with Roberts' letter of May 12, the conclusion seems necessarily to follow that all of such written portions were inserted in the printed froms at Hamilton, Ohio, before the two copies were sent to Milwaukee, and that the defendant consequently knew, before the contract was drawn, the names of all of the partners. Were it not so, it is not probable that the company would have been requested to return to Hamilton but one copy of the executed contract.

Importance cannot be rightfully attached to the fact that the party of the second part is referred to in the contract by the

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

pronoun 'his,' instead of 'its,' or 'their.' The contract is on a printed form, prepared on the theory that it would be used in dealing with a single individual. The manifest intention of the parties cannot be overthrown by their nonobservance of a grammatical error. The contract pledged the entire time of the firm, and consequently of the individuals composing it, to the making of sales of the typewriter and to the work incidental thereto. That the parties thus understood their contract is further evidenced by Exhibits 17, 18, and 19.

Carl R. Thomas, in May and early June, spent three weeks at Hamilton, Ohio, in attending an instruction school conducted by defendant at its plant, to acquaint him and 18 other agents with the machine ***381** 'and the selling end.' The purpose of the school was the training of good managers or salesmen, for 'to be a first-class salesman * * * you had to know about the factory business, the machine itself, and the parts of it.' It was for this reason Thomas pulled the machine apart and reassembled it, which, when so reconstructed by him, was operative. He so familiarized himself with the device's simple parts that he could adjust a machine, if something went wrong about it, but with considerable difficulty. In the matter of adjustment he was given, so he states, 'competent instructions,' and, when unable to proceed, was assisted by the factory men. Occasionally he operated a machine. Several of them were completed and in operation more or less of the time, to all of which he had access. He saw the device operated satisfactorily. It would 'stop once in a while, but a little adjustment would fix it; we gave it no thought. ' Parhn, who worked at the school alongside of Thomas, makes the defective operation of the machines more serious. He states that in his and Thomas' presence for two or three days at a time the pins would bend or break, lines would be misspaced, clutch trouble would occur, bands and springs would break, and the carriage return mechanism would operate defectively; the machine trouble being such as to cause comment by all of the 19 salesmen.

The first machine shipped to the Thomas-Bonner Company was for demonstration purposes and was forwarded June 24. It was put into use not later than the 27th. On the 28th the defendant sent Cornelson to instruct some one to be chosen by the Thomas-Bonner Company to act as demonstrator. On June 18 the members of the firm and Mahoney (and, according to the defendant's brief, Niemyer also) took steps to form a corporation to be known as the Thomas-Bonner Company, and on June 29 a certificate of incorporation was issued to such company by the Wisconsin secretary of state. The stockholders were the members of the firm and Mahoney. Whether Niemyer was also an incorporator and stockholder I am not able to determine, for the reason that Exhibits 1, 2, and 3 have not come into my possession. The extent of each stockholder's holdings does not appear. The firm assigned all of its business and affairs, rights, contracts, and assets, including its contract with the defendant and its liabilities thereunder, to the corporation, and in so far as such firm was able to do so made the corporation its successor in all of the partnership business. The corporation was authorized to sell, not only automatic typewriters, but office and electrical supplies. No notice was given to the defendant of the firm's assignment of its contract to the corporation. The defendant's first knowledge of the existence of such corporation and of the firm's assignment of its contract to it was acquired after the petition was filed in this case.

Carl R. Thomas set up the machine shipped to Milwaukee in June. On account of difficulty encountered, Cornelson on June 28 went to that city and remained there a week. He was not very long in getting the machine to run, and such trouble as occurred during his visit called only for minor adjustments. After his departure the typewriter would get out of order. It would, for instance, skip the space of a ***382** line, or a spring or carriage band would break. The difficulties encountered appear in detail in the correspondence which passed between the parties to this action. When properly adjusted, the machine worked satisfactorily. The contrast between Thomas' evidence and that of Bonner as to the operation of the machine at Milwaukee is quite as marked as that between his and Parhn's evidence as to observable difficulties at Hamilton. Cornelson found the machine at Milwaukee all right, outside of the little needed adjustment. It was in operation every day he was there, but he used it but little. Miss Nee was the only one to whom he gave instructions. The Thomas-Bonner Company did not succeed in operating successfully any machine sent it, and in consequence placed but one, and that proved a failure. During the activities of that company the defendant placed a number of machines which worked successfully and with the need of only slight occasional adjustments. Beneficial changes in certain parts of the device were effected; the change, however, not being in the functions performed. That the typewriter is an operative and commercial success seems clear.

The conclusion which I have reached is that the Thomas-Bonner Company never sufficiently mastered knowledge of the machine to keep it in steady running order. Carl R. Thomas was the only member of the firm that took instruction from a competent person. His information was not thorough. I am also of the opinion that the machine sent to Milwaukee was not so perfectly constructed as were those upon which

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

changes in certain respects were installed, and that such fact contributed to the difficulties encountered by the firm. The defendant caused some of its typewriter parts to be manufactured for it elsewhere, which it elected to discard. The Milwaukee machine may not have been up to standard. I am disposed to think there was fault on both sides. The letters of the Thomas-Bonner Company recite the difficulties encountered. They also speak at times of the machine's satisfactory working and of their great confidence in it as a successful invention. The company at all times clung to and expressed the desire to continue the agency. On October 30 it notified the defendant that after November 5 Carl R. Thomas 'will not be connected with this company,' and asked to know 'where we stand.' On November 1 the company by wire requested the defendant to state its position. On November 6 the defendant answered that, if it could be shown that some one could be secured to handle the proposition, it would be glad to continue the agency. On November 9 the defendant asked Bonner to advise what was intended about continuing as the defendant's representative, and was informed on November 15 that a continuance was desired. On December 3 the defendant wrote the company as follows:

'According to the terms of your contract you are to maintain your own service department by employing some one competent to take charge of same. This you have not done. Further, we have received just one order from you since you started in with the proposition. Therefore this is to inform you that, unless you are able to show some ability to sell the number of machines called for in your contract, we will have to cancel same. We will be glad to furnish you with a man who is able to take care of your service department at $15 to $18 per week.'

***383** Other correspondence followed, and on February 10 the defendant canceled the contract. The only claim pressed by the plaintiff is that it ought to recover $10,800, being the commissions which it asserts it could and would have earned in a year on the sale of 72 machines (six per month), had the device been operative and the contract continued for that period. The defense rests on the nonassignable character of the contract.

The plaintiff relies on the provision in the statutes of both Wisconsin (section 2605, Wis. Stat. 1911) and Ohio (section 11241, G.C.) that, subject to certain exceptions here immaterial, and action must be prosecuted in the name of the real party in interest. By virtue of the practice conformity act the rule requiring actions to be brought by the real party in interest prevails in actions at law in the federal courts sitting in the Code states. 15 Ency. Pl. & Pr. 709; Arkansas Valley Smelting Co. v. Belden Co., 127 U.S. 379, 387, 8 Sup.Ct. 1308, 32 L.Ed. 246. Whether the assignment of a contract makes the assignee the real party in interest, and vests in him the right to prosecute an action in his own name, depends on the terms and nature of the contract (American Bonding & Trust Co. v. B. & O.S.W.R. Co., 124 Fed. 866, 60 C.C.A. 52 (C.C.A. 6)); the vital question being (and it is the big one here) whether the contract is in fact assignable (Arkansas Valley Smelting Co. v. Belden Co., 127 U.S. 387, 8 Sup.Ct. 1308, 32 L.Ed. 246). Real party in interest does not mean one who will be affected by the judgement, but relates only to a legal interest, or one which would have been recognized either at law or in equity before the Code. 1 Bates, Pl. & Pr. 8.

The Code made nothing assignable that was not so before its adoption. Hodgman v. Western R. Co., 7 How.Prac.(N.Y.) 492, cited in note to section 2605, Wis. Stat. 1911. The only interpretation that can be placed upon the language that an action must be prosecuted in the name of the real party in interest is that, whenever a thing in action transferable by law is absolutely assigned, so that the ownership passes to the assignee, without conditions or reservations, and the legal or equitable claim is fully vested in him, he is the real party in interest, and must sue in his own name. Gruber v. Baker, 20 Nev. 453, 23 Pac. 858, 9 L.R.A. 302, 305. That there are contracts which are not assignable without assent of both parties is the law of both Wisconsin and Ohio. Varney v. Bartlett, 5 Wis. 276, 278; Johnson v. Vickers, 139 Wis. 145, 120 N.W. 837, 21 L.R.A.(N.S.) 359, 131 Am.St.Rep. 1046; Chapin v. Longworth, 31 Ohio St. 421. We must look to the nature and terms of the instrument under consideration.

The contract is executory. An executory contract for personal services, or a contract otherwise involving personal credit, trust, or confidence, cannot be assigned by one of the parties thereto, so as to compel the other party to accept performance by the assignee. Clark on Contracts, 364; American Bonding & Trust Co. v. B. & O.S.W.R. Co., 124 Fed. 872, 60 C.C.A. 52; Johnson v. Vickers, 139 Wis. 148, 120 N.W. 837, 21 L.R.A.(N.S.) 359, 131 Am.St.Rep. 1046; 4 Cyc. 22, 23; Page on Contracts, Sec. 1262; Sloan v. Williams, 138 Ill. 43, 27 N.E. 531, 12 L.R.A. 496, 497; ***384** Chapin v. Longworth, 31 Ohio St. 421; Edison v. Babka, 111 Mich. 235, 238, 69 N.W. 499. In Delaware County v. Diebold Safe & Lock Co., 133 U.S. 473, 488, 10 Sup.Ct. 399, 404 (33 L.Ed. 674), the rule is stated to be that:

'When rights arising out of contract are coupled with obligations, to be performed by the contractor, and involve

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

such a relation of personal confidence that it must have been intended that the rights should be exercised and the obligations performed by him alone, the contract, including both his rights and his obligations, cannot be assigned without the consent of the other party to the original contract. Arkansas (Valley Smelting) Co. v. Belden (Mining) Co., 127 U.S. 379, 387, 388.'

The personal acts and qualities of the three partners were material ingredients of the contract. Their engagement was for their personal services, requiring skill and peculiar qualifications, which they agreed to devote entirely to the marketing of defendant's device. The defendant contracted with them to assist in launching a new and important enterprise, by reason of the trust and confidence placed in them personally as men and skilled salesmen, and to a considerable extent on account of their financial ability and integrity, for they were to finance their agency and also to assist whenever possible in effecting prompt collections of all accounts due in their territory. This would seem to involve the measurable handling of the defendant's funds. The typewriter was a new, delicate, high-speed, and somewhat complex mechanism, requiring proper care and accurate adjustment to do its work efficiently. An operator ill trained and of erratic touch will fail to get an even movement of its operative parts, and consequently the work of which it is capable. Even the employment of the right kind of paper, rightly adjusted and thus maintained, is important to its successful use.

The burden of selecting a suitable employee to instruct operators in the use of the machine was undertaken by the partners. The responsibility for the training of such instructor was cast upon and assumed by them. The important and delicate task of demonstrating the machine to prospective purchasers was theirs. Its character and the necessity of creating a favorable impression on its first introduction to interested inquirers and the public were such that it was deemed necessary to teach salesmen 'all the essence of ordinary adjustment ' and 'the elements of proper selling.' A school of instruction was therefore conducted by defendant, in which sales agents were taught to disassemble and then to reassemble the device, that they might acquaint themselves with the device and its several parts, the office to be performed by each, and the manner of operation. Its successful and speedy operation, the demonstration of its utility and its economy producing qualities, its extensive and prompt marketing, its good reputation, and the profits to accrue to defendant, depended on successful salesmen and operators, acquainted with the device and its various parts, and capable of maintaining them in proper relation.

The defendant intrusted its business, and consequently the good name of itself and its novel device, in a large and attractive territory, to the personal diligence and skill of the partners. The fact that subsequently a service man was stationed at each sales agency to adjust out of order machines bespeaks the firm's difficult undertaking and the ***385** skill which they stipulated to acquire and exercise. Their pledge of that skill is evidenced by their obligation of a financial nature, without charge to purchasers and at their own expense, to care for, adjust, and make repairs when called upon by purchasers so to do. They were selected as agents and empowered to act as such because they represented themselves to be and were believed to be energetic, resourceful, high-grade men, of strong personality, experienced in organizing and handling a high-class selling force. They were accepted on the theory that they were to remain with, and as growing master salesmen were to be made a part of, the defendant's organization. The defendant emphasized the kind of men it desired for its sales agencies and its intention to make its own selections.

By the terms of the contract the entire estates of the respective partners were financially bound for any loss or damage which the defendant might sustain through the agency. It could not be required without its consent to accept, as a substitute named by them, a corporation which did not propose to devote its whole time and energy to the sale of defendant's device, but which was chartered to conduct another line of business also. Whether Mahoney's holdings were such as to enable him to select the corporate board of directors does not appear, but the right to dispose of stock made possible the change of corporate control, and the foisting upon defendant of agents of other than its own selection, would strip it of the individual financial liability of the members of the firm, would remit it to the financial responsibility or irresponsibility, as the case might be, of a corporation, and defeat its purpose of building up a permanent efficient selling organization. The partners were not authorized by an assignment of their contract to transfer their financial obligations, or their other obligations to perform, to a third party, effect their own release, and defeat in important respects, and perhaps entirely, the intent of the contracting parties. The defendant contracted with reference to the character, credit, and substance of the members of the firm, and it had the right to the benefit it anticipated therefrom. Arkansas Valley Smelting Co. v. Belden Min. Co., 127 U.S. 379, 8 Sup.Ct. 1308, 32 L.Ed. 246. The reasoning in Harper v. Dalzell, Gilmore & Leighton Co., 27 Bull. 274, and Johnson v. Vickers, 139 Wis. at page 148, 120 N.W. 837, 21 L.R.A. (N.S.) 359, 131 Am.St.Rep. 1046, is pertinent. It must be held that the contract was not assignable.

Nor is there merit in the contention that the defendant, by sending an imperfect machine to the firm in June, 1915, breached its contract, and thereby gave rise to a cause of action which was assignable, and was assigned to the corporation. If there was such a breach (which need not be determined), neither the firm nor the corporation availed themselves of it. On the contrary, the correspondence shows that they elected to treat and keep the contract alive, and without suggestion that it had been breached continued to operate thereunder; the defendant believing, however, all the while, that it was still dealing with a partnership, and the corporation and its members who had constituted the partnership insisting on maintaining and retaining the agency. The contract was canceled by the defendant. It was not renounced by either the partners or the corporation. The failure to elect ***386** to renounce defeats the contention made. 3 Page, Contracts, Sec. 1494; Tickler v. Andrae Mfg. Co., 95 Wis. 352, 70 N.W. 292; Pratt v. Freeman, 115 Wis. 648, 660, 92 N.W. 368.

The Wisconsin cases cited by plaintiff are easily distinguished. In Hanrahan v. Janesville, 145 Wis. 457, 130 N.W. 482, it was expressly stated that all the work required to be done under the contracts was done by the plaintiffs (the assignees) with the knowledge and consent of the defendant. In Day v. Buckingham, 87 Wis. 215, 218, 58 N.W. 254, it appears that the claims upon which the assignees sued had accrued and become the basis of actions before their assignment occurred. State v. Hastings, 15 Wis. 83, went off on the principal that the salary of an officer to become due is a possibility coupled with an interest, and as such is capable of being assigned. In Wisconsin, as elsewhere, in so far as I have been able to discover, the rule prevails that a contract is not assignable, unless by its terms and nature it is made so.

It follows, from the foregoing, that judgment must be entered for the defendant, and the case dismissed.

All Citations

284 F. 377, 1 Ohio Law Abs. 210

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-35

KeyCite Yellow Flag - Negative Treatment
Distinguished by Star Windshield Repair, Inc. v. Western Nat. Ins. Co., Minn., July 16, 2009

683 N.W.2d 267
Supreme Court of Minnesota.

TRAVERTINE CORPORATION, Appellant,
v.
LEXINGTON–SILVERWOOD, a Minnesota Limited Partnership, Respondent.

No. A03–210.
|
July 1, 2004.
|
Rehearing Denied July 22, 2004.

Synopsis
Background: Shareholder's judgment creditor, as assignee of shareholder's right to compensation under management agreement with corporation, sought payment of compensation owed under the agreement. The District Court, Hennepin County, Cara Lee Neville, J., granted corporation's motion to stay arbitration. Creditor appealed. The Court of Appeals, 670 N.W.2d 444,reversed and remanded. Review was granted.

The Supreme Court, Russell A. Anderson, J., held that a nonassignment clause precludes assignment of the right to payment under a contract, even if it does not explicitly limit, beyond the express nonassignment terms contained in that clause, the power of assignment, or provide that any purported assignment shall be invalid or void.

Court of Appeals reversed.

Procedural Posture(s): On Appeal.

***269** *Syllabus by the Court*

1. When a contractual provision is clear and unambiguous, courts should not rewrite, modify, or limit its effect by a strained construction.

2. A nonassignment clause precludes assignment of the right to payment under a contract even if it does not explicitly limit, beyond the express nonassignment terms contained in that clause, the power of assignment, or provide that any purported assignment shall be invalid or void.

Attorneys and Law Firms

Donald R. McNeil (# 200840), Steven F. Buterin (# 248642), Coleman, Hull & Van Vliet, PLLP, Minneapolis, MN, for Travertine Corporation.

Curtis D. Smith (# 102313), Peter A. Koller (# 150459), Moss & Barnett, Minneapolis, MN, for Lexington–Silverwood.

Heard, considered, and decided by the court en banc.

OPINION

ANDERSON, RUSSELL A., Justice.

We are asked to determine whether a nonassignment clause precludes assignment of the right to payment under a contract if the clause does not explicitly limit, beyond the express nonassignment terms contained in that clause, the power of assignment, or provide that any purported assignment shall be invalid or void. We hold that such a nonassignment clause does preclude assignment, and therefore reverse the court of appeals' decision to the contrary.

The underlying dispute in this case concerns the claim of respondent Lexington–Silverwood, L.P. that it was assigned the compensation that James E. Lennon was due under a "management agreement" to which Lennon, George Berkey, and appellant Travertine Corporation, a real-estate development venture, were parties. In August 1989, Travertine entered into the management agreement with Lennon and Berkey. The agreement provides that Lennon and Berkey would serve as the board of directors and officers of Travertine and would "provide all of the management services necessary to undertake the land acquisition, assembly and disposition" described in Travertine's business plan. Lennon subsequently served as President of Travertine. In return for their services, Travertine agreed to pay Lennon and Berkey a percentage of its net profits.

The management agreement further provides that if Travertine terminated the agreement, Lennon and Berkey would be entitled to compensation for their services up to the termination date. Disputes under the agreement are subject to an arbitration clause, which provides that "[i]n the event of a dispute between the parties with reference to the interpretation

of this Agreement or their rights hereunder, the same shall be submitted to arbitration." The nonassignment clause at issue provides in its entirety that:

> This Agreement shall be binding on the parties and their respective personal representatives, successors and assigns; provided, however, that the rights and obligations of Berkey/ Lennon shall not be assignable except that Berkey may ***270** assign to Lennon or Lennon assign to Berkey such rights and obligations.

In February 1992, Berkey assigned all of his rights under the management agreement to Lennon. In May 1996, Lexington–Silverwood obtained a judgment against Lennon in a matter unrelated to Travertine. In settlement of the judgment, Lennon purported to assign to Lexington–Silverwood his rights to compensation under the management agreement with Travertine. The assignment agreement [1] provided that Lexington–Silverwood "has an equitable assignment of Lennon's stock in Travertine" and that "Lennon agrees to transfer all other compensation, including anything due Lennon from his management agreement with Travertine."

On November 12, 1999, Travertine's Board of Directors terminated Lennon as President and "suspended" the management agreement. Not having secured a willing and able buyer for the real estate it had acquired, Travertine cancelled the management agreement on January 15, 2001. Lexington–Silverwood filed a demand for arbitration in March 2002, alleging that, as Lennon's assignee, it was entitled to the compensation due him under the management agreement and that Travertine had refused to pay it. Travertine moved the district court for an order staying arbitration. The court determined that Lennon's transfer of his right to compensation was not a valid present assignment, concluding that even if the assignment was enforceable, it was only an assignment of Lennon's right to receive compensation and not his right to demand arbitration. The court granted Travertine's motion to stay arbitration, but the court of appeals reversed. We granted Travertine's petition for further review, and now reverse.

I.

There is no dispute in this case that Lennon attempted to transfer his right to receive compensation under the management agreement, in violation of the anti-assignment clause; the issue before us is what effect that assignment should be afforded. Contract rights are generally assignable, except where the assignment is (1) prohibited by statute; [2] (2) prohibited by contract; (3) or where the contract involves a matter of personal trust or confidence. *Vetter v. Sec. Cont'l Ins. Co.,* 567 N.W.2d 516, 521 (Minn.1997); *Wilkie v. Becker,* 268 Minn. 262, 267, 128 N.W.2d 704, 707 (1964); *see also Klotz v. Jeddeloh,* 201 Minn. 355, 358, 276 N.W. 244, 245 (1937); 6 Am.Jur.2d *Assignments* §§ 17, 28 (1999).

***271** Contract interpretation is a question of law which we review de novo. *Employers Mut. Cas. Co. v. A.C.C.T., Inc.,* 580 N.W.2d 490, 493 (Minn.1998). The primary goal of contract interpretation is to determine and enforce the intent of the parties. *Motorsports Racing Plus, Inc., v. Arctic Cat Sales, Inc.,* 666 N.W.2d 320, 323 (Minn.2003). Where there is a written instrument, the intent of the parties is determined from the plain language of the instrument itself. *Metro. Sports Facilities Commn. v. General Mills,* 470 N.W.2d 118, 123 (Minn.1991). We have consistently stated that when a contractual provision is clear and unambiguous, courts should not rewrite, modify, or limit its effect by a strained construction. *Telex Corp. v. Data Products Corp.,* 271 Minn. 288, 295, 135 N.W.2d 681, 687 (1965); *Anderson v. Twin City Rapid Transit Co.,* 250 Minn. 167, 178, 84 N.W.2d 593, 601 (1957); *Grimes v. Toensing,* 201 Minn. 541, 545, 277 N.W. 236, 238 (1938).

The primary purpose of clauses prohibiting the assignment of contract rights is to protect the contracting party from dealing with parties he has not chosen to do business with. *See generally* 6 Am.Jur.2d *Assignments* § 29 (1999). Travertine contends that the management agreement prohibits the assignment of the rights and obligations of the parties. Lexington-Silverwood argues that the antiassignment clause in the management agreement only creates a covenant not to assign because it does not specifically state that any attempted assignment will be "void" or "invalid," or that Lennon "lacks the power" to assign the contract. Travertine counters that the use of these terms is not required because the contract expressly prohibits Lennon from assigning his rights.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

Lexington–Silverwood contends that the assignment should be upheld despite the antiassignment clause because the modern trend of authority disfavors contractual prohibitions on assignments, especially in this case where the clause failed to expressly make the assignment void. Lexington–Silverwood urges us to adopt the default interpretive rules provided by the Restatement (Second) of Contracts:

> (1) Unless the circumstances indicate the contrary, a contract term prohibiting assignment of "the contract" bars only the delegation to an assignee of the performance by the assignor of a duty or condition.
>
> (2) A contract term prohibiting assignment of rights under the contract, unless a different intention is manifested,
>
> (a) does not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation;
>
> (b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective;
>
> (c) is for the benefit of the obligor, and does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition.

Restatement (Second) of Contracts § 322 (1981).

We will not adopt a provision of a Restatement of the Law if our precedent is to the contrary and we believe that our precedent still reflects the proper rule of law. *See* ***272** *Coyle v. Richardson-Merrell, Inc.,* 526 Pa. 208, 584 A.2d 1383, 1385 (1991) ("Where the facts of a case demonstrate that the [Restatement] rule outruns the reason, the court has the power, indeed the obligation, to refuse to apply the rule, a power for the most part unavailable where the rule is legislatively ordained. Were it otherwise, our recognition of the work of the American Law Institute would approach an improper conferral of legislative authority.").

In this case, we need not adopt the default interpretive rules provided by the Restatement (Second) of Contracts § 322 because our precedent that parties may agree that their contractual rights and obligations are not to be assigned is well-established. *Vetter,* 567 N.W.2d at 521; *Wilkie,* 268 Minn. at 267, 128 N.W.2d at 707. In our 1964 decision of *Wilkie v. Becker,* we explained

> The general rule is that the right to receive money due or to become due under an existing contract may be assigned even though the contract itself may not be assignable. A contract to pay money may be assigned by the person to whom the money is payable, *unless there is* ***something*** *in the terms of the contract manifesting the intention of the parties that it shall not be assigned.*

Wilkie, 268 Minn. at 267, 128 N.W.2d at 707 (quoting 6 Am.Jur.2d *Assignments* § 16) (emphasis added). The language emphasized above is crucial. We did not require that the parties use specific terms to preclude assignment, but merely required the parties to include *something* expressing their intent that the contract not be assignable. Because there was nothing in the terms of the contract manifesting the intention of the parties that it was not to be assigned, we upheld the assignment. *Wilkie,* 268 Minn. at 268, 128 N.W.2d at 708. We rearticulated this same general rule in our 1997 decision of *Vetter v. Security Continental Insurance:*

> As a general rule, *and in the absence of a contractual provision to the contrary,* an obligor on a contract may assign all beneficial rights to another, or may delegate his or her duty to perform under the contract to another, without the consent of the obligee.

567 N.W.2d at 521 (emphasis added). Once again, we did not require specific terms or magic words, but merely some indication that the parties intended that the contract not be assigned.

Here the contract provides in relevant part that *"the rights and obligations of Berkey/Lennon shall not be assignable."* (Emphasis added.) It is a well-worn maxim that use of the term "shall" reflects a mandatory imposition. *Ind. Sch. Dist. No. 561 v. Ind. Sch. Dist. No. 35,* 284 Minn. 426, 436, 170 N.W.2d 433, 440 (1969). The inclusion of the language quoted above satisfies the requirement that the parties include

something in the terms of the contract manifesting the intention of the parties that it shall not be assigned. *Vetter,* 567 N.W.2d at 521; *Wilkie,* 268 Minn. at 267, 128 N.W.2d at 707. Therefore, we hold that the contract between Travertine and Lennon is nonassignable.

II.

Even under the so-called "modern" Restatement view, however, Lennon's purported assignment is void. The crucial phrase in section 322 is "unless a different intention is manifested." If the contract shows an intent by the parties to limit both delegations of duties and assignment of rights, and specifically states who is bound by the assignment prohibition, then the interpretive default rules are inapplicable. We acknowledge that there is a split of authority regarding the appropriate standard for determining when the parties have sufficiently manifested an intention to prohibit the power of assignment. *See* ***273** *Rumbin v. Utica Mut. Ins. Co.,* 254 Conn. 259, 757 A.2d 526, 531–36 (2000) (collecting cases and discussing the various approaches taken).

Some courts that have interpreted Restatement (Second) of Contracts § 322 have generally distinguished between a party's "right" to assign and a party's "power" to assign. *See, e.g., Bel–Ray Co. v. Chemrite Ltd.,* 181 F.3d 435, 442 (3d Cir.1999); *Cedar Point Apartments, Ltd. v. Cedar Point Inv. Corp.,* 693 F.2d 748, 754 (8thCir.1982). As reflected by section 322(2)(b), the law presumes that "contractual provisions limiting or prohibiting assignments operate only to limit a parties' right to assign the contract, but not their power to do so, unless the parties manifest an intent to the contrary with specificity." *Bel–Ray Co.,* 181 F.3d at 442 (citations omitted). In its 1982 decision of *Cedar Point Apartments, Ltd. v. Cedar Point Inv. Corp.,* the Eighth Circuit held that the following language served "only as a restriction on the delegation of duties, and not on the assignment of rights":

> Purchaser shall have the right to assign this Agreement to any partnership of which [sic] is a general partner; provided, however, that Purchaser shall have such right of assignment only if such assignee or transferee shall in writing expressly assume and agree to perform and discharge each and every obligation and liability of Purchaser set forth in this agreement.

693 F.2d at 752.

Likewise, in its 1999 decision of *Bel-Ray Co. v. Chemrite Ltd.,* the Third Circuit held that the following contract language did not limit the assignor's "power" to assign: "Agreement and the obligations and rights under this Agreement will not be assignable by [Chemrite] without express prior written consent of Bel-Ray, which may be withheld at the sole discretion of Bel-Ray." 181 F.3d at 442–43. According to the *Bel-Ray* court, in order to limit the parties' power to assign, "the assignment provision must generally state that nonconforming assignments (i) shall be 'void' or 'invalid,' or (ii) that the assignee shall acquire no rights or the nonassigning party shall not recognize any such assignment." *Id.* at 442 (citations omitted). "In the absence of such language, the provision limiting or prohibiting assignments will be interpreted merely as a covenant not to assign * * *." *Id.* Breach of the covenant may give rise to damages, but it will not render the assignment invalid or unenforceable. *Id.* Finally, the Supreme Court of Oklahoma has held that the following contract language "clearly and unambiguously precludes assignment": "Plaintiffs agree that they maintain no right to * * * have *power* to sell, mortgage, encumber, or anticipate the future payments, or any part thereof by assignment or otherwise." *In re Kaufman,* 37 P.3d 845, 855 (Okla.2001) (emphasis added).

The Seventh Circuit, however, has rejected the requirement of using such "magic words," classifying them as "empty verbiage." *Bank of America, N.A. v. Moglia,* 330 F.3d 942, 948 (7th Cir.2003) (applying law of Illinois, which had adopted Restatement (Second) of Contracts § 322). We agree with the Seventh Circuit. We will not impose formulaic restraints on the language that contracting parties may employ to craft an anti-assignment clause that limits the power to assign. We believe the best approach is to simply apply the plain meaning of the words employed by the parties. When a contract prohibits assignment in very specific and unmistakable terms, any purported assignment is void. Although requiring the use of specific language, such as "void" or "invalid"—as mandated by the Third Circuit in *Bel-Ray*—would help to resolve ***274** any conceivable ambiguity about whether the parties intended to limit the "power" to assign rather than the "right" to assign, it is difficult to identify a clearer way to

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

communicate an intent to deny a party the power to assign than to expressly say so.[3]

With the exception that Berkey may assign to Lennon and Lennon may assign to Berkey, the management agreement provides that *"the rights and obligations of Berkey/Lennon shall not be assignable."* (Emphasis added.) We hold that the anti-assignment clause is a valid and enforceable term of the management agreement, and that the parties intended to deny Lennon the power to assign his rights under the management agreement to anyone but Berkey. Therefore, Lennon's purported assignment of his right to compensation to Lexington–Silverwood is void.

Reversed.

All Citations

683 N.W.2d 267

Footnotes

1 This agreement was also entitled "Management Agreement," but to avoid confusion, we simply refer to it as the "assignment agreement."

2 We are cognizant of the fact that Minn.Stat. § 181.05 (2002) provides that an assignment of unearned wages or salary is void:

> No assignment, sale, or transfer, however made or attempted, of any unearned wages or salary shall be in any manner valid or effectual for the transfer of any salary or wages to be earned or accruing after the making of such assignment, sale, or transfer, unless the person, firm or corporation from whom such wages or salary are to accrue shall consent thereto in writing. Any employer or agent of such employer accepting or charging any fee or commission for collecting the amount due on any such assignment, sale, or transfer shall be deemed guilty of a misdemeanor.

The record before us, however, is inconclusive with regard to (1) Lennon's employment relationship with Travertine; and (2) the time period over which Lennon earned the compensation he purported to assign to Lexington–Silverwood. For these reasons, we decline Travertine's invitation to decide this case based upon application of Minn.Stat. § 181.05.

3 Other courts have taken this approach, and given effect to contract provisions that specifically prohibit the assignment of ones right to receive money due under a contract. *See, e.g., Liberty Life Assurance Co. of Boston v. Stone Street Capital, Inc.,* 93 F.Supp.2d 630, 638 (D.Md.2000) (upholding anti-assignment provision in structured settlement agreement in spite of fact that the provision did not contain the words "void" or "invalid."); *Grieve v. General American Life Ins. Co.,* 58 F.Supp.2d 319, 321 (D.Vt.1999) (same); *Johnson v. First Colony Life Ins.,* 26 F.Supp.2d 1227, 1229–30 (C.D.Cal.1998) (same); *Parrish Chiropractic Centers, P.C. v. Progressive Cas. Ins. Co.,* 874 P.2d 1049, 1055 (Colo.1994) (upholding anti-assignment provision as preventing any effective assignment because "[w]hen a contractual provision is clear and unambiguous, courts should neither rewrite it nor limit its effect by a strained construction."); *CGU Life Insurance Co. v. Singer Asset Finance Co.,* 250 Ga.App. 516, 553 S.E.2d 8, 15 (2001) (upholding anti-assignment provision even though structured settlement agreement failed to make assignments expressly void or otherwise ineffective); *J.G. Wentworth S.S.C. v. Callahan,* 256 Wis.2d 807, 649 N.W.2d 694, 696 (2002) (refusing to require "magic" words in order to enforce a nonassignability clause).

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-36

UNIDROIT

International Institute for the Unification of Private Law

UNIDROIT PRINCIPLES

OF INTERNATIONAL COMMERCIAL CONTRACTS

2016

Suggested form of citation:

Art. 1.6(2) UNIDROIT Principles 2016

Published by the
International Institute for the Unification of Private Law
(UNIDROIT), Rome

info@unidroit.org

ISBN: 978 - 88 - 86449 - 37 - 3

Copyright © UNIDROIT 2016

FOREWORD TO THE 2016 EDITION

In presenting this fourth edition of the UNIDROIT Principles of International Commercial Contracts, we would like first of all to express our deepest appreciation to the Members of the Working Group, in particular to the Rapporteurs responsible for the various topics that were addressed in this revision to take better into account the special needs of long-term contracts. We also wish to express our gratitude to the Observers who participated in the sessions of the Working Group in representation of important international organisations and other interested institutions and arbitration associations. It was only on account of the outstanding competence and extraordinary efforts of all those experts, again so ably coordinated by Mr Michael Joachim Bonell, that this new edition of the UNIDROIT Principles was made possible.

We must again recognise all those who, through scholarly writings or by applying the UNIDROIT Principles in practice, have contributed to the great success of the Principles. Such writings and practical experience have greatly assisted the Working Group in their deliberations. We hope that this support of the Principles and sharing of experiences will continue in the future.

A special word of thanks goes to Mr Neale Bergman and Ms Lena Peters of the UNIDROIT Secretariat, who served as Secretaries to the Working Group and undertook the important task of editing the additions and amendments.

Our gratitude also goes to the other members of the Secretariat, in particular Ms Frédérique Mestre for preparing the French language version of the Principles in co-operation with Mr Marcel Fontaine and Ms Isabelle Dubois for her formatting work of the new edition.

Last but by no means least, we would like to express our deepest appreciation to the Max-Planck-Institut für ausländisches und internationales Privatrecht and its Director Reinhard Zimmermann for generously hosting the second meeting of the Working Group in Hamburg.

José Angelo Estrella Faria	*Alberto Mazzoni*
Secretary-General	*President*

CHAPTER 9

ASSIGNMENT OF RIGHTS, TRANSFER OF OBLIGATIONS, ASSIGNMENT OF CONTRACTS

SECTION 1: ASSIGNMENT OF RIGHTS

ARTICLE 9.1.1
(Definitions)

"Assignment of a right" means the transfer by agreement from one person (the "assignor") to another person (the "assignee"), including transfer by way of security, of the assignor's right to payment of a monetary sum or other performance from a third person ("the obligor").

COMMENT

In many circumstances an obligee entitled to the payment of a monetary sum or to another performance from an obligor may find it useful to assign its right to another person. For instance, an assignment to a bank is a common way to finance the credit granted to a customer. The Articles of the present Section cover the assignment of rights as defined in this Article.

1. Transfer by agreement

Only transfers by agreement are concerned, as opposed to situations in which the applicable law may provide for legal transfers of certain rights (such as, in certain jurisdictions, the transfer of a seller's rights against an insurer to the purchaser of an insured building, or the automatic transfer of rights in the case of the merger of companies (see Article 9.1.2(b)).

The definition equally does not cover unilateral transfers, which in certain jurisdictions may take place without the assignee's participation.

2. Right to payment of a monetary sum or to other performance

On the other hand, the definition is not restricted to the assignment of rights to the payment of a monetary sum. It also covers rights to other kinds of performance, such as the rendering of a service. Nor are the assignable rights limited to rights of a contractual nature. Claims deriving from non-contractual claims or based on a judgment, for instance, can be governed by the present Section, subject to Article 1.4. Future rights may also be transferred under the conditions of Article 9.1.5.

3. Notion of "transfer"

The "transfer" of the right means that it leaves the assignor's assets to become part of those of the assignee. The definition also covers transfers for security purposes.

4. Third party rights

Transfers from the assets of the assignor to those of the assignee remain subject to third party rights. Different third persons can be affected by the assignment of a right between an assignor and an assignee, such as, first and foremost, the obligor, but also the assignor's creditors and successive assignees. Third party rights are covered in part by other provisions of this Section (see Articles 9.1.10 and 9.1.11 concerning the obligor and successive assignees). They may in some instances be governed by mandatory rules of the otherwise applicable law (e.g. the law of bankruptcy).

ARTICLE 9.1.2
(Exclusions)

This Section does not apply to transfers made under the special rules governing the transfers:

(a) of instruments such as negotiable instruments, documents of title or financial instruments, or

(b) of rights in the course of transferring a business.

COMMENT

Some types of assignment of rights are normally subject to very specific rules under the applicable law, and are therefore not governed by this Section.

1. Transfer of instruments governed by special rules

The transfer of certain types of instrument governed by special rules are outside the scope of this Section. This applies for instance to negotiable instruments, such as bills of exchange, that are usually transferred by endorsement or delivery of the document, and which are subject to further distinct rules, e.g. concerning defences that would have been available to the transferor. This exclusion also applies to documents of title, such as bills of lading or warehouse receipts, and financial instruments such as stocks and bonds. The transfer of such instruments are all normally subject to specific rules.

This does not exclude the possibility that such rights, in certain jurisdictions, could also be transferred by a normal assignment, which would then be subject to this Section.

2. Transfer of a business

Another exclusion is assignment made in the course of transferring a business under special rules governing such transfers, as may happen in the case of the merger of companies. The applicable law often provides for mechanisms that cause all rights and obligations, under certain conditions, to be transferred in their entirety by operation of law.

Article 9.1.2(b) does not prevent this Section from applying when certain rights pertaining to the transferred business are assigned individually. On the contrary, the mere transfer of shares in a company may fall under Article 9.1.2(a) and therefore not be covered by this Section.

Illustrations

1. Company A is transferred to company B. If the otherwise applicable law provides that all rights pertaining to the former company are automatically transferred to the latter, the Principles do not apply.

2. The initial facts are the same as in Illustration 1, but B is not interested in taking over a specific claim against customer X, and prefers that right to be assigned to company C. This particular transfer is subject to the Principles.

ARTICLE 9.1.3
(Assignability of non-monetary rights)

A right to non-monetary performance may be assigned only if the assignment does not render the obligation significantly more burdensome.

COMMENT

The assignment of a right does not in principle affect the obligor's rights and obligations. However, to a certain extent the fact that performance is now due to another obligee can modify the conditions under which the obligation is to be performed. The place of performance may be different. The change of obligee may in itself render the obligation more burdensome.

Article 9.1.8 entitles the obligor to be compensated by the assignor or the assignee for any additional costs caused by the assignment. That provision should be sufficient to take care of the problem in the case of the assignment of monetary obligations. However, when the assigned right concerns a non-monetary performance, the remedy may not always be sufficient. This Article excludes the possibility of assigning such rights when the transfer would render the obligation significantly more burdensome for the obligor.

Illustrations

1. Company X has undertaken to provide the security service aimed at preventing theft in warehouses used by company A for the storage of wood. The premises are sold to company B, which intends to apply them to the same use. Nothing in this provision prevents A from assigning to B its right to the security services provided by X.

2. The initial facts are the same as in Illustration 1, but B intends to use the warehouses for the storage of electronic equipment. A's right to the security services provided by X may not be assigned to B: such services would become significantly more burdensome since the security risks are obviously much higher with electronic equipment than with the storage of wood.

ARTICLE 9.1.4
(Partial assignment)

(1) A right to the payment of a monetary sum may be assigned partially.

(2) A right to other performance may be assigned partially only if it is divisible, and the assignment does not render the obligation significantly more burdensome.

COMMENT

1. Economic interest

The partial assignment of a right may serve different economic purposes. A contractor may for instance want to assign part of its right to payment from a customer to a financing institution and keep the rest for itself. Or it may want to assign the other part to a supplier of raw materials.

Permitting partial assignment may however affect the principle that the assignment should not worsen the obligor's situation. If the right is split, the obligor will have to perform in several parts, which could entail extra costs.

2. Monetary and non-monetary rights

The obligor's burden of having to make two or several monetary payments instead of one is not in itself deemed to be excessive, and partial assignments of monetary rights are therefore permitted in principle (paragraph (1)).

Another rule prevails for the assignment of non-monetary rights, where the validity of the partial assignment is made dependent on two cumulative conditions: the divisibility of the performance due and the degree of additional burden the partial assignment may place on the obligor. Article 9.1.3 already excludes the possibility to assign non-monetary rights in their entirety if the assignment would render the obligation significantly more burdensome. Paragraph (2) applies the same rule to the partial assignment of such rights.

In any event, additional costs borne by the obligor as a result of having to perform in several parts must be compensated under Article 9.1.8.

Illustrations

1. Buyer X is due to pay a price of USD 1,000,000 to seller A on 31 October. A urgently needs USD 600,000 and assigns a corresponding part of its right to bank B. Notice of the partial assignment is given to X. On 31 October, both A and B claim payment of their respective parts. X must pay A USD 400,000 and B USD 600,000.

2. Metal company X is to deliver 1,000 tons of steel to carmaker A on 31 October. Due to a decrease in sales, A estimates that it will not need that much steel at that time, and assigns the right to delivery of up to 300 tons to carmaker B. Notice of the partial assignment is given to X. On 31 October both A and B claim delivery of their respective quantities. X must deliver 700 tons to A and 300 tons to B.

3. Tax consultant X has promised to spend 30 days in examining the accounts of company A in order to determine the proper policy to be followed in the light of new tax regulations. A subsequently regrets this arrangement, in consideration of the level of the fees to be paid. It proposes to assign 15 of the days to company B. X can argue against such a partial assignment on the grounds that performance of tasks of that nature is not divisible. It can also argue that the accounts of B are of a significantly more complex nature than those of A.

ARTICLE 9.1.5
(Future rights)

A future right is deemed to be transferred at the time of the agreement, provided the right, when it comes into existence, can be identified as the right to which the assignment relates.

COMMENT

1. Economic interest

For the purposes of this Section, a future right is a right that will or might come into existence in the future (as opposed to a present right to a performance due in the future). Examples of future rights are rights that a bank may have against a customer who might be granted a credit line in the future, or that a company may have against another

company on the basis of a contract which might be concluded in the future. The assignment of such future rights can be highly significant economically.

2. Determinability

According to this Article a future right can be assigned on condition that it can be determined as the right to which the assignment relates when it comes into existence. The reason for this is the need to avoid the difficulties that might be caused by a transfer of future rights that are described in vague and too broad general terms.

3. Retroactive effect

This Article also provides that the assignment of future rights is effective with retroactivity between the assignor and the assignee. When the right comes into existence, the transfer is considered to have taken place at the time of the assignment agreement.

As regards third parties, it will be recalled that their rights may in some instances be governed by mandatory rules of the otherwise applicable law (e.g. the law of bankruptcy). However, third party rights are partly covered by other provisions of this Section, including the consequences of notices specified in Articles 9.1.10 and 9.1.11.

Illustration

> In order to finance new investments, company A assigns the royalties to be earned from future licences of a certain technology to lending institution B. Six months later, A licenses that technology to company X. The royalties due are considered to have been assigned to B from the date of the assignment agreement, provided the royalties can be related to this agreement.

ARTICLE 9.1.6

(Rights assigned without individual specification)

A number of rights may be assigned without individual specification, provided such rights can be identified as rights to which the assignment relates at the time of the assignment or when they come into existence.

COMMENT

Rights are often assigned as a bundle or in bulk. A company may for instance assign all its receivables to a factoring company. In practice it would be excessively burdensome to require individual specification of each assigned right, but the global identification of the rights assigned as a bundle must be such as to permit the recognition of each right concerned as part of the assignment.

In the case of existing rights, such recognition must be possible at the time of the assignment. If future rights are included in the bundle, in accordance with Article 9.1.5 identification must be possible when the rights come into existence.

Illustration

Retailer A assigns all its receivables to factor B. There are thousands of existing and/or future rights. The assignment does not require the specification of each single claim. Later, B gives notice of the assignment to the obligor of a specific receivable. B must be able to demonstrate the inclusion of that receivable in the bundle either at the time of the assignment, or, in the case of a right which did not exist yet at that time, when the right came into existence.

ARTICLE 9.1.7

(Agreement between assignor and assignee sufficient)

(1) A right is assigned by mere agreement between the assignor and the assignee, without notice to the obligor.

(2) The consent of the obligor is not required unless the obligation in the circumstances is of an essentially personal character.

COMMENT

In the definition of Article 9.1.1 the assignment of a right is described as a “transfer by agreement”. Articles 9.1.7 to 9.1.15 govern the respective legal positions of assignor, assignee and obligor.

1. Mere agreement between assignor and assignee

According to paragraph (1) of this Article, the assignment of a right is effective, i.e. the right is transferred from the assignor's assets to the assignee's assets, by mere agreement between these two parties. The provision is an application to the assignment of a right of the general principle laid down in Article 1.2 according to which nothing in the Principles requires a contract to be concluded in a particular form. Yet it does not affect the possible application of mandatory rules of the otherwise applicable law according to Article 1.4: thus, for instance, an assignment for security purposes may be subject to special requirements as to form.

As already stated in Comment 4 on Article 9.1.1, the rule laid down in paragraph (1) remains subject to third party rights, which are partly covered by other provisions of this Section (see Articles 9.1.10 and 9.1.11 concerning the obligor and successive assignees), and may in some instances be governed by mandatory rules of the otherwise applicable law (e.g. the law of bankruptcy) according to Article 1.4. However, it should be stressed that notice to the obligor as provided for by Article 9.1.10 is not a condition for the effectiveness of the transfer of the right(s) between the assignor and the assignee.

2. Consent of the obligor in principle not required

Paragraph (2) states explicitly what is already implied in paragraph (1), i.e. that the obligor's consent is not required for the assignment to be effective between the assignor and the assignee.

3. Exception: obligation of an essentially personal character

An exception is made for the case in which the right to be assigned relates to an obligation of an essentially personal character, i.e. a right that has been granted by the obligor specifically to the person of the obligee. This characteristic prevents the right from being assigned without the consent of the obligor, since it would be inappropriate to oblige the obligor to perform in favour of another person.

Illustrations

1. Company X promises to sponsor activities organised by organisation A, engaged in the defence of human rights. A wishes to assign the right to organisation B, active in the protection of the environment. The assignment can only take place with X's agreement.

2. A famous soprano has made a contract with agent A to sing in concerts organised by A. A sells its claims against the soprano to agent B. This transfer will require the soprano's consent, if the circumstances reveal that she was willing to sing only for A.

4. Effect of other provisions

The possibility to assign a right without the obligor's consent may be affected by the presence of a non-assignment clause in the contract between the assignor and the obligor (see Article 9.1.9), although such a clause does not in itself necessarily imply the essentially personal character of the obligation.

This Article does not address the issue of the necessity to give notice of the assignment to the obligor in order to avoid that the obligor pay the assignor after the assignment has taken place. On these issues, see Articles 9.1.10 and 9.1.11.

ARTICLE 9.1.8
(Obligor's additional costs)

The obligor has a right to be compensated by the assignor or the assignee for any additional costs caused by the assignment.

COMMENT

1. Compensation for additional costs

The assignment of a right does not necessarily affect the obligor's rights and obligations. However, should the obligor bear additional costs due to the fact that performance has to be rendered to the assignee instead of the original obligee, this Article entitles the obligor to require due compensation.

Illustration

1. Company X is obliged to reimburse a loan of EUR 1,000,000 to company A. Both companies are located in country M. A assigns its right to company B, located in country N. X has a right to be compensated for the additional costs involved in what has now become an international transfer.

The rule laid down in this Article is in conformity with Article 6.1.6, which provides a similar solution if a party to the contract changes its place of business after the conclusion of the contract.

2. Compensation by the assignor or the assignee

The obligor may claim compensation for additional costs either from the assignor or from the assignee. In the case of a monetary obligation, the obligor will often be in a position to set off its right to compensation against the obligation it owes to the assignee.

3. Partial assignment

Additional costs may arise in particular in the case of partial assignment (see Article 9.1.4). This Article applies accordingly.

Illustration

2. In Illustration 2 to Article 9.1.4, A has assigned to B part of its right to receive a delivery of steel from X. Instead of having to deliver 1,000 tons to A, X became obliged to deliver 700 tons to A and 300 tons to B. X is entitled to be compensated for the additional costs resulting from having to deliver in two parts.

4. Obligation becoming significantly more burdensome

In two cases compensation for additional costs is not considered to be a sufficient remedy. Firstly, under Article 9.1.3 the assignment of a right to a non-monetary performance is not allowed when it would render the obligation significantly more burdensome. Secondly, under Article 9.1.4 the partial assignment of a right to a non-monetary performance is also not allowed in similar circumstances.

ARTICLE 9.1.9

(Non-assignment clauses)

(1) The assignment of a right to the payment of a monetary sum is effective notwithstanding an agreement between the assignor and the obligor limiting or prohibiting such an assignment. However, the assignor may be liable to the obligor for breach of contract.

(2) The assignment of a right to other performance is ineffective if it is contrary to an agreement between the assignor and the obligor limiting or prohibiting the assignment. Nevertheless, the assignment is effective if the assignee, at the time of the assignment, neither knew nor ought to have known of the agreement. The assignor may then be liable to the obligor for breach of contract.

COMMENT

1. Balance of interests

According to Article 9.1.7(2) the consent of the obligor is not required for the assignment to be effective between the assignor and the assignee unless the obligation is of an essentially personal character. However, in practice it is frequent for the contract between the original obligee/assignor and the obligor to contain a clause limiting or prohibiting the assignment of the original obligee/assignor's rights as the obligor may not wish to change obligee. Should the original obligee/assignor subsequently assign such rights in spite of the non-assignment clause, the conflicting interests of the obligor and of the assignee must be weighed. The obligor suffers a violation of its contractual rights, but the assignee must equally be protected. At a more general level, it is also important to favour the assignment of rights as an efficient means of financing.

In this respect this Article makes a distinction between the assignment of monetary rights and the assignment of rights to other performances.

2. Monetary rights

In the case of the assignment of monetary rights, paragraph (1) gives preference to the needs of credit. The assignee of a monetary right is protected against non-assignment clauses and the assignment is fully effective. However, as the assignor acts contrary to its contractual duties, it is liable in damages to the obligor for non-performance of the contract under Chapter 7, Section 4.

Illustrations

1. Contractor A is entitled to the payment of USD 100,000 from its customer X after a certain stage of construction work has been completed. The contract contains a clause prohibiting A from

assigning the right. A nevertheless assigns the right to bank B. B can rely on the assignment despite the clause, and can claim payment when it is due. X is however entitled to sue A for acting in breach of the clause. X could for instance claim damages if it demonstrates that it has suffered some prejudice.

2. Company X is to reimburse EUR 500,000 to company A at a date when it can set off this obligation partially with a claim of EUR 200,000 it has against A. The contract between X and A contains a non-assignment clause. Disregarding that clause, A assigns its right to reimbursement to company B. X may claim damages against A for the costs it incurs in having to engage in a separate procedure to recover the sum of EUR 200,000.

3. Non-monetary rights

The assignment of rights to non-monetary performances does not have the same relationship to credit, thus justifying another solution which is to be found in paragraph (2). In order to achieve a fair balance between the conflicting interests of the three parties concerned, the rule is that non-assignment clauses are given effect vis-à-vis the assignee with the result that the assignment is ineffective. The solution is however reversed if it can be established that, at the time of the assignment, the assignee did not know and ought not to have known of the non-assignment clause. In such a case, the assignment is effective, but the assignor may be liable in damages to the obligor for non-performance of the contract under Chapter 7, Section 4.

Illustration

3. Company X has agreed to communicate to company A all improvements it will develop to a technical process over a period of time. Their contract stipulates that A’s rights towards X may not be assigned. A does not need the technology for itself any longer and attempts to assign its rights to company B. Such an assignment is ineffective. X does not become B’s obligor. In such a case, B has a claim against A under Article 9.1.15(b).

ARTICLE 9.1.10
(Notice to the obligor)

(1) Until the obligor receives a notice of the assignment from either the assignor or the assignee, it is discharged by paying the assignor.

(2) After the obligor receives such a notice, it is discharged only by paying the assignee.

COMMENT

1. Effect of notice on the obligor

Whereas the assignment is effective between the assignor and the assignee as a result of their agreement (see Article 9.1.7), the obligor will be discharged by paying the assignor until it receives notice of the assignment. If the obligor pays the assignor, the assignee can recover that payment from the assignor (see Article 9.1.15(f)). Only after the obligor receives a notice of assignment does the assignment become effective towards the obligor. The obligor can then be discharged only by paying the assignee.

I l l u s t r a t i o n s

1. Seller A assigns its right to payment from buyer X to bank B. Neither A nor B gives notice to X. When payment is due, X pays A. This payment is fully valid and X is discharged. It will be up to B to recover it from A under Article 9.1.15(f).

2. Seller A assigns to bank B its right to payment from buyer X. B immediately gives notice of the assignment to X. When payment is due, X still pays A. X is not discharged and B is entitled to oblige X to pay a second time.

Before the obligor receives a notice of the assignment, it is discharged when it pays the assignor irrespective of whether it knew, or ought to have known, of the assignment. The purpose is to place the burden of informing the obligor of the assignment on the parties to the assignment agreement, i.e. the assignor and the assignee. This solution is considered to be justified in the context of international commercial contracts. However, it does not necessarily exclude that in certain circumstances the obligor will be liable for damages if it acted in bad faith when it paid the assignor.

Parties sometimes resort to so-called “silent assignments”, where the assignor and the assignee agree not to inform the obligor of the assignment. This arrangement is valid between parties, but since the obligor receives no notice, it will be discharged by paying the assignor, as provided in Article 9.1.10(1).

2. Meaning of “notice”

“Notice” is to be understood in the broad sense of Article 1.10. Although this Article does not specify the content of the notice, the latter should indicate not only the fact of the assignment, but also the identity of the assignee, the specifications of the right transferred (subject to Article 9.1.6) and, in the case of partial assignment, the extent of the assignment.

3. Who should give notice

Article 9.1.10(1) leaves the question of who should give notice open, i.e. whether it should be the assignor or the assignee. In practice, it is probable that in most cases the assignee will take the initiative, as it has a major interest in avoiding that the obligor will perform in favour of the assignor notwithstanding the assignment. But notice given by the assignor has the same effect. When notice is given by the assignee, the obligor may request adequate proof of the assignment (see Article 9.1.12).

4. When must notice be given

This Article does not explicitly require notice to be given only after the assignment agreement has been concluded. In some cases the contract between a future assignor and the obligor will provide that the rights arising from it will be assigned to a financial institution. Whether this can be considered to be adequate notice having the consequences provided for in this Article is a matter of interpretation, and may possibly depend on the definiteness of the clause regarding the identity of the future assignee.

5. Revocation of notice

Notice given to the obligor can be revoked in certain circumstances, e.g. if the assignment agreement itself becomes invalid, or if an assignment made for security purposes is no longer necessary. This will not affect payments made before the revocation to the person who was the assignee at the time, but if the obligor pays that person after the revocation it would no longer be discharged.

ARTICLE 9.1.11
(Successive assignments)

If the same right has been assigned by the same assignor to two or more successive assignees, the obligor is discharged by paying according to the order in which the notices were received.

COMMENT

1. Priority of first notice

This Article deals with the case where the same assignor assigns the same right to different assignees. Normally this should not happen, although in practice it may occur, whether the assignor does so consciously or inadvertently. Preference is then given to the assignee who was the first to give notice. The other assignees can only claim against the assignor under Article 9.1.15(c) below.

Illustration

On 5 February seller A assigns its right to payment from buyer X to bank B, and then on 20 February to bank C. C notifies the assignment on 21 February, and B does so only on 25 February. X is discharged by paying C, even though the right was assigned to C after it had been assigned to B.

Unlike the solution prevailing under certain jurisdictions, this Article does not take into consideration the actual or constructive knowledge the obligor may have of the assignment(s) in the absence of notice. This approach is motivated by the wish to encourage the giving of notice, thus ensuring a degree of certainty that is especially advisable in the context of international contracts.

2. No notice given

If no notice is given by any of the successive assignees the obligor will be discharged by paying the assignor (see Article 9.1.10(1)).

3. Notice without adequate proof

Notice by an assignee without there being adequate proof that the assignment has been made, may be ineffective under Article 9.1.12.

ARTICLE 9.1.12
(Adequate proof of assignment)

(1) If notice of the assignment is given by the assignee, the obligor may request the assignee to provide within a reasonable time adequate proof that the assignment has been made.

(2) Until adequate proof is provided, the obligor may withhold payment.

(3) Unless adequate proof is provided, notice is not effective.

(4) Adequate proof includes, but is not limited to, any writing emanating from the assignor and indicating that the assignment has taken place.

COMMENT

Since receiving the notice of assignment has the important effects provided for in Articles 9.1.10 and 9.1.11, this Article intends to protect the obligor against the risk of receiving a fraudulent notice from a fake "assignee" by requiring adequate proof that the assignment has actually been made. Until adequate proof is provided, the obligor may withhold payment to the alleged assignee. If adequate proof is provided, notice is effective from the date it was provided.

Illustration

On 1 December purchaser X has to pay USD 200,000 to contractor A as an instalment of the sum due for the construction of a plant. In October A assigns the right to bank B. Either A or B may give notice of the assignment to X. If B takes the initiative and writes to X that it has become the assignee of the sum, X may require B to provide adequate proof. Without prejudice to other types of evidence, B will probably produce the assignment agreement or any other writing from A confirming that the right has been assigned. Until such adequate proof is provided, X may withhold payment.

ARTICLE 9.1.13
(Defences and rights of set-off)

(1) The obligor may assert against the assignee all defences that the obligor could assert against the assignor.

(2) The obligor may exercise against the assignee any right of set-off available to the obligor against the assignor up to the time notice of assignment was received.

COMMENT

1. Assertion of defences

A right can in principle be assigned without the obligor's consent (see Article 9.1.7(2)). This solution rests on the assumption that the assignment will not adversely affect the obligor's legal situation.

It can happen that the obligor would have been able to withhold or refuse payment to the original obligee on the basis of a defence such as the defective performance of that obligee's obligations vis-à-vis the obligor. To determine whether such defences can be asserted also against the assignee, the respective interests of the parties have to be weighed: the obligor's situation should not deteriorate as a result of the assignment, while the assignee has an interest in the integrity of the right it has acquired.

According to paragraph (1) of this Article, the obligor may assert against the assignee all the defences that it would have been able to assert if the claim had been made by the assignor. In this case, however, the assignee will have a claim against the assignor under Article 9.1.15(d).

Illustration

1. Software company A promises customer X to install a new accounting application before the end of the year. The main payment is to take place one month after completion. A immediately assigns the right to bank B. When the payment is due, B wants to claim it from X, but the latter explains that the new software is not working properly and that the accounting department is in chaos. X refuses to pay until this catastrophic situation has been remedied. X is justified in asserting this defence against B, which can then claim against A under Article 9.1.15(d).

The same solution applies to defences of a procedural nature.

Illustration

2. Company X sells a gas turbine to contractor A, to be incorporated into a plant built for customer B. When the work has been completed, A assigns the guarantee of satisfactory performance to B. When the turbine does not work properly, B sues X before a court at its place of business. X will successfully invoke the arbitration clause included in its contract with A.

2. Set-off

According to paragraph (2), the obligor may exercise against the assignee any right of set-off provided that the right of set-off was available to the obligor under Article 8.1 before the notice of the assignment was given.

This solution is in accord with the principle that the obligor's situation should not deteriorate as a result of the assignment. The assignee's interests are protected by the claim it may then have against the assignor under Article 9.1.15(e).

Illustration

3. Company A assigns to company B the right to the payment of EUR 100,000 that it has against company X. X however has a claim of EUR 60,000 against A. The two claims have not yet been set off by notice given under Article 8.3 of the Principles, but the required conditions for set-off were satisfied before the assignment was notified. X may still exercise its right of set-off by giving notice to the assignee. B can then only claim EUR 40,000 from X. B can recover the difference from A which had undertaken under Article 9.1.15(e) that the obligor would not give notice of set-off as regards the assigned right.

ARTICLE 9.1.14

(Rights related to the right assigned)

The assignment of a right transfers to the assignee:

(a) all the assignor's rights to payment or other performance under the contract in respect of the right assigned, and

(b) all rights securing performance of the right assigned.

COMMENT

1. Scope of the assignment

This provision is inspired by the same principle as Article 9.1.13. The assignment transfers the assignor's right as it is, not only with the defences the obligor may be able to assert, but also with all the rights to payment or to other performances under the contract in respect of the right assigned, and all rights securing performance of the right assigned.

Illustrations

1. Bank A is entitled to receive reimbursement of a loan of EUR 1,000,000 made to customer X, bearing interest at a rate of 3%. A assigns its right to reimbursement of the principal to bank B. The assignment also operates as a transfer of the right to interest and of the underlying security.

2. The initial facts are the same as in Illustration 1, but the loan contract entitles A to claim early repayment if X fails to pay the interest due. This right is also transferred to B.

3. The initial facts are the same as in Illustration 1, but X has deposited some shares as security to the benefit of A. This benefit is transferred to B, subject to the possible application of mandatory requirements of the otherwise applicable law under Article 1.4.

2. Partial assignment

When a right is partially assigned, if the rights covered by Article 9.1.14 are divisible they will be transferred in proportion. If they are not, parties should decide whether they are transferred to the assignee or whether they will remain with the assignor.

3. Contractual deviations

The rule laid down in paragraph (1) may however be modified by an agreement between the assignor and the assignee, who may stipulate, for instance, a separate assignment of interest.

4. Assignor's co-operation

It follows from the general duty to co-operate laid down in Article 5.1.3 that the assignor is obliged to take all the steps necessary to permit the assignee to enjoy the benefit of accessory rights and securities.

ARTICLE 9.1.15
(Undertakings of the assignor)

The assignor undertakes towards the assignee, except as otherwise disclosed to the assignee, that:

(a) the assigned right exists at the time of the assignment, unless the right is a future right;

(b) the assignor is entitled to assign the right;

(c) the right has not been previously assigned to another assignee, and it is free from any right or claim from a third party;

(d) the obligor does not have any defences;

(e) neither the obligor nor the assignor has given notice of set-off concerning the assigned right and will not give any such notice;

(f) the assignor will reimburse the assignee for any payment received from the obligor before notice of the assignment was given.

COMMENT

When assigning a right by agreement to the assignee, the assignor assumes several undertakings.

1. Existence of the right

The assigned right should exist at the time of the assignment. This would, for instance, not be the case if the payment had already been made or if the right to a payment had previously been avoided.

Illustration

1. Company A assigns a bundle of rights to factor B. When required to pay by B, customer X demonstrates that the amount due had been paid to A before the assignment. B has a claim against A, since at the time of the assignment the right no longer existed.

If, as permitted by Article 9.1.5, a future right is assigned, no such undertaking exists.

Illustration

2. Company A assigns to bank B the royalties from a technology licence that is to be granted in the near future to company X. The licence never materialises. B has no claim against A.

2. Assignor entitled to assign the right

The assignor is entitled to assign the right. This is, for instance, not the case if there is a legal or contractual prohibition to assign the right.

Illustration

3. Company X has agreed to communicate to company A all the improvements to a technical process that it will develop over a period of time. Their contract stipulates that A's rights towards X cannot be assigned. A no longer needs the technology itself, and attempts to assign its rights to company B. This illustration was already given above, under Article 9.1.9, to give an example of an ineffective assignment. In this case, B has a claim against A under Article 9.1.15(b). It will be recalled that the solution would be reversed, should B demonstrate that it neither knew nor ought to have known of the non-assignment clause.

3. No previous assignment, no third party rights or claims

If the assignor has already assigned a right to another assignee, it is generally not entitled to make a second assignment of that same right and this prohibition could be considered as already covered by the undertaking under sub-paragraph (b). The practical importance of this hypothesis is such that a separate and explicit provision is justified. It will however be recalled that under Article 9.1.11 the second assignee may prevail over the first one if it gives earlier notice to the obligee.

However, a previous assignment may have been made merely for security purposes. In this case, the right is still assignable, with proper disclosure to the second assignee.

4. No defence from the obligor

According to Article 9.1.13(1), the obligor may assert against the assignee all the defences that the obligor would have been able to assert against the assignor. In such a case, the assignee has a claim against the assignor on the basis of this undertaking.

Illustration

4. Bank B is the assignee of contractor A's right to payment of a certain sum from customer X. When payment is due, X refuses to pay arguing that A did not perform its obligations properly. Such defence can be successfully set up against B under Article 9.1.13(1). B would then have a claim against A.

5. No notice of set-off

The right of set-off may be exercised by the obligor against the assignee if it was available to the obligor before the notice of assignment was received (see Article 9.1.13(2)). The assignor undertakes vis-à-vis the assignee that neither the assignor nor the obligor has already given notice of set-off affecting the assigned right. The assignor also undertakes that such notice will not be given in the future. If, for instance, the obligor were to give such a notice to the assignee after the assignment, as permitted by Article 9.1.13(2), the assignee would have a claim against the assignor under Article 9.1.15(e).

6. Reimbursement of payment by the obligor

Article 9.1.10(1) provides that until it receives the notice of assignment the obligor is discharged by paying the assignor. This is the correct solution to protect the obligor, but the assignor and the assignee have agreed between themselves on the transfer of the right. The assignor therefore undertakes that it will reimburse the assignee for any payment it received from the obligor before the notice of assignment was given.

Illustration

5. Seller A assigns to bank B its right to payment from buyer X. Neither A nor B gives notice to X. When payment is due, X pays A. As already explained in the Comment on Article 9.1.10, this payment is fully valid and B is discharged. However, Article 9.1.15(f) enables B to recover the sum paid from A.

7. No undertaking concerning the obligor's performance or solvency

Parties to the assignment may certainly provide for an undertaking by the assignor concerning the obligor's present or future solvency, or, more generally, the obligor's performance of its obligations. However, without such an agreement, there is no such undertaking under this Article.

Illustration

6. Company B is the assignee of company A's right to payment of a certain sum from customer X. When payment is due, B finds out that X has become insolvent. B has to bear the consequences. The solution would be the same if B discovered that X was already insolvent at the time of the assignment.

In case of breach of one of the assignor's undertakings, the remedies provided for in Chapter 7 become available. The assignee may for instance claim damages from the assignor or terminate the agreement if the conditions of Article 7.3.1 *et seq.* are fulfilled.

8. Effect of disclosure on undertaking

Some of the assignor's undertakings may be affected by disclosures made at the time of the transfer. The assignor may for instance advise the assignee of the existence of a claim by a third party, in which case the assignee may accept the transfer of the right at its own risk, with no undertaking on that matter on the part of the assignor.

SECTION 2: TRANSFER OF OBLIGATIONS

ARTICLE 9.2.1
(Modes of transfer)

An obligation to pay money or render other performance may be transferred from one person (the "original obligor") to another person (the "new obligor") either

(a) by an agreement between the original obligor and the new obligor subject to Article 9.2.3, or

(b) by an agreement between the obligee and the new obligor, by which the new obligor assumes the obligation.

COMMENT

As is the case with the assignment of rights covered by Section 1 of this Chapter, also the transfer of obligations may serve useful economic purposes. For instance, if company A can claim payment from its customer B, but itself owes a similar amount to its supplier X, it may be practical to arrange for the customer to become the supplier's obligor.

Such a transfer of an obligation may occur in two different ways.

1. Transfer by agreement between the original obligor and the new obligor

In practice, the more frequent of the two ways indicated in this Article to transfer an obligation is by agreement between the original obligor and the new obligor, with the obligee's consent as required by Article 9.2.3.

Illustration

1. Company A owes its supplier X EUR 50,000, and customer B owes the same sum to A. A and B agree that the latter will take over the former's obligation towards X. The obligation is transferred if X agrees to the transaction.

2. Transfer by agreement between the obligee and the new obligor

Another possibility is an agreement between the obligee and the new obligor, by which the new obligor accepts to take over the obligation.

I l l u s t r a t i o n

> 2. The products of company X are sold by distributor A on a certain market. The contract between the parties is close to termination. Distributor B enters into negotiations with X, proposing to take over the distributorship. In order to gain X's acceptance, B promises that it will assume a debt of EUR 50,000 still owed by A to X, and X accepts. B has become X's obligor.

3. Obligee's consent necessary

In both cases, the obligee must give its consent to the transfer. This is obvious when the transfer occurs by agreement between the obligee and the new obligor. If it occurs by an agreement between the original obligor and the new obligor, the requirement is stated in Article 9.2.3. Consent may be given in advance under Article 9.2.4.

Without the obligee's consent, the obligor may agree with another person that the latter will perform the obligation under Article 9.2.6.

4. Transfer by agreement only

Only transfers by agreement are governed by this Section, as opposed to situations where the applicable law may provide for legal transfers (such as, under certain jurisdictions, the automatic transfer of obligations in the case of the merger of companies – see Article 9.2.2).

5. Obligations in respect of payment of money or other performance

This Section is not restricted to the transfer of obligations in respect of payment of money. It covers also the transfer of obligations relating to other kinds of performance, such as the rendering of a service. Nor are transferable obligations limited to obligations of a contractual nature. Obligations deriving from tort law or based on a judgment, for instance, can be governed by this Section, subject to Article 1.4.

6. What is meant by "transfer"

The "transfer" of an obligation means that it leaves the original obligor's assets to enter those of the new obligor.

However, in some cases although the new obligor becomes bound towards the obligee, the original obligor is not discharged (see Article 9.2.5).

ARTICLE 9.2.2
(Exclusion)

This Section does not apply to transfers of obligations made under the special rules governing transfers of obligations in the course of transferring a business.

COMMENT

The Articles contained in this Section do not apply to transfers of obligations made in the course of transferring a business under any special rules governing such transfers, as may happen in the case of the merger of companies. The applicable law often provides for mechanisms that cause all rights and obligations to be transferred under certain conditions in their entirety by operation of law.

Article 9.2.2 does not prevent this Section from applying when certain obligations pertaining to the transferred business are transferred individually.

Illustrations

1. Company A is transferred to company B. If the otherwise applicable law provides that all obligations pertaining to the former company are automatically transferred to the latter, the Principles do not apply.

2. The facts are the same as in Illustration 1, but B has reasons to prefer not to become the obligor of company X, one of A's suppliers. A can transfer the obligations concerned to company C, with the consent of X. This particular transfer is subject to the Principles.

ARTICLE 9.2.3
(Requirement of obligee's consent to transfer)

The transfer of an obligation by an agreement between the original obligor and the new obligor requires the consent of the obligee.

COMMENT

1. Agreement between the original and the new obligor

As stated in Article 9.2.1(a), the transfer of an obligation may occur by an agreement between the original obligor and the person who will become the new obligor.

2. Obligee's consent required

This agreement, however, does not suffice to transfer the obligation. It is also necessary for the obligee to give its consent.

This is different from the corresponding rule on the assignment of rights, where the operation is in principle effective without the consent of the obligor (see Article 9.1.7). The assignment of a right does not affect the obligor's situation, except that the obligor will have to deliver performance to another person. On the contrary, a change of obligor may considerably affect the obligee's position, as the new obligor may be less reliable than the original one. The change may therefore not be imposed on the obligee, who must consent to it.

I l l u s t r a t i o n

Company A owes USD 150,000 to company X, located in Asia, for services rendered. Due to a reorganisation of the group, A's activities in Asia are taken over by affiliate company B. A and B agree that B will take over A's debt towards X. The obligation is transferred only if X gives its consent.

3. Original obligor not necessarily discharged

With the obligee's consent, the new obligor becomes bound by the obligation. It does not necessarily follow that the original obligor is discharged (see Article 9.2.5).

4. Lack of consent by the obligee

If the obligee refuses to consent to the transfer, or if its consent is not solicited, an arrangement for a third party performance is possible under Article 9.2.6.

ARTICLE 9.2.4
(Advance consent of obligee)

(1) The obligee may give its consent in advance.

(2) If the obligee has given its consent in advance, the transfer of the obligation becomes effective when a notice of the transfer is given to the obligee or when the obligee acknowledges it.

COMMENT

1. Advance consent by the obligee

Paragraph (1) of this Article provides that the obligee's consent, required under Article 9.2.3, may be given in advance.

Illustration

1. Licensor X enters into a transfer of technology agreement with licensee A. For a period of ten years, A will have to pay royalties to X. When the contract is concluded, A envisages that at some time in the future it will prefer the royalties to be paid by its affiliate, company B. X may agree in advance in the contract to the obligation to pay the royalties being transferred by A to B.

2. When the transfer is effective as to the obligee

According to paragraph (2), if the obligee has given its consent in advance, the transfer of the obligation becomes effective when it is notified to the obligee or when the obligee acknowledges it. This means that it is sufficient for either the original or the new obligor to notify the obligee of the transfer when it occurs. Notification is not needed if it appears that the obligee has acknowledged the transfer, to which it had given its consent in advance. "Acknowledgement" means giving an overt sign of having become aware of the transfer.

Illustrations

2. The facts are the same as in Illustration 1, but there comes a time when A actually agrees with B that from then on the latter will take over the obligation to pay the royalties. This decision becomes effective when notice is given to X.

3. The facts are the same as in Illustration 1. No notice is given, but the first time B pays the yearly royalties, X writes to B to acknowledge receipt of the payment and to confirm that from then on it will expect B to pay the royalties. The transfer is effective with this acknowledgement.

ARTICLE 9.2.5
(Discharge of original obligor)

(1) The obligee may discharge the original obligor.

(2) The obligee may also retain the original obligor as an obligor in case the new obligor does not perform properly.

(3) Otherwise the original obligor and the new obligor are jointly and severally liable.

COMMENT

1. Extent of original obligor's discharge

The obligee's consent, whether given under Article 9.2.1(b) or under Article 9.2.3, has the effect of binding the new obligor to the obligation. What still remains to be determined is whether the original obligor is discharged. It is primarily up to the obligee to choose among different options. Only in the case of Article 9.2.1(b) will the choice depend also on the original obligor.

2. Obligee's choice: full discharge

The obligee may first of all fully discharge the original obligor.

Illustration

1. Supplier X accepts that its obligor company A transfer its obligation to pay the price to customer B. Fully confident that the new obligor is solvent and reliable, X discharges A. Should B fail to perform, the loss will be on X who will have no recourse against A.

3. Obligee's choice: original obligor retained as a subsidiary obligor

Another possibility is for the obligee to accept the transfer of the obligation from the original obligor to the new obligor on condition that it retain a claim against the original obligor.

There are two options.

The first option is that the original obligor is retained as an obligor in the event that the new obligor does not perform properly. In this case the obligee must claim performance first from the new obligor, but if the new obligor does not perform properly the obligee may call upon the original obligor.

I l l u s t r a t i o n

2. Supplier X accepts that its obligor company A transfer its obligation to pay the price to customer B, but this time stipulates that A will remain bound if B does not perform properly. X no longer has a direct claim against A, and must first request performance from B. However, should B fail to perform, X will have a claim against A.

4. Obligee's choice: original obligor and new obligor jointly and severally liable

The second option, the one most favourable to the obligee, is to consider the original obligor and the new obligor jointly and severally liable. This means that when performance is due, the obligee can exercise its claim against either the original or the new obligor (see Articles 11.1.3 *et seq.*). Should the obligee obtain performance from the original obligor, the latter would then have a claim against the new obligor (see Articles 11.1.10 *et seq.*).

I l l u s t r a t i o n

3. Supplier X accepts that its obligor company A transfer its obligation to pay the price to customer B, but stipulates that A and B will remain jointly and severally liable. In this case X may request performance from either A or B. Should B perform properly, both A and B would be fully discharged. Should A have to render performance to X, it would then have right of recourse against B.

5. Default rule

The language of this Article makes it clear that the last-mentioned option is the default rule. In other words, if the obligee has neither indicated that it intends to discharge the original obligor, nor indicated that it intends to keep the original obligor as a subsidiary obligor, the original obligor and the new obligor are jointly and severally liable.

Illustration

4. Supplier X accepts that its obligor company A transfer its obligation to pay the price to customer B, but says nothing about the liability of A. Also in this case X may request performance from either A or B. Should B perform properly, both the original and the new obligor would be fully discharged. Should A have to render performance to X, it would then have right of recourse against B.

6. Original obligor refusing to be discharged

When the obligation is assumed by means of an agreement between the obligee and the new obligor, as provided in Article 9.2.1(b), and the agreement provides that the original obligor is discharged, the agreement amounts to a contract in favour of a third party. Under Article 5.2.6 such a benefit cannot be imposed on the beneficiary, who may have reasons not to accept it. The original obligor may thus refuse to be discharged by the agreement between the obligee and the new obligor.

If such a refusal occurs, the new obligor is bound to the obligee, but the original obligor and the new obligor are jointly and severally liable, in accordance with the default rule of Article 9.2.5(3).

Illustration

5. The facts are the same as in Illustration 1, except that the obligation is assumed by an agreement between X and B, and that X discharges A. If A is no longer interested in a business relationship with B, it may accept to be discharged. On the other hand, if A wants to keep the possibilities it has of benefiting from a renewal of its contract with X, it might wish to keep the relationship and may therefore refuse to be discharged.

ARTICLE 9.2.6
(Third party performance)

(1) Without the obligee's consent, the obligor may contract with another person that this person will perform the obligation in place of the obligor, unless the obligation in the circumstances has an essentially personal character.

(2) The obligee retains its claim against the obligor.

COMMENT

1. Agreement on performance by another party

Obligations can be transferred either by an agreement between the original obligor and the new obligor, with the obligee's consent (see Article 9.2.1(a)), or by an agreement between the obligee and the new obligor (see Article 9.2.1(b)).

There may be situations in which the consent of the obligee is lacking, either because it has not been solicited, or because it has been refused. In such cases the obligor may agree with another person that this person will perform the obligation in its place. When performance becomes due, the other person will render it to the obligee.

While an obligee may refuse to accept a new obligor before performance is due, in principle it may not refuse to accept the performance itself when it is offered by another party.

Illustration

1. Companies A and B have entered into a co-operation agreement for their activities on a certain market. At a certain point they decide to redistribute some of their tasks. Thus, B will take over all operations concerning telecommunications which were previously A's responsibility. On the following 30 October A would have been bound to pay company X, a local operator, a sum of USD 100,000. The two partners agree that B will pay that amount when it is due. On 30 October X may not refuse such a payment made by B.

2. Obligation of an essentially personal character

Third party performances may not be refused by the obligee in all the cases in which they would be equally satisfactory as performances rendered by the obligor. The situation is different when the performance due is of an essentially personal character, linked to the obligor's specific qualifications. The obligee may then insist on receiving performance by the obligor itself.

Illustration

2. In Illustration 1, B also takes over operations for the maintenance of some sophisticated technological equipment developed by A and sold to company Y. The partners agree that the next yearly maintenance will be carried out by B. When B's technicians arrive at Y's premises, Y may refuse their intervention, invoking the fact that due to the highly technical nature of the

verifications involved, they are entitled to receive performance from the specialised staff of A.

ARTICLE 9.2.7
(Defences and rights of set-off)

(1) The new obligor may assert against the obligee all defences which the original obligor could assert against the obligee.

(2) The new obligor may not exercise against the obligee any right of set-off available to the original obligor against the obligee.

COMMENT

1. Assertion of defences

The obligation transferred to the new obligor is the very same obligation that used to bind the original obligor (and, in some cases, still binds it - see Article 9.2.5).

Whenever the original obligor would have been able to withhold or refuse payment to the obligee on the basis of a defence, such as the defective performance of the obligee's own obligations, the new obligor may rely on the same defence against the obligee.

Illustration

1. Company A owes company X EUR 200,000, due to be paid at the end of the year, as payment for facilities management services. With X's consent A transfers this obligation to company B. X renders A extremely defective services which would have given A a valid defence for refusing payment. When payment is due, B may assert the same defence against X.

2. Defences of a procedural nature

The same solution applies to defences of a procedural nature.

Illustration

2. The facts are the same as in Illustration 1, except that X sues B before a court at its place of business. B can successfully invoke the arbitration clause included in the contract between A and X.

3. Set-off

The right of set-off relating to an obligation owed by the obligee to the original obligor may however not be exercised by the new obligor. The reciprocity requirement is not fulfilled between the obligee and the new obligor. The original obligor may still exercise its right of set-off if it has not been discharged.

ARTICLE 9.2.8

(Rights related to the obligation transferred)

(1) The obligee may assert against the new obligor all its rights to payment or other performance under the contract in respect of the obligation transferred.

(2) If the original obligor is discharged under Article 9.2.5(1), a security granted by any person other than the new obligor for the performance of the obligation is discharged, unless that other person agrees that it should continue to be available to the obligee.

(3) Discharge of the original obligor also extends to any security of the original obligor given to the obligee for the performance of the obligation, unless the security is over an asset which is transferred as part of a transaction between the original obligor and the new obligor.

COMMENT

1. Scope of the transfer

The rules laid down in this Article are inspired by the same principle as Article 9.2.7. The obligation is transferred to the new obligor as it is, not only with the defences the original obligor was able to assert, but also with all the rights to payment or to other performances under the contract that the obligee had in respect of the obligation transferred.

The following illustrations provide examples of such rights.

Illustrations

1. Company A must reimburse bank X for a loan of EUR 1,000,000 bearing an interest rate of 3%. A transfers its obligation to reimburse the principal to company B. The transfer also includes the obligation to pay the 3% interest.

2. The facts are the same as in Illustration 1, except that the loan contract entitles X to claim premature reimbursement if A fails to pay the interest due. X can assert also this right against B.

2. Contractual deviations

Party autonomy permits deviations from the rules laid down in this Article, such as a separate transfer of the obligation to pay interest.

3. Securities in assignment of rights and transfer of obligations compared

In the case of the assignment of a right, all rights securing performance are automatically transferred to the assignee (see Article 9.1.14(b)). This solution is justified by the fact that the assignment of a right does not alter the obligor's situation, i.e. securities can continue to serve their purposes in unchanged circumstances.

The transfer of an obligation to a new obligor on the contrary modifies the context in which the security has been granted. If the original obligor is discharged, and if the security were to be transferred with the obligation, the risk of breach or insolvency to be covered would be that of another person, thus completely altering the object of the security.

4. Suretyship

If the original obligor's obligation was covered by a suretyship granted by another person, this suretyship can survive if the original obligor remains bound. If, on the other hand, the original obligor is discharged, the suretyship cannot be transferred to cover the new obligor, unless the person who granted the suretyship agrees that it should continue to be available to the obligee.

Illustration

3. Company A owes USD 1,000,000 to company X. Bank S has agreed to guarantee due performance of this obligation. With X's agreement, A transfers the obligation to company B, and X accepts to discharge A. S does not guarantee B's obligation, unless it agrees to continue to provide the security.

A special case occurs when the suretyship was granted by the person who was itself to become the new obligor. In such a case, the security necessarily disappears, since a person cannot provide a security for its own obligation.

5. Securities over assets

The original obligor may have given one of its assets as security. In this case, if the obligation is transferred and the original obligor is discharged, the security ceases to cover the obligation now binding the new obligor.

Illustration

4. Bank X has granted a loan of EUR 100,000 to company A, secured by a deposit of shares by the obligor. With X's agreement, A transfers the obligation to pay back the loan to company B, and X accepts to discharge A. The shares cease to serve as security.

The solution is different if the asset given as security is transferred as part of a transaction between the original and the new obligor.

Illustration

5. The facts are the same as in Illustration 4, but the transfer of the obligation between A and B occurs as part of a broader operation in which ownership of the shares is also transferred to B. In such a situation, the shares will continue to serve as security for B's obligation to reimburse the loan.

SECTION 3: ASSIGNMENT OF CONTRACTS

ARTICLE 9.3.1
(Definitions)

"Assignment of a contract" means the transfer by agreement from one person (the "assignor") to another person (the "assignee") of the assignor's rights and obligations arising out of a contract with another person (the "other party").

COMMENT

Rights and obligations can be transferred separately, under the respective rules of Sections 1 and 2 of this Chapter. In some cases, however, a contract is assigned as a whole. More precisely, a person transfers to another person all the rights and obligations deriving from its being a party to a contract. A contractor, for instance, may wish to let another contractor replace it as one of the parties in a construction contract. The Articles of this Section cover the assignment of contracts as defined in this Article.

Only transfers by agreement are concerned, as opposed to various situations where the applicable law may provide for legal transfers (such as, under certain jurisdictions, the automatic transfer of contracts in the case of the merger of companies - see Article 9.3.2).

ARTICLE 9.3.2
(Exclusion)

This Section does not apply to the assignment of contracts made under the special rules governing transfers of contracts in the course of transferring a business.

COMMENT

The assignment of contracts may be subject to special rules of the applicable law when it is made in the course of the transfer of a

business. Such special rules often provide for mechanisms that cause all contracts of the business to be transferred, under certain conditions, by operation of law.

This Article does not prevent the present Section from applying when certain contracts pertaining to the transferred business are assigned individually.

Illustrations

1. Company A is transferred to company B. If the otherwise applicable law provides that all contracts to which the former company was a party are automatically transferred to the latter, the Principles do not apply.

2. The facts are the same as in Illustration 1, but B is not interested in taking over a particular contract with company X, and prefers that contract to be assigned to company C. This particular transfer is subject to the Principles.

ARTICLE 9.3.3

(Requirement of consent of the other party)

The assignment of a contract requires the consent of the other party.

COMMENT

1. Agreement between assignor and assignee

The first requirement for the assignment of a contract is that the assignor and the assignee agree on the operation.

2. Other party’s consent required

This agreement does not however suffice to transfer the contract. It is also necessary for the other party to give its consent.

If it were only for the assignment of the rights involved, such a consent would in principle not be needed (see Article 9.1.7). However, the assignment of a contract also involves a transfer of obligations, which cannot be effective without the obligee’s consent (see Article 9.2.3). The assignment of a contract can thus only occur with the other party’s consent.

Illustration

Office space is let by owner X to company A. The contract expires only six years from the date of the contract. Due to the development of its business, A wants to move to larger premises. Company B would be interested in taking over the lease. The contract can be assigned by an agreement between A and B, but the operation also requires X's consent.

3. Assignor not necessarily discharged of its obligations

With the other party's consent, the assignee becomes bound by the assignor's obligations under the assigned contract. It does not necessarily follow that the assignor is discharged (see Article 9.3.5).

ARTICLE 9.3.4

(Advance consent of the other party)

(1) The other party may give its consent in advance.

(2) If the other party has given its consent in advance, the assignment of the contract becomes effective when a notice of the assignment is given to the other party or when the other party acknowledges it.

COMMENT

1. Advance consent by the other party

Paragraph (1) of this Article provides that the other party's consent, required under Article 9.3.3, may be given in advance.

This rule, concerning the assignment of contracts, corresponds to the rule in Article 9.2.4 according to which the obligee, who must consent to the transfer of the obligation may give its consent in advance. Similarly, the other party, who must consent to the assignment of the contract, may also give its consent in advance.

Illustration

1. Company X enters into an agreement with agency A, providing that the latter will be responsible for advertising X's products in country M for the next five years. A, however, is already

considering ceasing its activities in country M in the not too distant future, and obtains X's advance consent to the subsequent assignment of the contract to agency B, located in country M's capital. This advance consent is effective under Article 9.3.4.

2. When the assignment of the contract is effective vis-à-vis the other party

According to paragraph (2), if the other party has given its consent in advance, the assignment of the contract becomes effective when it is notified to the other party or when the other party acknowledges it. This means that it is sufficient for either the assignor or the assignee to notify the assignment when it occurs. Notification is not needed if it appears that the obligee has acknowledged the transfer, to which it had given its consent in advance. "Acknowledgement" means giving an overt sign of having become aware of the transfer.

Illustrations

2. The facts are the same as in Illustration 1. When A actually assigns its contract to B, the assignment becomes effective vis-à-vis the other party when either A or B notifies it to X.

3. The facts are the same as in Illustration 1. No notice is given, but B sends X a proposal for a new advertising campaign. X understands that the assignment has taken place and sends its comments on the proposal to B. The assignment of the contract is effective with this acknowledgement.

ARTICLE 9.3.5

(Discharge of the assignor)

(1) The other party may discharge the assignor.

(2) The other party may also retain the assignor as an obligor in case the assignee does not perform properly.

(3) Otherwise the assignor and the assignee are jointly and severally liable.

COMMENT

1. Extent of assignor's discharge

This Article, concerning the assignment of contracts, corresponds to Article 9.2.5. To the extent that the assignment of a contract causes obligations to be transferred from the assignor to the assignee, the other party, as an obligee, may decide the effect that the acceptance of the assignee as a new obligor will have on the assignor's obligations. This Article gives the other party several choices and provides for a default rule.

2. Other party's choice: full discharge

The other party may first of all fully discharge the assignor.

Illustration

1. By contract with company X, company A has undertaken to dispose of the waste produced by an industrial process. At a certain point, X accepts that the contract is assigned by A to company B. Fully confident that B is solvent and reliable, X discharges A. Should B fail to perform properly, X will have no recourse against A.

3. Other party's choice: assignor retained as a subsidiary obligor

Another possibility is for the other party to accept the assignment of the contract on condition that it retain a claim against the assignor.

There are two options.

The first option is that the assignor is retained as an obligor in the event that the assignee does not perform properly. In this case the other party must necessarily claim performance first from the assignee, but if the assignee does not perform properly, the other party may call upon the assignor.

Illustration

2. The facts are the same as in Illustration 1, except that X, when consenting to the assignment, has stipulated that A will remain bound if B does not perform properly. X no longer has a direct claim against A, and must first request performance from B. However, should B fail to perform, then X would have a claim against A.

4. Other party's choice: assignor retained as jointly and severally liable with the assignee

The second option, the one most favourable to the other party, is to consider the assignor and the assignee jointly and severally liable. This means that when performance is due, the other party can exercise its claim against either the assignor or the assignee (see Articles 11.1.3 *et seq.*). Should the other party obtain performance from the assignor, the latter would then have a claim against the assignee (see Articles 11.1.10 *et seq.*).

Illustration

> 3. Company X accepts that company A assign the contract to company B, but stipulates that A and B will remain jointly and severally liable. In this case X may require performance from either A or B. Should B perform properly, both A and B would be fully discharged. Should A have to render performance to X, it would then have a right of recourse against B.

5. Default rule

The language of this Article makes it clear that the last-mentioned option is the default rule. In other words, if the other party has neither indicated that it intends to discharge the assignor, nor indicated that it intends to keep the assignor as a subsidiary obligor, the assignor and the assignee are jointly and severally liable.

Illustration

> 4. Company X accepts that company A assign the contract to company B, but says nothing about the liability of A. Also in this case X may request performance from either A or B. Should B perform properly, both A and B would be fully discharged. Should A have to render performance to X, it would then have a right of recourse against B.

6. Differentiated options possible

A party to a contract is often subject to a whole set of obligations. When the contract is assigned, the other party may choose to exercise different options with regard to the different obligations. The other party may for instance accept to discharge the assignor for a certain obligation, but to retain it either as a subsidiary obligor or to consider it jointly and severally liable with the assignee with respect to other obligations.

Illustration

5. Company A has entered into a know-how licence contract with company X. In return for the transferred technology, A has undertaken to pay royalties and to co-operate with X in the development of a new product. When X later on accepts that A assign the contract to company B, X discharges A from the obligation to participate in the joint research, for which it will deal with the assignee only, but retains A as a subsidiary or a jointly and severally liable with B for the payment of royalties.

ARTICLE 9.3.6
(Defences and rights of set-off)

(1) To the extent that the assignment of a contract involves an assignment of rights, Article 9.1.13 applies accordingly.

(2) To the extent that the assignment of a contract involves a transfer of obligations, Article 9.2.7 applies accordingly.

COMMENT

The assignment of a contract entails both an assignment of the original rights and a transfer of the original obligations from the assignor to the assignee. The transaction should not adversely affect the other party's situation as an obligor and it should put the assignee in the same situation as the assignor in its capacity as obligor.

As a consequence, the provisions concerning defences in Sections 1 and 2 of this Chapter apply accordingly. When the assignee exercises its rights, the other party may assert all the defences it could have asserted as obligor if the claim had been made by the assignor (see Article 9.1.13). When the other party exercises its rights, the assignee may assert all the defences that the assignor could have asserted as obligor if the claim had been made against it (see Article 9.2.7)

Illustrations

1. Company X has out-sourced its risk management department to consultant A. With X's consent, the contract is assigned to consultant B. Due to A's incompetence, X was not properly insured for a loss it subsequently suffered. Pending indemnification, X may suspend paying B the agreed fees.

2. Airline A has a contract with catering company X. A transfers the operation of its flights to certain destinations to airline B. With X's consent, the catering contract is assigned by A to B. Litigation later arises, and X sues B before a court at its place of business. As a procedural defence B may successfully invoke that the assigned contract includes an arbitration clause.

ARTICLE 9.3.7

(Rights transferred with the contract)

(1) To the extent that the assignment of a contract involves an assignment of rights, Article 9.1.14 applies accordingly.

(2) To the extent that the assignment of a contract involves a transfer of obligations, Article 9.2.8 applies accordingly.

COMMENT

The assignment of a contract entails both an assignment of the original rights and a transfer of the original obligations from the assignor to the assignee. In parallel to what has been said about defences under Article 9.3.6, the operation should not adversely affect the other party's situation as an obligee and it should place the assignee in the same situation as the assignor in its capacity as obligee.

As a consequence, the provisions of Sections 1 and 2 of this Chapter concerning rights related to the claim assigned and to the obligation transferred will apply accordingly.

When the assignee acts against the other party, it may assert all the rights to payment or other performances under the contract assigned with respect to the rights assigned, as well as all rights securing such performance (see Article 9.1.14). When the other party exercises its rights, it may assert all its rights to payment or other performances under the contract with respect to the obligation transferred against the assignee (see Article 9.2.8(1)). Securities granted for the performance of the assignor's obligations are maintained or discharged in accordance with Article 9.2.8(2) and (3).

Illustrations

1. A service contract provides that late payment of the yearly fees due by customer X to supplier A will bear interest at the rate of 10%. With X's consent, A assigns the contract to supplier B. When X fails to pay the yearly fees on time, B is entitled to claim such interest (see Article 9.1.14(a)).

2. The facts are the same as in Illustration 1, but X has also provided A with a bank guarantee covering payment of the fees. B may call upon that guarantee should X fail to pay the fees (see Article 9.1.14(b)).

3. Company X has ordered the construction and installation of industrial equipment from company A. Performance levels have been agreed between the parties, and the contract provides for liquidated damages should actual performance be insufficient. With X's consent, A assigns the contract to company B. The assignee delivers equipment that does not meet the required performance levels. X may avail itself of the liquidated damages against B (see Article 9.2.8(1)).

4. The facts are the same as in Illustration 3, but A has provided X with a bank guarantee covering satisfactory performance. The bank guarantee will not apply to B's obligations resulting from the assignment, unless the bank accepts to continue to offer its guarantee in respect of the assignee's obligations (see Article 9.2.8(2)).

LEGAL AUTHORITY AA-37

KeyCite Yellow Flag - Negative Treatment
Disagreed With by Re/Max Intern. v. Realty One, Inc., N.D.Ohio, May 10, 1995

7 F.3d 986
United States Court of Appeals,
Eleventh Circuit.

U.S. ANCHOR MFG., INC., Plaintiff, Counterclaim defendant, Appellee, Cross–Appellant,
v.
RULE INDUSTRIES, INC., Defendant–Appellant, Cross–Appellee,
Tie Down, Inc., a/k/a Tie Down Engineering, Inc., Defendant, Counterclaim plaintiff, Appellant, Cross–Appellee,
William Chapman, Counterclaim defendant.

No. 91–8854.
|
Nov. 23, 1993.

Synopsis

Anchor manufacturer brought action against competitor and distributor alleging violation of antitrust law and tortious interference with business relationships in violation of Georgia law. The United States District Court for the Northern District of Georgia, No. 1:86–cv–2447–JTC, Jack T. Camp, J., imposed civil liability for alleged predatory pricing. Defendants appealed. The Court of Appeals, Dubina, Circuit Judge, held that: (1) defendants could not be held liable for antitrust violations in the absence of showing that they had dangerous probability of success in monopolization; (2) distributor could not be held liable for conspiracy; and (3) pendent jurisdiction would be exercised over Georgia claim.

Reversed and rendered in part and questions certified.

Procedural Posture(s): On Appeal.

Attorneys and Law Firms

***989** Harold T. Daniel, Jr., Laurie Webb Daniel, Webb & Daniel, Atlanta, GA, for Tie Down, Inc.

Charles M. Shaffer, Jr., J. Kevin Buster, Sean R. Smith, Atlanta, GA, for Rule Industries, Inc.

J. Alexander Porter, Simuel F. Doster, Jr., Porter & Barrett, Atlanta, GA, for U.S. Anchor Mfg., Inc.

Appeals from the United States District Court for the Northern District of Georgia.

Before COX and DUBINA, Circuit Judges, and GODBOLD, Senior Circuit Judge.

Opinion

DUBINA, Circuit Judge:

This is an appeal from a jury verdict imposing civil liability for alleged predatory pricing in violation of the antitrust laws. More specifically, appellants Rule Industries, Inc. ("Rule") and Tie Down Engineering, Inc. ("Tie Down"), defendants below, appeal the district court's denial of their motions for judgment notwithstanding the verdict on claims by U.S. Anchor Manufacturing, Inc. ("U.S. Anchor") that Rule and Tie Down attempted and conspired to monopolize the United States market for light weight fluke-style anchors for small boats by means of below-cost pricing intended to drive out competition. U.S. Anchor cross-appeals the district court's order of a directed verdict on its state law claims arising from the same allegations. We reverse the denial of defendants' motions concerning the federal claims. With respect to the state law claims, we certify the dispositive issues for authoritative resolution by the Supreme Court of Georgia.

I. FACTS

This case involves several manufacturers and suppliers of light weight anchors for ultimate retail purchase by owners of recreational boats and small commercial fishing craft. As the district court observed in denying cross-motions for summary judgment,

> [a]nchors and other marine industry products are generally sold by suppliers to wholesale distributors, who in turn sell the anchors to boat dealers, marinas, and other retailers for ultimate resale to the consumer, the boat owner. The supplier may either manufacture its own anchors, as does U.S. Anchor, or purchase them from another domestic manufacturer,

as [Rule] does from Tie Down, or import them from abroad.

U.S. Anchor Mfg. v. Rule Indus., 717 F.Supp. 1565, 1568 (N.D.Ga.1989).

Within the general category of fluke anchors are four distinct product groups recognized in the industry: (1) expensive premium anchors, (2) the "Danforth Standard" brand line of anchors sold only by Rule, (3) so-called "generic" versions of the Danforth Standard, and (4) inexpensive economy anchors used primarily for lake boating.

Rule is a diversified Massachusetts firm that sells an assortment of marine, hardware and automotive products to wholesale distributors. It entered the fluke anchor industry in 1983 when it obtained the rights to sell the Danforth brand line of anchors. Prior to 1985, Danforth anchors were manufactured for Rule exclusively by the Jacquith Company ("Jacquith") in New York. Tie Down is a smaller manufacturing firm in Georgia that began selling generic and economy fluke anchors in the late 1970s under the "Hooker" brand name. In May 1985 Rule obtained the Hooker trademark and the exclusive right to purchase and distribute Tie Down's anchor production in a transaction that U.S. Anchor has characterized as a "merger." After it sold the right to market its own anchors, Tie ***990** Down agreed to manufacture both generic/economy and Danforth brand anchors for Rule. Tie Down's only role in the fluke anchor industry since 1985 has been as one of Rule's suppliers.

U.S. Anchor is a Georgia company founded in 1985 by William Chapman ("Chapman"), the immediate past president of Tie Down whose responsibilities there had recently ended. U.S. Anchor both manufactures and distributes generic and economy fluke anchors under the "Sentinel" brand name. Between August 1985 when it first sent out price lists and December 31, 1990, its market share increased to between 45 and 68%, depending on how the relevant product market is defined and measured.

Shortly after U.S. Anchor entered the market in August 1985, on the eve of the 1985–86 marine products season, [1] Rule and U.S. Anchor engaged in a price war. Following publication of U.S. Anchor's August price list, Rule published prices in September that were approximately 11 to 18% higher than U.S. Anchor's. Thus, U.S. Anchor's prices were 10 to 15% lower than Rule's. (R30–27; *compare* USTX 343 *with* USTX 345.) [2] In October, after U.S. Anchor had received substantial orders from Rule customers, Rule cut its prices by 20%, *i.e.,* to levels 6 to 12% below U.S. Anchor's August prices. (R49–28; RTX 584.) U.S. Anchor then matched Rule's October prices. In a written report to Rule, USTX 683, Tie Down's president Charles MacKarvich ("MacKarvich") estimated U.S. Anchor's costs of production and hypothetical projected sales for a twelve-month period. He theorized that if Rule lowered its prices further and offered extended credit terms to customers, U.S. Anchor would be forced to adopt even more attractive terms in order to compete. From his estimates of cash flow and net revenue derived from these cost and sales projections, he predicted that such terms would subject U.S. Anchor to a negative cash flow and an actual net loss over the 1985–86 marketing year. Rule implemented price reductions consistent with MacKarvich's report in November 1985. In December, U.S. Anchor merely matched Rule's prices and did not attempt to undercut them. (R30–39–40, USTX 351, 353, 543.) U.S. Anchor contends that Rule's first price cut in October was predatory and that all subsequent sales at or below that level were also predatory.

After the pricing conduct at issue in this case began, distributors' prices for generic brands in the smaller, popular sizes ranged between $3 and $14 depending on weight, and prices for Danforths were spread 50 to 96% higher. [3] Among the more expensive, larger anchors the spread between Danforth and generic brands was even greater. Excluding premium anchors, [4] annual unit sales of fluke anchors in the United States during the time relevant to this case has varied from 232,000 to 347,000. (USTX 479.)

At trial the parties noted differing possible measures of Rule's share of the relevant product market after the acquisition of Tie Down's anchor line in May 1985, four months before the close of the 1984–85 marine season at the end of August. This dispute encompassed two aspects of market share: whether to define the product market as including the high priced Danforth anchors or only the less expensive generic and economy models, and whether to measure market shares in terms of unit sales or dollar revenues. Including the Danforth line and measuring market shares in revenue, U.S. Anchor asserts that Rule and Tie Down together ***991** controlled 90.5% of the fluke anchor market during the 1984–85 season, the last year before Rule's alleged predation began and the last year before the merger with Tie Down, and that Rule possessed 60.0% of the market during the 1985–86 selling year. (USTX 467.) Using Rule's most favorable calculation, which measures share in units and excludes Danforths from

the market, Rule contends that the combined Rule/Tie Down market share in 1984–85 was only 61.5%, (RTX 674), and that Rule's aggregate 1985–86 share was 30.1%, (*id.;* RTX 675 at 1).[5] Rule also submitted evidence that its 1985–86 unit market share, including Danforths, was 43.1%. (RTX 675 at 1.) Notably, all of these figures encompass an entire season and none of them attempts to pinpoint Rule's share at the exact date when the alleged predation began in October 1985, several months after U.S. Anchor entered the market. The evidence shows, and the parties agree, that the Rule/Tie Down market share consistently decreased after August 1985 when U.S. Anchor first began to solicit orders. The parties also agree that the relevant geographic market was the United States.

II. PROCEDURAL HISTORY

In November 1985 Rule filed suit against U.S. Anchor for various violations of state and federal law not involving predatory pricing. The suit was settled on March 19, 1986, when U.S. Anchor and Rule executed an agreement releasing each other from liability for all events occurring prior to the date of the release. Tie Down was a party to neither the litigation nor the ensuing release.

On November 13, 1986, U.S. Anchor sued Rule and Tie Down, alleging that Rule had attempted to monopolize the fluke anchor market in violation of section 2 of the Sherman Act[6] beginning in October 1985 by engaging in predatory pricing. U.S. Anchor also alleged that Rule and Tie Down had conspired to restrain trade in violation of section 1 of the Sherman Act[7] and conspired to attain a monopoly in violation of section 2, by agreeing to charge predatory prices, also beginning in October 1985. U.S. Anchor also asserted an illegal tying arrangement by Rule, whereby its newly patented and supposedly revolutionary "Deepset" anchors allegedly were sold only to distributors who abstained from buying generic fluke anchors from suppliers other than Rule, in violation of section 1 of the Sherman Act and section 3 of the Clayton Act, as amended by the Robinson–Patman Act.[8] U.S. Anchor further alleged that Rule and Tie Down had conspired to restrain trade in violation of Georgia law.

***992** The district court denied the parties' cross-motions for summary judgment. 717 F.Supp. 1565. A jury trial followed during which the defendants moved for directed verdicts[9] as to all claims. The court granted their motions on the state law claims because it concluded that Georgia law did not permit damages to be recovered for a conspiracy in restraint of trade. The jury found Rule solely liable for attempted monopolization and jointly liable with Tie Down on both conspiracy counts. The verdict exonerated Rule of illegal tying. (R10–321.) The jury set damages for each of the three violations at $1,638,028, which the court trebled to $4,914,084. Tie Down and Rule both moved for judgment notwithstanding the verdict on liability and for a new trial on the issue of damages. (R11–348, 349.) The district court denied these motions, awarded U.S. Anchor statutory attorney fees in the stipulated amount of $800,000 and entered judgment accordingly. (R14–382.) Rule and Tie Down appealed, and U.S. Anchor cross-appealed with respect to the state law tort claims. U.S. Anchor does not appeal the judgment on the tying claim.

III. CONTENTIONS OF THE PARTIES

Rule contends that it engaged in no predatory conduct and disputes U.S. Anchor's showing of Rule's and Tie Down's costs of producing the anchors. Since a predatory pricing claim requires proof that defendants attempted or conspired to drive a competitor out of the relevant market by "pricing below some appropriate measure of cost," the issue of which costs to count may be vital. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.,* 475 U.S. 574, 585 n. 8, 106 S.Ct. 1348, 1355 n. 8, 89 L.Ed.2d 538 (1986) (noting but not resolving debate over which costs are "relevant"), *on remand, In re Japanese Elec. Prods. Antitrust Litig.,* 807 F.2d 44 (3d Cir.1986), *cert. denied,* 481 U.S. 1029, 107 S.Ct. 1955, 95 L.Ed.2d 527 (1987). Rule advances numerous criticisms of U.S. Anchor's expert testimony on this point. Tie Down contends that U.S. Anchor failed to adduce any evidence that Tie Down's prices to Rule were below Tie Down's cost, that Tie Down had any knowledge of (or control over) Rule's other costs, or that it had any control over Rule's prices.

Rule also contends that it had no dangerous probability of successfully achieving a monopoly. The parties first dispute the existence of barriers to entry in the relevant market. Rule and Tie Down contend that without high barriers, a successful monopolist would not have been able to recoup the foregone profits inherent in below-cost pricing by charging supra-competitive prices following the end of the victim's competitive presence.[10] U.S. Anchor contends that there was sufficient evidence of entry barriers to permit the jury to find them and that in any case actual recoupment is not

required as a matter of law before the jury may find an attempt or conspiracy to monopolize. Second, Rule points to U.S. Anchor's own success and Rule's declining fortunes in the anchor market as evidence that it could not have monopolized.

Rule and Tie Down also challenge the sufficiency of the evidence of unlawful conspiracy. The parties dispute the inference to be drawn from plaintiff's exhibit 683, the MacKarvich market report. U.S. Anchor contends that MacKarvich was proposing to drive the new entrant from the marketplace. Defendants offered expert testimony, corroborated by MacKarvich himself, that studies ***993** of competitors' costs and revenues are common in competitive industries and that a projected loss after the first year of operation is ordinarily not enough to drive any new entrant from the market, since start-up companies must generally expect early losses. In its cross-appeal U.S. Anchor challenges the district court's exclusion of certain evidence that allegedly supports the existence of a conspiracy.

Rule and Tie Down challenge the sufficiency of U.S. Anchor's proof concerning damages. They argue that at least some of their price cuts were instituted to meet competition from foreign fluke anchor manufacturers and any loss of sales by U.S. Anchor resulting from such reductions is not antitrust injury. Moreover, they contend, the base price from which U.S. Anchor's revenue losses were calculated should have reflected competitive levels as shown by Rule's and U.S. Anchor's early, allegedly non-predatory reductions rather than prices prevailing before U.S. Anchor's entry into the market.

Rule and U.S. Anchor dispute the scope and effect of their settlement agreement in the prior litigation. Rule contends that liability for all predatory sales before the date of the release was discharged. Moreover, Rule maintains that the alleged predatory scheme was ongoing at the time the contract was executed and therefore all post-release liability was discharged as well. U.S. Anchor contends that a general release is ineffective to discharge undiscovered antitrust liability as a matter of law and, moreover, that post-release damages were not waived. We do not reach this dispute as it applies to the federal antitrust claims.[11] As applied to the state law claims, we certify the question, along with the substantive issues of Georgia law, for resolution by the Supreme Court of Georgia.

In its cross-appeal U.S. Anchor also argues that the district court should not have granted a directed verdict on its state law claims because Georgia law allows private damage actions for conspiracies in restraint of trade. Rule and Tie Down disagree with U.S. Anchor's interpretation of Georgia law.

IV. STANDARD OF REVIEW

We review rulings on motions for judgment as a matter of law by applying de novo the same legal standards used by the district court. *Miles v. Tennessee River Pulp & Paper Co.,* 862 F.2d 1525, 1528 (11th Cir.1989). Both courts consider all the evidence, but all reasonable inferences must be drawn in the nonmovant's favor. If the jury verdict is supported by substantial evidence—that is, enough evidence that reasonable minds could differ concerning material facts—the motion should be denied. A mere scintilla of evidence in the entire record, however, is insufficient to support a verdict. *See Hessen ex rel. Allstate Ins. Co. v. Jaguar Cars, Inc.,* 915 F.2d 641, 644 (11th Cir.1990). Denial of a motion for a new trial is reviewed for clear abuse of discretion. *Id.* at 644–45. A district court's evidentiary rulings are not disturbed unless there is a clear showing of abuse of discretion. *Id.* at 645.

V. ATTEMPTED MONOPOLIZATION

There are three essential elements of a claim alleging attempted monopolization under section 2 of the Sherman Act. First, the plaintiff must show that the defendant possessed the specific intent to achieve monopoly power by predatory or exclusionary conduct. Second, the defendant must in fact commit such anticompetitive conduct. Third, there must have existed a dangerous probability that the defendant might have succeeded in its attempt to achieve monopoly power. *Spectrum Sports, Inc. v. McQuillan,* 506 U.S. 447, ——, 113 S.Ct. 884, 890, 122 L.Ed.2d 247 (1993); *see McGahee v. Northern Propane Gas Co.,* 858 F.2d 1487, 1493 (11th Cir.1988), *cert. denied,* 490 U.S. 1084, 109 S.Ct. 2110, 104 L.Ed.2d 670 (1989); 3 Phillip Areeda & Donald F. Turner, *Antitrust Law* ¶ 820 at 312 (1978) [hereinafter Areeda & Turner, *Antitrust Law*]. We address these elements in reverse order.

***994** A. *Dangerous Probability of Success*

To have a dangerous probability of successfully monopolizing a market the defendant must be close to achieving monopoly power.[12] Monopoly power is "the power to raise prices to supra-competitive levels or ... the

power to exclude competition in the relevant market either by restricting entry of new competitors or by driving existing competitors out of the market." *American Key Corp. v. Cole Nat'l Corp.,* 762 F.2d 1569, 1581 (11th Cir.1985). Most attempts to measure monopoly power involve quantifying the degree of concentration in a relevant market and/or the extent of a particular firm's ability to control productive capacity in that market. In analyzing attempted monopolization's dangerous probability of success element, the estimate of market power is necessarily speculative to some extent because it requires an evaluation of future behavior by market participants, viewed at the time the alleged attempt began. We are not without guideposts, however.

> Relevant determinants of the market power of a prospective predator in this regard include its absolute and relative market shares, and those of competing firms; the strength and capacity of current competitors; the potential for entry; the historic intensity of competition; and the impact of the legal or natural environment.
>
> *International Tel. & Tel. Corp.,* 104 F.T.C. 208, 412 (1984) (citation and footnotes omitted). Despite the seemingly broad array of factors employed by the Federal Trade Commission, the principal judicial device for measuring actual or potential market power remains market share, typically measured in terms of a percentage of total market sales. Thus, at the outset the appropriate market must be defined or identified. [13]

Defining the market is a necessary step in any analysis of market power and thus an indispensable element in the consideration of any monopolization or attempt case arising under section 2. *Walker Process Equip., Inc. v. Food Mach. & Chem. Corp.,* 382 U.S. 172, 177, 86 S.Ct. 347, 350, 15 L.Ed.2d 247 (1965); *American Key,* 762 F.2d at 1579. Although the issue is fully developed in the fact section of Rule's brief, the argument section does not address the precise question of market definition. U.S. Anchor, in the fact section of its brief, contends that the question of market definition is not appropriately before us because Rule does not argue the point. (U.S. Anchor's Br. at 3 n. 1.) We must consider the question nevertheless before passing on the legal significance of evidence concerning Rule's potential market power. As the issue of Rule's dangerous probability of success has been preserved through argument, the subsidiary question of market definition is also preserved because it is set forth fully in the fact section of Rule's brief. [14] The issue was fully argued before the district court. [15]

The definition of the relevant market is essentially a factual question, so the precise issue we first must address is whether U.S. Anchor introduced sufficient evidence to raise a jury question on the inclusion of Danforths. *See, e.g., Yoder Bros. v. California–Florida* ***995** *Plant Corp.,* 537 F.2d 1347, 1366 (5th Cir.1976), *cert. denied,* 429 U.S. 1094, 97 S.Ct. 1108, 51 L.Ed.2d 540 (1977). [16]

1. Defining the Market

"Defining a relevant product market is primarily 'a process of describing those groups of producers which, because of the similarity of their products, have the ability—actual or potential—to take significant amounts of business away from each other.' " *General Indus. Corp. v. Hartz Mountain Corp.,* 810 F.2d 795, 805 (8th Cir.1987) (quoting *SmithKline Corp. v. Eli Lilly & Co.,* 575 F.2d 1056, 1063 (3d Cir.), *cert. denied,* 439 U.S. 838, 99 S.Ct. 123, 58 L.Ed.2d 134 (1978)). The reasonable interchangeability of use or the cross-elasticity of demand [17] between a product and its substitutes constitutes the outer boundaries of a product market for antitrust purposes. *Brown Shoe Co. v. United States,* 370 U.S. 294, 325, 82 S.Ct. 1502, 1523, 8 L.Ed.2d 510 (1962).

> [W]ithin this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.... The cross-elasticity of production facilities may also be an important factor in defining a product market....
>
> *Id.* at 325 & n. 42, 82 S.Ct. at 1523–24 & n. 42 (citations and footnotes omitted). As the Supreme Court's language itself suggests, defining a "submarket" is the equivalent of defining a relevant product market for antitrust purposes. *International Telephone & Telegraph* adequately summarizes our view of the relevant proof:
>
> > Reliable measures of supply and demand elasticities provide the most accurate estimates of relevant markets. However, it is ordinarily quite difficult to measure cross-elasticities of supply and demand accurately. Therefore, it is usually necessary to consider other factors that can serve as useful surrogates for cross-elasticity data.... In

the case of product market definition, these factors may include

> whether the products and services have sufficiently distinctive uses and characteristics; whether industry firms routinely monitor each other's actions and calculate and adjust their own prices (at least in part) on the basis of other firms' prices; the extent to which consumers consider various categories of sellers ... as substitutes; and whether a sizeable price disparity between different types of ... sellers ... persists over time for equivalent amounts of comparable goods and services.

104 F.T.C. at 409 (quoting *Grand Union Co.,* 102 F.T.C. 812, 1041 (1983)) (footnotes omitted).

We note that Danforth brand anchors are functionally interchangeable with their equivalent counterparts among the generic brands. Indeed, among smaller sized anchors the Hooker and Danforth anchors have always been virtually identical. (R30–131–33; R33–129–31.) This interchangeability suggests a likelihood that consumers of generic brands would willingly switch to Danforths in the event of significant price increases among generics. Similarly, Danforth customers might switch to generic brands if Rule implemented a significant increase in the price of Danforths. The likelihood of demand substitution, if proven, weighs strongly in favor of including the two categories of product within a single market for antitrust analysis. This is so because the very purpose of defining the relevant market under section 2 is to determine whether a monopolist, cartel or oligopoly in that market would be able to reduce marketwide output simply by cutting its own output, and thereby ***996** raise marketwide prices above competitive levels. *United States v. E.I. du Pont de Nemours & Co. (The Cellophane Case),* 351 U.S. 377, 395, 76 S.Ct. 994, 1007, 100 L.Ed. 1264 (1956); *Satellite Television & Associated Resources, Inc. v. Continental Cablevision, Inc.,* 714 F.2d 351, 356 (4th Cir.1983), *cert. denied,* 465 U.S. 1027, 104 S.Ct. 1285, 79 L.Ed.2d 688 (1984).[18]

We hold, however, that the relevant market in this case constituted light weight generic and economy fluke anchors. Four of the *Brown Shoe* factors weigh strongly in favor of excluding Danforths from the relevant market: distinctly higher prices, a distinct group of customers, strongly inelastic demand and limited substitution of supply. Moreover, the higher prices charged for Danforths are evidence that a distinct group of customers was unwilling to switch away from the prestigious branded product in response to price increases above competitive levels. The fact that this group remained loyal to Danforths despite prices 50 to 96% and more above prices for functionally interchangeable alternative products shows inelastic demand and limited demand interdependence. More importantly, U.S. Anchor showed no reasonable possibility that a significant number of consumers would have switched to Danforths, many of which were offered at nearly double the price of their generic substitutes, in response to more modest increases in generic prices. And as more fully discussed below, there is no evidence that Rule had (or would have) varied its output of Danforths in response to price changes in the broader market. We hold, therefore, that the record provides no support for finding significant cross-elasticity of demand or supply between Danforths and generic anchors.

First, U.S. Anchor's evidence was insufficient for a reasonable juror to conclude that there was a significant cross-elasticity of demand. U.S. Anchor's evidence demonstrated that an increase in the spread between prices for Danforths and other anchors had coincided with lower sales of Danforths. During the period from September 1985 until August 1990, sales of Danforths fell by 61.5% while the spread between the prices of Danforths and other anchors increased by 9.1%. (USTX 638; R40–106.) (According to the exhibit, Danforth prices rose while Sentinel and Hooker prices fell). Although we recognize that correlation is often relied upon to infer causation, *see, e.g., Cellophane,* 351 U.S. at 400, 76 S.Ct. at 1010, we do not believe that this aggregation of sales data over five years provided a sufficiently close correlation between changes in demand and price to justify the inference that consumers were willing and able to switch away from Danforths *because of* increasing price differences. The exhibit wholly fails to take account of factors other than price (or quality) which may have affected demand for Danforths. If changes in relative prices had been more closely correlated in time with shifting purchases then it might have been reasonable to infer that the demand shifts were caused by the price differences. As the evidence stands, however, the datum aggregating demand behavior from 1985 to 1990 fails to provide any basis from which the jury could have inferred that the demand shifts were caused by prices instead of other factors. Those non-price, non-quality factors might well have included consumers' increased awareness of the similarities between Danforths and other brands (perhaps caused by U.S. Anchor's successful promotion of its own products), changing attitudes concerning thrift and the value of money, the decline in demand for fluke anchors generally after the 1987–88 season, (*see* USTX 479), or competition

from Rule's own more expensive premium Deepset line. Over time the shape of a demand curve changes independently of variations in the pricing and quality of particular substitute products. Aggregate (or average) evidence of demand over too long a period of time provides no support for inferring that changes apparently correlated with substitute price movements represent shifts in the curve caused by those variations in prices. Given the changes in the behavior of competitors that occurred over the five years in ***997** question, namely the development of fierce price competition between Rule and U.S. Anchor in the generic and economy market and the introduction of Deepsets, we conclude that the average Danforth sales statistic was insufficient evidence from which the jury could have inferred demand cross-elasticity in October 1985 or thereafter. *Cf. Yoder Bros.,* 537 F.2d at 1367–68. This conclusion is buttressed by the more precise sales data provided by USTX 508. Comparing the 1985–86 and 1986–87 seasons, which are the two closest in time to the date when the alleged predation began in October 1985 for which data were offered, the exhibit shows that unit sales of Danforths fell 5.4% [19] despite a price reduction of 0.5% and a simultaneous increase in the prices of generic anchors of 0.8%. *Id.* at 2. Danforths suffered this decline while the overall demand for fluke anchors jumped 19%, from 273,000 to 325,000 in annual unit sales. (USTX 479.) [20]

Just as an increase in Danforth prices might have been expected to drive customers away from Rule and into the arms of generic manufacturers, an increase in prices for generic brands would likely cause some otherwise price-sensitive customers to prefer the more expensive Danforths. Nonetheless, the present record provides no basis other than guesswork for concluding that a shift away from generics would have been significant in magnitude; [21] the large spread in prices between generic anchors and Danforths tends to suggest that the shift would not have been great. Thus, we conclude that the record provides no support for finding significant cross-elasticity of demand between Danforths and generics.

Second, the evidence was insufficient for a reasonable juror to find a significant cross-elasticity of supply. The jury could not reasonably have found that the manufacturing capacity used to make Danforths likely would have been switched to making generic anchors in response to moderate price increases by a sole seller of the lower priced products. To be sure, the productive processes employed in manufacturing Danforths were virtually identical to those used for generics. (R33–145–50.) Yet it defies logic to suggest that a rational supplier [22] would switch from selling branded products at high prices to selling equally costly equivalent products at lower prices, even assuming that the lower prices would yield significant supranormal profits. Put another way, it would be unreasonable to expect Rule to lower the price of Danforths and abandon its ability to discriminate against brand-conscious boaters solely to earn smaller profits. There was insufficient evidence of likely supply substitution from which to conclude that any portion of Danforth output would have served to constrain price increases among the generic anchors. [23]

Moreover, the record demonstrates that the Danforth line, although functionally equivalent to their counterparts, may have constituted its own market based on consumer brand loyalty. The fluke anchor industry presented the unusual circumstance of severe price discrimination against a distinct group of consumers based solely on brand preference. U.S. Anchor's expert, Dr. Willard F. ***998** Mueller, testified on direct examination that "people have gotten an attachment to the Danforth Standard in this case, it had kind of a mystique about it at one time, ... what happens in one year, simply a price difference, doesn't result in an immediate kind of shift." (R40–106.) Although interbrand competition generally restrains the pricing behavior of individual brand sellers, *Continental T.V., Inc. v. GTE Sylvania Inc.,* 433 U.S. 36, 52 n. 19, 97 S.Ct. 2549, 2558 n. 19, 53 L.Ed.2d 568 (1977), *on remand,* 461 F.Supp. 1046 (N.D.Cal.1978), *aff'd,* 694 F.2d 1132 (9th Cir.1982), it is settled that customer brand loyalty may constitute an impediment to competition and thus an aid in the exercise of market power. *See, e.g., United States v. Pabst Brewing Co.,* 384 U.S. 546, 559–61, 86 S.Ct. 1665, 1672, 16 L.Ed.2d 765 (1966) (Harlan, J., concurring), *on remand,* 296 F.Supp. 994 (E.D.Wis.1969). [24] A single branded product may, in rare cases, constitute its own relevant market. *Los Angeles Mem. Coliseum Comm'n v. National Football League,* 726 F.2d 1381, 1393 (9th Cir.), *cert. denied,* 469 U.S. 990, 105 S.Ct. 397, 83 L.Ed.2d 331 (1984).

The understanding that brand loyalty may facilitate monopolization is consistent with the general proposition that the ability to discriminate against a distinct group of customers by charging higher prices for otherwise similar products demonstrates the existence of market power with respect to that group. *See United States v. Grinnell Corp.,* 384 U.S. 563, 574, 86 S.Ct. 1698, 1706, 16 L.Ed.2d 778 (1966). [25] The existence of such market power may, as a practical matter, remove the higher priced product from the

broader market composed of its functional substitutes. *See C.E. Services, Inc. v. Control Data Corp.,* 759 F.2d 1241, 1246 (5th Cir.), *cert. denied,* 474 U.S. 1037, 106 S.Ct. 604, 88 L.Ed.2d 583 (1985) (holding that "a ubiquitous price differential of some 20–25%" between branded and unbranded services, combined with other *Brown Shoe* factors, could justify finding a separate market for the unbranded services and thus precluded summary judgment on the issue of market definition).

We do not suggest that the existence or hypothetical possibility of monopoly power over one product automatically excludes it from a broader market. "[S]ubmarkets are not a basis for the disregard of a broader line of commerce that has economic significance." *United States v. Phillipsburg Nat'l Bank & Trust Co.,* 399 U.S. 350, 360, 90 S.Ct. 2035, 2041, 26 L.Ed.2d 658 (1970). We do hold, however, that regardless of which party in the case bears the ultimate burden of persuasion, the broader economic significance of a submarket must be supported by demonstrable empirical evidence. Although perhaps difficult to come by, evidence that the dominant firm within a submarket costs of production were insensitive to changes in the quantity of goods sold, suggesting that its only rational response would be to increase output to satisfy the higher demand in the event of price increases above competitive levels in the broader market, might show that submarket production in fact disciplined price levels in the broader market. Especially if the submarket represents a premium-priced segment of the broader market, the relevance of proof regarding elasticity of supply would depend on the validity of the assumption that significant numbers of consumers would switch in response to significant price increases in the broader market, an assumption that may or may not be supported by evidence or common experience. In the present case U.S. Anchor can rely upon neither evidence nor inference. Simpler evidence of supply and demand substitution, like proof that producers in the submarket had actually increased or decreased their sales in response to corresponding price ***999** changes in the broader market, would also suffice. As we have pointed out, however, U.S. Anchor failed to meet its burden of proving interdependent market behavior by this method as well.

Considering all the evidence in light of the factors identified by *Cellophane* and *Brown Shoe* and explained in subsequent decisions, we conclude as a matter of law that the relevant product market was light weight generic and economy fluke anchors.

2. Measuring Power in the Market

The principal measure of actual monopoly power is market share, and the primary measure of the probability of acquiring monopoly power is the defendant's proximity to acquiring a monopoly share of the market. Thus, a sufficiently large market share may alone create a genuine dispute over whether the defendant possessed a dangerous probability of successfully monopolizing a market despite the existence of other facts tending to make monopolization unlikely, thereby precluding summary judgment for the defendant. *McGahee v. Northern Propane Gas Co.,* 858 F.2d at 1506. When assessing market shares for the purpose of ascertaining market power the appropriate measure of a firm's share is the quantity of goods or services actually sold to consumers. Although revenues are often relied upon as a surrogate for quantity, actual unit sales must be used whenever a price spread between various products would make the revenue figure an inaccurate estimator of unit sales. *Brown Shoe,* 370 U.S. at 341 n. 69, 82 S.Ct. at 1533 n. 69.

In *McGahee* we noted in dicta that several factors may be relevant to whether a particular market share evidences a dangerous probability of success. 858 F.2d at 1505 (citing *McGahee v. Northern Propane Gas Co.,* 658 F.Supp. 189, 196–97 (N.D.Ga.1987), *rev'd,* 858 F.2d 1487 (11th Cir.1988)). In finding no dangerous probability of success the district court had relied upon the ease of entry by new firms and expansion from adjacent geographic markets, the number and size of alleged victims of the predation and the defendant's declining market share during the alleged attempt to monopolize. 658 F.Supp. at 196–97. Nevertheless, we held:

> Without examining any factors to determine what market share would be necessary for Northern Propane's alleged predatory pricing to present a dangerous probability of success, we can say that a sixty or sixty-five percent market share is a sufficiently large platform from which such a scheme could be launched to create a genuine issue of material fact as to whether there was a dangerous probability that Northern

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> Propane would succeed in achieving a monopoly.

McGahee, 858 F.2d at 1506. Finding it "undisputed" that the defendant possessed such a share, we reversed the district court's order of summary judgment for the defendant and remanded for further proceedings. Our holding in *McGahee* that market share estimated with reasonable confidence to fall between 60 and 65% suffices to raise a jury question concerning dangerous probability of success is binding circuit precedent. *Sherry Mfg. Co. v. Towel King, Inc.,* 822 F.2d 1031, 1034 n. 3 (11th Cir.1987). We do note, however, the tension between *McGahee* 's bright-line approach and *Cliff Food Stores, Inc. v. Kroger, Inc.,* 417 F.2d 203 (5th Cir.1969), in which the court noted that "one must be particularly wary of the numbers game of market percentage when considering an 'attempt to monopolize' suit" under the dangerous probability standard. 417 F.2d at 207 n. 2; *cf. United States v. Columbia Steel Co.,* 334 U.S. 495, 528, 68 S.Ct. 1107, 1124, 92 L.Ed. 1533 (1948) ("the relative effect of percentage command of a market varies with the setting in which that factor is placed") (actual monopolization case). We believe the cases may be reconciled by requiring a careful definition of the relevant market (as mandated by *Walker Process* and *American Key*)[26] and an assessment of each firm's ***1000** ability to vary its output in calculating the size of the market and attributing individual market shares. *See, e.g., United States v. General Dynamics Corp.,* 415 U.S. 486, 499–504, 508–10, 94 S.Ct. 1186, 1194–97, 1199–1200, 39 L.Ed.2d 530 (1974) (measuring power in market for coal in terms of possession or likely near-term acquisition of uncommitted reserves instead of overall sales, because most sales represented fulfillment of existing long-term requirements contracts).

In *Cliff Food Stores* the former Fifth Circuit stated that something more than 50% market share would be required to show *actual* monopoly, at least in the absence of collusive price leadership or tacit coordination in an industry. 417 F.2d at 207 n. 2. The Second Circuit in *Broadway Delivery Corp. v. United Parcel Service of America, Inc.,* 651 F.2d 122 (2d Cir.), *cert. denied,* 454 U.S. 968, 102 S.Ct. 512, 70 L.Ed.2d 384 (1981), similarly suggested that the absence of *actual* monopoly power could be found as a matter of law when the defendant supplies only 50% of the market, "or even somewhat above that figure, [when] the record contains no significant evidence concerning the market structure to show that the defendant's share of that market gives it monopoly power." 651 F.2d at 129. Despite these suggestions, we have discovered no cases in which a court found the existence of actual monopoly established by a bare majority share of the market. Nevertheless, a dangerous *probability* of achieving monopoly power may be established by a 50% share. For this reason, it is usually necessary to evaluate the prospects for monopolization as they existed when the alleged attempt began. As shown by the undisputed facts discussed *infra,* Rule never possessed a dangerous probability of success during the time for which U.S. Anchor seeks damages.

U.S. Anchor points to the combined market shares of Rule and Tie Down at the end of the 1984–85 season, immediately before the transaction that eliminated Tie Down as a supplier and transferred its production to Rule. Accepting *arguendo* the implicit contention that Tie Down's pre-transaction market share should be attributed to Rule, we conclude from the undisputed evidence that Rule's market share on August 31, 1985, the eve of the 1985–86 season, was 61.5%, (RTX 674), and its aggregate (average) share over the entire season was 30.1%, (*id.;* RTX 675 at 1).

Rule has argued that we should not attribute all of Tie Down's pre-transaction market share to it. After the transaction Tie Down had no need for its anchor sales representatives, many of whom found engagements with U.S. Anchor and employed their connections and reputation on behalf of the newcomer's selling efforts. Moreover, U.S. Anchor's Chapman was well known to customers from his days with Tie Down. Thus, according to Rule, U.S. Anchor stepped into Tie Down's shoes and inherited at least some of Tie Down's pre-transaction market share, presumably that portion which U.S. Anchor had the productive capacity to satisfy. This argument is persuasive, although it may be subject to rebuttal on at least two grounds. *Cf. American Academic Suppliers, Inc. v. Beckley–Cardy, Inc.,* 922 F.2d 1317, 1321–22 (7th Cir.1991). First, the depth of Rule's product line and the expertise of its own sales force conferred competitive advantages which might have induced some of Tie Down's former customers to stay with the Hooker line. Second, the anchor industry was highly concentrated and customers had few alternative sources of supply, a factor that is especially important in view of Rule's effort to link purchase of the Deepset anchors to exclusive dealing arrangements with distributors. We need not reach the merits of Rule's contention, however, because even if we consider Rule to have had 61.5% of the market on August 31, 1985, there was insufficient evidence from which the jury could have found a dangerous probability of monopolization in October.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

As we have outlined above, Rule's *average* market share for the 1985–86 season was 30.1%, a fact which strongly indicates that Rule's share declined sharply from 61.5% after U.S. Anchor's entry into the market in August. For the month of October, U.S. Anchor's sales of generic and economy anchors exceeded Rule's by 5.7%. (RTX 675 at 15). Prior to October U.S. Anchor had no sales at all, but the firm was accepting orders ***1001** during this time and apparently possessed the capacity to fill them. Thus, Rule was never able to maintain a majority position in the market during the 1985–86 season. *Cf. General Dynamics,* 415 U.S. at 501–02, 94 S.Ct. at 1196. Accordingly, because Rule possessed less than 50% of the market at the time the alleged predation began and throughout the time when it was alleged to have continued, there was no dangerous probability of success in October 1985 as a matter of law.

3. Recoupment

Rule argues that the district court should have granted its motion for judgment notwithstanding the verdict based on its contention that there can be no dangerous probability of successful monopolization by predatory pricing unless it is shown that the defendant would have recouped the foregone revenues associated with its price-cutting strategy.[27] Our disposition of this case, however, makes it unnecessary to address Rule's recoupment argument.

B. *Anticompetitive Conduct, Specific Intent and Damages*

Our conclusion that U.S. Anchor failed to show a dangerous probability of success makes it unnecessary for purposes of resolving its attempt claim to evaluate the evidence of Rule's and Tie Down's costs, as would be required to classify its pricing conduct as anticompetitive. *See Matsushita,* 475 U.S. at 585 n. 8, 106 S.Ct. at 1355 n. 8; *International Air Industries, Inc. v. American Excelsior Co.,* 517 F.2d 714, 723–25 (5th Cir.1975). The same is true with respect to the evidence of specific intent to achieve monopoly power by unlawful conduct, although we note that such intent may sometimes be inferred from predatory conduct itself. *Spectrum Sports,* 506 U.S. at ––––, 113 S.Ct. at 892; *International Tel. & Tel.,* 104 F.T.C. at 401–02; *see also McGahee,* 858 F.2d at 1503–04. Nor must we decide whether to parse this evidence for the precise level during each season at which Rule's prices unlawfully dropped below its costs in order to assess U.S. Anchor's proof of damages, as requested by Rule. *See MCI Communications Corporation v. American Telephone and Telegraph Company,* 708 F.2d 1081, 1162, 1165 (7th Cir.1983).

VI. CONSPIRACY

U.S. Anchor's conspiracy claims are distinct from its attempted monopolization claim. The elements of a conspiracy to monopolize under Section 2 are (1) an agreement to restrain trade, (2) deliberately entered into with the specific intent of achieving a monopoly rather than a legitimate business purpose, (3) which could have had an anticompetitive effect, and (4) the commission of at least one overt act in furtherance of the conspiracy. *Seagood Trading Corp. v. Jerrico, Inc.,* 924 F.2d 1555, 1576 (11th Cir.1991). The elements of a conspiracy to restrain trade under Section 1 are (1) an agreement to enter a conspiracy (2) designed to achieve an unlawful objective. *Bolt v. Halifax Hosp. Medical Ctr.,* 891 F.2d 810, 820 (11th Cir.), *cert. denied,* 495 U.S. 924, 110 S.Ct. 1960, 109 L.Ed.2d 322 (1990), *appeal after remand,* 980 F.2d 1381 (11th Cir.1993). The plaintiff must also prove (3) "actual unlawful effects [or] facts which radiate a potential for future harm" to competition. *Times–Picayune Publishing Co. v. United States,* 345 U.S. 594, 622, 73 S.Ct. 872, 888, 97 L.Ed. 1277 (1953).

There is no requirement, however, that a conspiracy under either provision have a dangerous probability of successfully achieving its objectives. *Copperweld Corp. v. Independence Tube Corp.,* 467 U.S. 752, 767–68, 104 S.Ct. 2731, 2740, 81 L.Ed.2d 628 (1984). Moreover, "[a] section 1 plaintiff ... need not prove an intent on the part of the co-conspirators to restrain trade or to build a monopoly. So long as the purported conspiracy has an anticompetitive effect, the plaintiff has made out a case under section 1." *Bolt,* 891 F.2d at 819–20 (citations omitted). We have said, however, that "a section 1 claim and a section 2 conspiracy to monopolize ***1002** claim require the same threshold showing—the existence of an agreement to restrain trade." *Seagood,* 924 F.2d at 1576.

U.S. Anchor points to evidence of the unlawful intent necessary to create such an agreement. We have reviewed this evidence and find it sufficient to show an intent to achieve an unlawful objective on Rule's part, namely the use of predatory means to monopolize the fluke anchor market. Nevertheless, there is insufficient evidence linking Tie Down to Rule's efforts to support a finding of conspiracy between them. Federal antitrust law requires a plaintiff to introduce evidence that tends to exclude the possibility that the defendants acted independently or legitimately. *Bolt,* 891 F.2d at 819; *see also Monsanto Co. v. Spray–Rite Serv. Co.,* 465 U.S. 752, 764,

104 S.Ct. 1464, 1470, 79 L.Ed.2d 775 (1984). U.S. Anchor did not meet this heightened standard of proof. *Cf. Boczar v. Manatee Hosps. & Health Sys., Inc.,* 993 F.2d 1514, 1518–19 (11th Cir.1993) (finding sufficient evidence when defendant's supposed legitimate reasons for acting were shown to be fabricated and contrived). [28] The MacKarvich market report, USTX 683, for instance, does not show that Tie Down desired to employ predatory means to drive U.S. Anchor from the market. Rather, it merely shows the prices at which it would be possible to inflict losses on the newcomer. It says nothing about Rule's costs, and U.S. Anchor does not dispute that Tie Down had no knowledge of Rule's costs other than the price paid for anchors. Tie Down's experts and MacKarvich himself testified that such studies are common in competitive industries and consistent with legitimate competition based on price. MacKarvich's recommendation to set prices low enough to inflict losses on U.S. Anchor merely shows a desire to win on the basis of efficiently producing a product and selling it at a lower price than less efficient rivals. It is not unlawful to slash prices in an attempt to obtain more sales, even if the result is that a competitor happens to be driven out of business. *Ball Mem. Hosp., Inc. v. Mutual Hosp. Ins., Inc.,* 784 F.2d 1325, 1338–39 (7th Cir.1986). Moreover, to suffer a loss in the first year of operation is common in competitive industries, and for MacKarvich to anticipate that U.S. Anchor would be temporarily unprofitable does not necessarily show a desire or expectation that the firm would be driven from the marketplace. In short, we have examined the record closely and find there is insufficient evidence linking Tie Down with Rule's scheme to constitute a conspiracy under the substantive proof requirements of federal antitrust law.

Without Tie Down, there was no one with whom Rule could have conspired. Hence, its unilateral conduct was not actionable as a conspiracy under federal antitrust law. The district court erred in denying judgment as a matter of law for Rule and Tie Down on the Sherman Act conspiracy claims.

VII. CLAIMS UNDER GEORGIA LAW

U.S. Anchor's complaint alleged violations of article III, § VI, ¶ 5 of the Georgia constitution and O.C.G.A. § 13–8–2(a)(2), which invalidate certain contracts in restraint of trade. (R1–1, ¶¶ 60–62.) U.S. Anchor concedes that these provisions merely render such agreements unenforceable and provide no cause of action for damages to those who are parties thereto, *see E.T. Barwick Indus. v. Walter E. Heller & Co.,* 692 F.Supp. 1331, 1349 (N.D.Ga.1987), but argues that Georgia recognizes a common law tort action in favor of third parties who are injured by a conspiracy in restraint of trade. We agree with U.S. Anchor that its complaint stated a valid claim for damages as a result of a conspiracy in restraint of trade. *See Blackmon v. Gulf Life Ins. Co.,* 179 Ga. 343, 175 S.E. 798, 802–03 (1934) (holding that allegations of predatory ***1003** pricing conspiracy with intent to monopolize stated a cause of action); *Atlanta Association of Fire Ins. Agents v. McDonald,* 181 Ga. 105, 181 S.E. 822, 828 (1935) (awarding nominal damages and injunction for group boycott); *see also Harrison Co. v. Code Revision Comm'n,* 244 Ga. 325, 260 S.E.2d 30, 34 (1979). The district court erred in failing to perceive "the distinction between a contract or agreement merely in restraint of trade as between the parties, and a combination or contract to stifle competition, or a conspiracy to ruin a competitor." *Brown v. Jacobs Pharmacy Co.,* 115 Ga. 429, 41 S.E. 553, 556 (1902) (suit for damages and injunction). Although we have found insufficient evidence of a conspiracy under federal law standards, this does not answer the question of whether Georgia courts would find sufficient evidence of conspiracy under their substantive law. *Cf. Sachdeva v. Smith,* 167 Ga.App. 80, 306 S.E.2d 19, 20 (1983).

We have previously held that Georgia law provides a cause of action for tortious interference with the business relationships between a plaintiff and its customers, suppliers or representatives. To be held liable the defendant "must have (1) acted improperly and without privilege, (2) purposely and with malice with the intent to injure, (3) induced a third party or parties not to enter into or continue a business relationship with the plaintiff, and (4) [caused] plaintiff [to] suffer[ ] some financial injury." *DeLong Equip. Co. v. Washington Mills Abrasive Co.,* 887 F.2d 1499, 1518 (11th Cir.1989) (quotation omitted), *cert. denied,* 494 U.S. 1081, 110 S.Ct. 1813, 108 L.Ed.2d 943 (1990), *appeal after remand,* 990 F.2d 1186 (11th Cir.1993), *amended,* 997 F.2d 1340 (11th Cir.1993) (per curiam); *see also NAACP v. Overstreet,* 221 Ga. 16, 142 S.E.2d 816, 822 (1965), *cert. dismissed,* 384 U.S. 118, 86 S.Ct. 1306, 16 L.Ed.2d 409 (1966). The defendant may show that competitive conduct is privileged by establishing that it used no improper means. *Integrated Micro Sys., Inc. v. NEC Home Elecs. (USA), Inc.,* 174 Ga.App. 197, 329 S.E.2d 554, 559 (1985), *cert. denied,* No. 69405 (Ga. Apr. 24, 1985).

U.S. Anchor's complaint adequately pleads a claim for relief under this theory to present it for adjudication by the district court. Count V gave full notice to the defendants that U.S. Anchor sought recovery under Georgia law for "Unfair Methods of Competition and

Unfair Acts and Practices," including conduct which was "inequitable, unfair, unscrupulous, in violation of public policy and unconscionable and tend[ing] to defeat or lessen competition...." (R1–1 ¶¶ 59–60.) The fact that paragraph 60 of the complaint also refers to the constitutional and statutory provisions which U.S. Anchor concedes confer no independent damages remedy does not by itself deprive the defendants of "fair notice of what the plaintiff's claim is and the grounds upon which it rests." *Quality Foods de Centro Am., S.A. v. Latin Am. Agribusiness Dev. Corp.,* 711 F.2d 989, 995 (11th Cir.1983) (quoting *Conley v. Gibson,* 355 U.S. 41, 47, 78 S.Ct. 99, 103, 2 L.Ed.2d 80 (1957)); *see* Fed.R.Civ.P. 8(a)(2). The issue of whether the tort theory is applicable to the facts of this case was adequately argued to the district court in connection with U.S. Anchor's requested jury instructions, (R28–136–45), and thus preserved for appellate review. *Cf. Weaver v. Casa Gallardo, Inc.,* 922 F.2d 1515, 1519 (11th Cir.1991).

The novel questions presented are whether below-cost pricing can satisfy the improper action element of the tort and whether low prices, standing alone, can constitute a prohibited inducement of the plaintiff's customers. *Cf. Parks v. Atlanta News Agency, Inc.,* 115 Ga.App. 842, 156 S.E.2d 137, 140 (1967) (holding that solicitation of competitor's customers is not itself tortious, even when combined with "preferential" prices), *cert. denied,* No. 42624 (Ga. July 14, 1967). We regard it as unclear whether tortious interference with business relations under Georgia law may be established by a showing of predatory pricing and, if so, what sort of pricing conduct would be deemed predatory. We also have some doubt as to whether intentional interference with business relations is a distinct cause of action from the tort of conspiracy in restraint of trade, or whether there is only a single theory of relief, so that proof of a conspiracy to interfere with the plaintiff's business relations ***1004** would be actionable as U.S. Anchor's sole remedy for the alleged joint conduct of Rule and Tie Down. *Compare Cook v. Robinson,* 216 Ga. 328, 116 S.E.2d 742 (1960) *with Jacobs Pharmacy,* 41 S.E. at 554–57 (quoting *Doremus v. Hennessy,* 176 Ill. 608, 52 N.E. 924 (1898)); *see also Overstreet,* 142 S.E.2d at 822. This is not a matter of mere semantics, for while it appears settled that predatory pricing by a group or conspiracy is actionable, we have found no Georgia authority addressing predation by a single defendant acting unilaterally.

Another issue affecting the outcome of U.S. Anchor's state law claims is the validity and effect of its settlement agreement with Rule, executed on March 19, 1986. The agreement provided that each party would release the other

> from any and all actions, demands, claims or causes of action whatsoever, which now exist or which may arise in the future, as a result of events which occurred prior to the execution of the Settlement Agreement, including, without limitation, any claims which were or could have been presented by way of complaint or counterclaim in Civil Action Number C85–4466A.

(RTX 457.) Because the predatory pricing scheme allegedly began in October 1985, Rule contends that the settlement agreement operated as a release of U.S. Anchor's cause of action. U.S. Anchor contends that its predatory pricing claims were undiscovered at the time the release was executed and therefore were not intended to be released. In addition, it contends that injuries caused by predatory conduct occurring after the release would not have been discharged even if they arose as a result of a scheme or conspiracy that was ongoing when the release was signed.[29] The district court concluded that the federal predatory pricing claims were undischarged because the agreement unambiguously applied only to causes of action related to the prior litigation. It also relied on Chapman's oral testimony concerning his intent at the time he signed the agreement and on *Covington v. Brewer,* 101 Ga.App. 724, 115 S.E.2d 368, 372–73 (1960), in which the court held that the scope of a release as intended by the parties could not be presumed to encompass rights respecting a subject matter not clearly referred to in the body of the agreement. *But cf. Ingram Corp. v. J. Ray McDermott & Co.,* 698 F.2d 1295, 1311–12 (5th Cir.1983).

The doctrine of pendent jurisdiction as outlined in *United Mine Workers v. Gibbs,* 383 U.S. 715, 86 S.Ct. 1130, 16 L.Ed.2d 218 (1966), gives the district court power to decide claims arising under state law as to which there was no independent basis for federal jurisdiction but which share a common nucleus of operative fact with federal claims. The court also has discretion not to hear such state law claims.

> Under *Gibbs,* a federal court should consider and weigh, in each case, and at every stage of the litigation, the values of judicial economy, convenience, fairness, and comity in order to decide whether to exercise jurisdiction over a case brought in that court involving pendent state-law claims. When the balance of these factors indicates that a case properly belongs in state court, as when the federal-law claims have dropped out of the lawsuit in its early stages and only state-law claims remain, the federal court should decline to exercise its jurisdiction by dismissing the case without prejudice.

Carnegie–Mellon Univ. v. Cohill, 484 U.S. 343, 350, 108 S.Ct. 614, 619, 98 L.Ed.2d 720 (1988) (footnote omitted). While the doctrine is a flexible one according great leeway to the court, *see id.* at 350 n. 7, 108 S.Ct. at 619 n. 7, we have found an abuse of discretion in failing to dismiss a case when the federal claims were resolved early in the proceedings ***1005** and the state law claims posed issues of first impression. *See Hardy v. Birmingham Bd. of Educ.,* 954 F.2d 1546 (11th Cir.1992).

In the present case, the federal claims have survived through trial and have only been resolved on appeal. Thus, the parties have already tried the state law claims in federal court, although the district court's ruling prevented the jury from considering them. The legal issues have been decided by the district court and are now properly before us for review, so that judicial economy and convenience weigh in favor of retaining jurisdiction. On the other hand some of the state law issues are novel, and comity between federal and state judicial systems weighs in favor of determination by state courts. Moreover, a ruling by this court in favor of U.S. Anchor's position would require a new federal trial in which only state law claims would be put in issue. Fairness to U.S. Anchor, however, prevents us from dismissing the state law claims. Dismissal would require the plaintiff to re-file its action in state court more than eight years after the allegedly tortious conduct began, thereby losing a substantial portion of its rights (if any) by application of Georgia's four-year statute of limitations. [30] We might have reached a different result under the Judicial Improvements Act of 1990, Pub.L. No. 101–650, § 310, 104 Stat. 5089, 5113–14, *codified at* 28 U.S.C. § 1367. Under 28 U.S.C. § 1367(d), the statute of limitations would be tolled while the claims were pending until 30 days after an order of dismissal, thus allowing the plaintiff time for filing a new action in state court without a lapse of its rights. But the present case was commenced before the statute's effective date on December 1, 1990, and § 1367 is not retroactive. *Yanez v. United States,* 989 F.2d 323, 327 n. 3 (9th Cir.1993). In view of the fact that the case may be certified to the Supreme Court of Georgia for interlocutory resolution of the state law issues, we conclude that the balance of factors involved in the discretionary decision to retain pendent jurisdiction weighs clearly against dismissal. [31]

Accordingly, we respectfully certify the following questions of law to the Supreme Court of Georgia and the Honorable Justices of that Court.

Questions for Certification

1. DOES A GENERAL RELEASE UNDER GEORGIA LAW DISCHARGE LIABILITY FOR INJURY CAUSED BY SUBSEQUENT ACTS IN THE COURSE OF A SCHEME OR CONSPIRACY THAT WAS ONGOING AT THE TIME THE RELEASE WAS EXECUTED BUT UNKNOWN TO THE RELEASING PARTY?

2. DOES A GENERAL RELEASE UNDER GEORGIA LAW DISCHARGE LIABILITY FOR INJURY CAUSED BY TORTIOUS CONDUCT ALREADY COMMITTED THAT WAS UNKNOWN TO THE ***1006** RELEASING PARTY AT THE TIME THE RELEASE WAS EXECUTED?

3. DOES THE TORT OF INTENTIONAL INTERFERENCE WITH BUSINESS RELATIONS ENCOMPASS PREDATORY PRICING BELOW SOME MEASURE OF THE DEFENDANT'S COSTS?

4. IF THE ANSWER TO QUESTION 3 IS YES, THEN IN A CASE OF ACTIONABLE PREDATORY PRICING BELOW SOME MEASURE OF COST BY A CONSPIRACY OR A SINGLE DEFENDANT, WHAT IS THE APPROPRIATE MEASURE OF THE DEFENDANTS' COSTS?

Our statement of the questions is not designed to limit the inquiry of the Supreme Court of Georgia. Instead, the

Supreme Court has the widest possible latitude to consider the problems and issues involved in this case as it perceives them to be. *Martinez v. Rodriquez,* 394 F.2d 156, 159 n. 6 (5th Cir.1968), *conformed to certified answer,* 410 F.2d 729 (5th Cir.1969). To assist the Supreme Court, the entire record in this case and copies of the parties' briefs are transmitted herewith.

VIII. CONCLUSION

The judgment of the district court is reversed with respect to all federal law causes of action and judgment is rendered in favor of the defendants thereon. Dispositive questions of law respecting the plaintiff's state law causes of action are certified to the Supreme Court of Georgia.

REVERSED and JUDGMENT RENDERED in part and QUESTIONS CERTIFIED.

All Citations

7 F.3d 986, 1993-2 Trade Cases P 70,426

Footnotes

1 The annual marine products selling season begins each September with a trade show.

2 U.S. Anchor's trial exhibits will be cited as “USTX _,” Rule's trial exhibits as “RTX _” and Tie Down's trial exhibits as “TDTX _.”

3 (USTX 372 (Rule's 1989–90 price list; 50.4 to 96.2% spread); USTX 368 (Rule's 1988–89 price list; 49.7 to 96.2% spread); USTX 362 (Rule's 1987–88 price list; 73.4 to 91.7% spread); USTX 355 (Rule's 1986–87 price list; 61.0 to 76.1% spread); *see also* USTX 371 (U.S. Anchor's 1989–90 price list); USTX 367 (U.S. Anchor's 1988–89 price list); USTX 365 (U.S. Anchor's 1987–88 price list).) U.S. Anchor repeatedly opened the marine season with prices higher than Rule's, only to reduce its prices when Rule failed to follow U.S. Anchor's pricing strategy.

4 The parties have treated this appeal as though premium fluke anchors were irrelevant. They have also ignored other types of anchors designed for holding on different bottom conditions (fluke anchors are most useful on sandy bottoms and least effective in gripping grassy bottoms). We do the same.

5 Although neither party adduced direct evidence of the combined Rule/Tie Down unit market share in 1984–85 with Danforths included, the jury must have concluded that the firms' combined unit share for that season with the higher-priced anchors included was somewhat greater than the 61.5% unit share they garnered in the non-Danforth market because only Rule marketed the Danforth line. U.S. Anchor's USTX 467 indicates that Rule itself had no 1984–85 revenues in the non-Danforth market. But Rule's RTX 674, which appears to represent the non-Danforth unit market (*compare* RTX 674, col. 1985–86 *with* RTX 675 at 1, rows 1985–86), shows Rule with 12.6% of that market in 1984–85. We assume that RTX 674 attributes to Rule the non-Danforth production of Tie Down following the Rule–Tie Down transaction in the final quarter of the 1984–85 season.

6 Section 2 provides: “Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony....” 15 U.S.C. § 2.

7 Section 1 provides in relevant part: “Every contract, combination ..., or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal.” 15 U.S.C. § 1.

8 Section 3 of the Clayton Act provides in relevant part:

> It shall be unlawful for any person engaged in commerce ... to lease or make a sale or contract for sale of goods ..., whether patented or unpatented, for use, consumption, or resale within the United States ... on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods ... of a competitor or competitors of the lessor or seller, where the effect of such lease, sale,

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

> or contract for sale or such condition ... may be to substantially lessen competition or tend to create a monopoly in any line of commerce.

15 U.S.C. § 14. Among other possible differences between the Sherman Act and Robinson–Patman Act tying provisions is that the Sherman Act prohibition extends to arrangements affecting the sale of services and realty as well as goods. *See, e.g., Tic–X–Press, Inc. v. Omni Promotions Co.,* 815 F.2d 1407 (11th Cir.1987) (tying arrangement conditioning the lease of coliseum theater space upon the employment of a ticket-selling agency affiliated with the lessor); *see generally Thompson v. Metropolitan Multi–List, Inc.,* 934 F.2d 1566, 1574–79 (11th Cir.1991), *cert. denied,* 506 U.S. 903, 113 S.Ct. 295, 121 L.Ed.2d 219 (1992).

9 A motion for directed verdict is now deemed a motion for judgment as a matter of law, and motions for judgment notwithstanding the verdict are now renewed motions for judgment as a matter of law. *See* Fed.R.Civ.P. 50.

10 A predatory pricing scheme could be successful by driving the victim out of business or by coercing him to reduce output to levels consistent with profit-maximization by a firm or syndicate possessing monopoly power. Either result would eliminate the victim's competitive presence.

11 Federal common law, not the state law of contracts, determines the effect of settlement agreements alleged to release federal antitrust claims. *Redel's Inc. v. General Elec. Co.,* 498 F.2d 95, 98 & n. 2 (5th Cir.1974).

12 The terms "monopoly power" and "market power" are synonymous and are used interchangeably in this opinion.

13 This inquiry may be labelled more appropriately as "market estimation." *See* Herbert Hovenkamp, *Economics and Federal Antitrust Law* 59 (1985).

14 *See* Fed.R.App.P. 28(a)(4) (brief shall include "a statement of the facts relevant to the issues presented for review, with appropriate references to the record"); *cf. Harris v. Plastics Mfg. Co.,* 617 F.2d 438, 440 n. 1 (5th Cir.1980) (per curiam) (brief that merely stated an issue, without providing any argument or facts, deemed to waive it). For instance, the plaintiff's brief in *American Key* raised the question of market definition but failed to raise, *inter alia,* the existence of monopoly power. Although the omission technically "abandoned" the issue of market power, the court addressed it anyway. 762 F.2d at 1579–81. We believe Rule's brief puts this case closer to *American Key* than cases in which a brief merely stated an issue without fact and argument, or actually ignored an entire claim or defense. *Cf. Joe Regueira, Inc. v. American Distilling Co.,* 642 F.2d 826, 833 n. 16 (5th Cir. Unit B April 1981); *In re Municipal Bond Reporting Antitrust Litig.,* 672 F.2d 436, 439 n. 6 (5th Cir.1982).

15 (*See* R10–301–4, Memo at 28–30 (Rule's Motion for Directed Verdict and Memorandum in Support); R9–299 Br. at 3–6 (Tie Down's Motion for Directed Verdict and Brief in Support).)

16 Decisions of the former Fifth Circuit rendered before October 1, 1981, are binding upon panels of this court. *Bonner v. City of Prichard,* 661 F.2d 1206, 1209 (11th Cir.1981) (en banc).

17 Also known as "demand substitution."

18 *See also, e.g.,* Richard A. Posner, *Antitrust Law: An Economic Perspective* 125–26 (1976); Hovenkamp, *supra* at 59.

19 U.S. Anchor's unit sales exhibit, USTX 479, shows an even more marked decrease in Danforth sales for the two seasons: a 7.8% drop from 56,431 in 1985–86 to 52,035 in 1986–87. This is only one example of inconsistency in the evidence offered by U.S. Anchor, but we assume that the jury credited the version least favorable to Rule.

20 Faced with this evidence, we can only note that the absence of proof concerning changes in prices and sales before the Rule–Tie Down transaction is an especially prominent flaw in U.S. Anchor's case.

21 By "significant in magnitude" we refer to a shift that is large enough to render unprofitable a monopolistic price increase in the broader market. Again, we defer the task of establishing criteria for testing the quantitative significance of changes in this variable.

22 There is no evidence that Rule was irrational in its pricing strategies, although it may well have been misinformed or overly optimistic concerning U.S. Anchor's staying power in the market.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

23 Of course, Rule's exclusive control over the Danforth trademark also eliminated the possibility of supply substitution by other firms making Danforths. This observation by itself, however, would not be sufficient to show that Danforths and generics represented distinct markets.

24 *See also Cellophane,* 351 U.S. at 392–93, 76 S.Ct. at 1005–06; *Ware v. Trailer Mart, Inc.,* 623 F.2d 1150, 1154 (6th Cir.1980); *cf. Justice Department Guidelines, supra* § 3.3 n. 33 (noting that ease or difficulty of long-term committed entry into a market may depend upon “the relative appeal, acceptability and reputation of incumbents' and entrants' products”).

25 *See also, e.g.,* 2 Areeda & Turner, *Antitrust Law, supra* ¶ 514; Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 518.1d (Supp.1991) [hereinafter Areeda & Hovenkamp, *Antitrust Law*]; Gregory J. Werden, *Market Delineation and the Justice Department's Merger Guidelines,* 1983 Duke L.J. 514, 522, 529–30.

26 Notably, in *McGahee* itself the district court had observed that despite the defendant's concession for summary judgment purposes concerning the relevant product market, “there is, at the very least, an issue of fact as to whether propane constitutes a distinct product market.” 658 F.Supp. at 192 n. 3 (citing *United States v. Empire Gas Corp.,* 537 F.2d 296, 303–304 (8th Cir.1976), *cert. denied,* 429 U.S. 1122, 97 S.Ct. 1158, 51 L.Ed.2d 572 (1977)).

27 If we accepted Rule's argument we could simply remand for a new trial with directions to instruct the jury concerning this “element” of the plaintiff's case, or we could evaluate the record to see whether the jury could have found the element proven.

28 We have considered U.S. Anchor's contention that the district court abused its discretion by excluding certain evidence that Rule's customers perceived an attempt by Rule to eliminate U.S. Anchor from the market, a perception based upon reported statements made by a Rule employee. (*See* USTX 206.) This evidence has such little bearing on the existence of an agreement between Rule and Tie Down that its exclusion on hearsay grounds, even if erroneous, *see United States v. Pendas–Martinez,* 845 F.2d 938, 942–43 (11th Cir.1988); *Southern Stone Co. v. Singer,* 665 F.2d 698, 703 (5th Cir. Unit B Jan. 1982), was harmless. Fed.R.Evid. 103(a). We see no abuse of discretion.

29 *Compare Imperial Point Colonnades Condominium, Inc. v. Mangurian,* 549 F.2d 1029, 1043–44 (5th Cir.1977), *cert. denied,* 434 U.S. 859, 98 S.Ct. 185, 54 L.Ed.2d 132 (1977), *Poster Exchange, Inc. v. National Screen Serv. Corp.,* 517 F.2d 117, 127 (5th Cir.1975), *cert. denied,* 423 U.S. 1054, 96 S.Ct. 784, 46 L.Ed.2d 643 *and* 425 U.S. 971, 96 S.Ct. 2166, 48 L.Ed.2d 793 (1976), *appeal after remand,* 542 F.2d 255 (5th Cir.1976) (per curiam), *cert. denied,* 431 U.S. 904, 97 S.Ct. 1697, 52 L.Ed.2d 388 (1977), *and Redel's Inc. v. General Elec. Co.,* 498 F.2d 95, 99 (5th Cir.1974) *with Record Club of Am., Inc. v. United Artists Records, Inc.,* 611 F.Supp. 211, 217 & n. 8 (S.D.N.Y.1985).

30 The mechanics of Georgia's statute of limitations have been explained as follows:

> The test to be applied in determining when the statute of limitations begins to run against an action sounding in tort is in whether the act causing the damage is in and of itself an invasion of some right of the plaintiff, and thus constitutes a legal injury and gives rise to a cause of action. If the act is of itself not unlawful in this sense, and a recovery is sought only on account of damage subsequently accruing from and consequent upon the act, the cause of action accrues and the statute begins to run only when the damage is sustained; but if the act causing such subsequent damage is of itself unlawful in the sense that it constitutes a legal injury to the plaintiff, and is thus a completed wrong, the cause of action accrues and the statute begins to run from the time the act is committed, however slight the actual damage then may be.

Fox v. Ravinia Club, Inc., 202 Ga.App. 260, 414 S.E.2d 243, 244 (1991) (quotation omitted), *cert. denied,* No. A91A1136 (Ga. Feb. 4, 1992). As we understand the test, U.S. Anchor's cause of action (if any) continued to accrue with each predatory sale, and would be time-barred under O.C.G.A. § 9–3–31 with respect to each transaction occurring more than four years before commencement of the new action in state court. *See Cleveland Lumber Co. v. Proctor & Schwartz, Inc.,* 397 F.Supp. 1088, 1094 (N.D.Ga.1975) (citing *Georgia Power Co. v. Moore,* 47 Ga.App. 411, 170 S.E. 520 (1933)); *accord Zenith Radio Corp. v. Hazeltine Research, Inc.,* 401 U.S. 321, 338, 91 S.Ct. 795, 806, 28 L.Ed.2d 77 (1971) (federal antitrust law).

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

31 We need not decide whether § 1367 would allow the court of appeals to decide the propriety of exercising supplemental jurisdiction or whether such discretion is vested in the district court alone.

End of Document © 2020 Thomson Reuters. No claim to original U.S. Government Works.

LEGAL AUTHORITY AA-38

Transfer of Rights Contract: Everything You Need to Know

A transfer of rights contract allows you to transfer your contractual rights and responsibilities to another party.3 min read

A transfer of rights contract allows you to transfer your contractual rights and responsibilities to another party. Transferring contract rights can happen either through assignment or delegation.

Assigning Contractual Rights

If you want to transfer your contractual rights to another person, you will need to make an assignment. On the other hand, if you're only interested in transferring your contractual duties but not your rights, you would use a delegation. After an assignment takes place, full contractual rights will be transferred to the assignee. These will be the exact same rights as enjoyed by the original contracted party.

Free Contractor Agreement
Ad Fill in the Blanks and Create Y
Customized Contractor Agreemer
LawDepot
Open

If the contractual rights being transferred aren't personal, then the party assigning their rights does not need to obtain permission from the other contracted party. Permission is a requirement if the assignment involves personal services.

There are certain circumstances when assignment is not possible:

1. The contract prohibits assignment.
2. Assignment is illegal or violates public policy.
3. The assignment get rejected by a court.

Delegating Contractual Obligations

Delegation is much different than assignment. With a delegation, you are transferring the obligation of performance to another party. Basically, this means that another person is performing your contractual duties but you are still legally responsible for the contract. For instance, if you delegated a contractual payment, and that payment is not made, the other party in the contract can hold you liable for the missed payment.

Certain contractual obligations are not eligible for delegation. If completion of the contract requires special knowledge, skills, or talents, delegation is not allowed.

Making an Assignment

If you want to assign your contractual rights to another party, you can do so in writing or verbally depending on the laws in your state. Either way, you should give the other party in the contract notice that you are making an assignment. Once notice is sent, the other party can perform their contractual duties on your behalf.

After receipt of the notice, the other party should fulfill their responsibilities to the assignee instead.

Transferring Copyrights

A tricky situation when it comes to transferring contract rights is who has the ability to transfer a copyright. The basic rule is that the person that holds the copyright owns exclusive rights to the work covered by the copyright. This means that only the copyright holder may license the creative work. The only exception to this rule is when the person that created the copyrighted work did so in a work-for-hire situation. In this case, the organization that hired the creator would own the copyrights.

Copyrights are like other types of property in that the owner of the copyright can transfer these rights to owner person. Copyrights are transferrable in whole or in part. For example, if you are a photographer, copyright law would apply whether or not you were paid for your services.

If someone else copies, sells, or uses your copyrighted photograph without your permission, they have violated your copyright, which is illegal and may result in both criminal and civil penalties. Even if someone buys a copy of your photograph, this doesn't mean that you have transferred ownership of your copyright. The buyer would not have the right to reproduce your photograph or publish the image.

As a copyright holder, you have the ability to license your copyright or to transfer it to another person. You could grant a company a license to reproduce your photo, for example. Copyright owners can transfer exclusive rights to their property to another person. If you want to transfer exclusive rights to a copyright, you must do so in writing. Otherwise, the transfer would not be valid. This written transfer should include the copyright owner's signature.

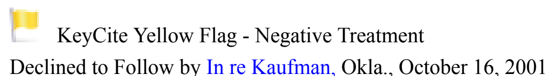
You do not need a written agreement when transferring non-exclusive rights to your copyright. If a copyright holder dies, ownership of the copyright can be transferred through a will or by the laws of succession.

Because a copyright is a type of personal property, state regulations and laws apply to copyright ownership. These laws also apply to transferring copyrights and inheritance of these property rights. If you have questions about which laws apply to transferring copyrights in your state, you should consult an attorney.

If you need help with a transfer of rights contract, you can post your legal needs on UpCounsel's marketplace. UpCounsel accepts only the top 5 percent of lawyers to its site. Lawyers on UpCounsel come from law schools such as Harvard Law and Yale Law and average 14 years of legal experience, including work with or on behalf of companies like Google, Menlo Ventures, and Airbnb.

Free Land Contract Forms Contract Form Template

LEGAL AUTHORITY AA-39


KeyCite Yellow Flag - Negative Treatment
Declined to Follow by In re Kaufman, Okla., October 16, 2001

32 F.Supp.2d 939
United States District Court,
E.D. Michigan,
Southern Division.

Chad J. WONSEY, Plaintiff,
v.
LIFE INSURANCE COMPANY OF NORTH AMERICA and Insurance Company of North America, Defendants.

No. CIV. 98–40239.
|
Dec. 18, 1998.

Synopsis

Beneficiary of annuity that was part of structured settlement of personal injury action brought action against insurers for declaratory judgment that anti-assignment clause was invalid. The District Court, Gadola, J., held as a matter of first impression that: (1) Uniform Commercial Code (UCC) provision on secured transactions did not apply, and (2) clause was unenforceable.

Judgment for beneficiary.

Attorneys and Law Firms

***939** Jeffrey D. Weisserman, Jaffe, Raitt, Detroit, MI, for Chad J. Wonsey, plaintiff.

Peter A. Davenport, Noeske & Abbo, Troy, MI, for Life Insurance Company of North America, Insurance Company of North America, defendants.

MEMORANDUM OPINION AND ORDER GRANTING PLAINTIFF'S MOTION FOR DECLARATORY JUDGMENT

GADOLA, District Judge.

On September 11, 1998, plaintiff Chad J. Wonsey filed a motion for declaratory judgment against defendants Life Insurance Company of North America ("Life") and Insurance Company of North America ("INA"). The Court is being called upon to determine whether Wonsey has the legal right to assign to a third-party specific future payments due him pursuant to an annuity contract purchased by Life in his name. Defendants have thus far refused plaintiff's request to assign the payments. On October 13, 1998, defendants filed their response to plaintiff's motion. On October 22, 1998, plaintiff filed his reply brief.

For the reasons set forth below, this Court will grant plaintiff's motion for declaratory judgment.

I. FACTUAL BACKGROUND

On December 15, 1980, Chad Wonsey sustained severe personal injuries as the result ***940** of an automobile accident in Genesee County, Michigan. At the time of the accident, Wonsey was a minor, approximately six years of age.[1] On December 8, 1983, Wonsey's parents, on his behalf, entered into a Settlement Agreement and Release with INA, insurer for Le–Rob Corporation ("LeRob"). *See* Exh. A to plaintiff's motion. Pursuant to the settlement agreement, and in consideration for the full settlement and release of plaintiff's claims against Le–Rob, INA agreed to make future payments to plaintiff according to an agreed upon schedule.[2] In order to facilitate payment of benefits, INA purchased an annuity contract on plaintiff from one of its affiliates, Life Insurance Company of North America.

On April 21, 1998, plaintiff, of adult age and legally competent to enter into contracts, entered into a Purchase Agreement with Singer Asset Financial Company, L.L.C. ("Singer"). *See* Exh. B to plaintiff's motion. The purchase agreement purported to assign specifically identified future payments from the annuity contract.[3] On the same date, plaintiff provided defendants with written notification of his decision to change the beneficiary designation of the settlement agreement and annuity contract to his estate. Plaintiff also directed defendants to change the address to which payments were to be forwarded and for defendants to acknowledge these changes in writing. *See* Exh. C to plaintiff's motion. To date, defendants have refused to comply with all of Wonsey's written requests, thereby impairing him from completing his assignment to Singer as envisioned in the purchase agreement.

It must also be mentioned that the settlement agreement dated December 8, 1983 provides that plaintiff shall have no right to change the beneficiary of the policy or to assign the policy. As the agreement states, "it is understood and agreed that the

Insurance Company of North America shall be the owner of the aforesaid annuity policy and the Plaintiffs should have: (1) no right to change the beneficiary of the policy...[and] (5) no right to assign the policy." *See* Exh. A to plaintiff's motion, p. 3.

II. DISCUSSION

The issue presented in the case at bar is whether the Court may set aside a provision in a structured settlement agreement which prohibits assignments of future payments to be made under an annuity policy. Plaintiff argues that he is entitled to assign all or part of his rights under the settlement agreement, despite the agreement's express language. In support of this position, plaintiff cites M.C.L. § 440.9318(4), Michigan's adoption of the Uniform Commercial Code's Article 9, Section 318(4), (hereinafter "Section 9–318(4)"). The Michigan statute provides that

> [a] term in any contract between an account debtor and an assignor is ineffective if it prohibits assignment of an account or prohibits creation of a security interest in a general intangible for money due or to become due or requires the account debtor's consent to such assignment or security interest.

M.C.L. § 440.9318(4). Plaintiff also points to the official comment to U.C.C. Section 9–318(4), which states that "[s]ubsection (4) breaks sharply with the older contract doctrines by denying effectiveness to contractual terms prohibiting an assignment...under contracts of sale, construction contracts and the like." The Restatement of Contracts (Second), Section 322, also lends support in that "a contract term prohibiting assignment of 'the contract' bars only the delegation to an assignee of the performance by the assignor of a duty or condition." RESTATEMENT (SECOND) OF CONTRACTS § 322(1).

Defendants' response centers upon the contention that Article 9 explicitly states that it does not apply to policies of insurance. ***941** *See* M.C.L. § 440.9104. As defendants note, Article 9 excludes from its scope "a transfer of an interest or claim in or under any *policy of insurance* except as provided with respect to proceeds...and priorities in proceeds...." M.C.L. § 440.9104 (emphasis added). Defendants further maintain that the language of the contract in this case is clear and unambiguous and must be enforced. Where a contract is not ambiguous, there is no room for construction. *See* *Reynolds Spring Co. v. L.A. Young Ind.,* 101 F.2d 257 (6th Cir.1939); *Stine v. Continental Casualty Co.,* 419 Mich. 89, 349 N.W.2d 127 (1984). Finally, defendants assert that assignments require a "complicated review process," whereby companies must "review substantial paper work" and determine whether the assignment appears to be legal. According to defendants, assignments should thus be disfavored, and are at odds with the intent of the parties. Defendants further maintain that assignments may be detrimental to beneficiaries who often suffer from the legal disabilities of minor status or physical and/or mental impairment.

1. WHETHER ARTICLE 9 OF THE U.C.C. APPLIES TO PLAINTIFF'S PROPOSED ASSIGNMENT OF FUTURE PAYMENTS UNDER THE SETTLEMENT AGREEMENT DATED DECEMBER 8, 1983

The issue presented is one of first impression for both state and federal courts located in Michigan. The critical question which first must be answered is whether Article 9 applies at all to plaintiff's proposed assignment of future payments. As mentioned above, if plaintiff is attempting to transfer "an interest or claim in or under [a] policy of insurance," then, with certain exceptions, Article 9 would not apply to a determination of the enforceability of the nonassignment clause. *See* M.C.L. § 440.9104(g). On the other hand, if the Court finds that plaintiff is not attempting to transfer an interest in a policy of insurance, then Article 9 would be applicable, and the non-assignment clause would be unenforceable pursuant to M.C.L. § 440.9318(4). [4]

The exclusionary language of Article 9 is clear. Although the cases are not plentiful, courts have applied Section 9–104(g) to exclude various transactions from the scope of Article 9. In *In re Duke Roofing Co.,* 47 B.R. 990 (E.D.Mich.1985), for example, the court excluded from Article 9 an assignment of unearned insurance premium refunds. Insurance payments will *not* be excluded, however, where such payments qualify as "proceeds" under Article 9. [5] This is the so-called "derivative insurance proceeds" rule, which only applies in the event of casualty loss of collateral subject to a previously perfected security interest. [6] The "derivative insurance proceeds" rule, however, is not applicable in the case at bar because the future payments

***942** at issue do not constitute "proceeds," i.e., they are not payable by reason of loss or damage to previously secured collateral. *See* M.C.L. § 440.9306.

In the instant case, payments are to be made pursuant to a structured settlement agreement entered into between plaintiff Chad Wonsey's parents and the Insurance Company of North America (INA). As the agreement explicitly states, "[INA] shall, in order to facilitate the payment of benefits specified herein, purchase...an annuity contract on the life of Chad Wonsey from Life Insurance Company of North America...." *See* Exh. A to plaintiff's motion, p. 2. The question thus becomes whether such an "annuity contract" qualifies as a "policy of insurance" under 9–104(g). Under Michigan law, it appears that an annuity contract does come within the definition of a "policy of insurance." *See* M.C.L. § 500.4000 *et seq.* (governing life insurance policies and certain annuity contracts); *see also* BLACK'S LAW DICTIONARY 90 (6th ed.1990)(defining "annuity policy" as "[a]n insurance policy providing for monthly or periodic payments to insured to begin at fixed date and [to] continue through insured's life"). As such, plaintiff is therefore precluded from invoking Article 9. Section 9–318(4) may not operate, in and of itself, to nullify the settlement agreement's prohibition on assignments. *See* M.C.L. § 440.9318(4).

2. SINCE ARTICLE 9 IS INAPPLICABLE, THE COURT MUST LOOK TO OTHER MICHIGAN STATUTORY LAW AND/OR THE COMMON LAW OF MICHIGAN, AS WELL AS TO ANY DEVELOPING TRENDS IN OTHER JURISDICTIONS

In a case, such as the present one, where Article 9 has been held inapplicable, the court must apply state statutory law. *See In re Duke Roofing Co.,* 47 B.R. 990, 992 (E.D.Mich.1985)(citing *Thico Plan, Inc. v. Maplewood Poultry Co.,* 2 B.R. 550, 555 (Bankr.D.Me.1980)). In the case at hand, there is no Michigan statute which definitively resolves the issue presently before the Court. Consequently, this Court will look to Michigan common law, as well as to any developing trends in other jurisdictions. *See id.*

Plaintiff has cited no Michigan case law addressing the issue of whether a court may set aside an anti-assignment provision in a structured settlement agreement providing for future payments to be made under an "annuity policy." Other jurisdictions, however, have dealt with similar issues. In *Berkowitz v. Haigood,* 256 N.J.Super. 342, 606 A.2d 1157 (N.J.Super. Ct. Law Div.1992), plaintiff, a chiropractic doctor, rendered medical services to defendant after the latter was involved in an automobile accident. *Id.* at 344, 606 A.2d 1157. Defendant had signed a document which purported to create a lien against the proceeds of his pending personal injury action. The document directed defendant's attorney to disburse the funds to plaintiff if certain conditions were satisfied. The New Jersey state court held that any proceeds derived from defendant's settlement of his claim for personal injuries were assignable. However, *Berkowitz* does not dispose of the issue in the instant case because the settlement agreement in *Berkowitz* contained no anti-assignment clause.

In *Fox–Greenwald Sheet Metal Co. v. Markowitz Bros.,* 452 F.2d 1346 (D.C.Cir.1971), the district court addressed a similar issue in the context of a subcontractor's assignment. The subcontract in *Fox–Greenwald* contained a clause prohibiting assignments, which the court, after careful consideration of Maryland law, found to be inoperative. In reaching its decision the court engaged in the following commentary:

> *[j]udicial holdings sustain overwhelmingly the proposition that a contractual ban on assignment ordinarily serves to protect the obligor alone, and in no way imperils the transaction as between assignor and assignee.* "Where a term in a contract prohibits assignment and is not rendered ineffective by statute or otherwise, the term is to be construed, unless a different intention is manifested, ...to be for the ***943** benefit of the obligor, *and not to prevent the assignee from acquiring rights against the assignor ....*" The obligor, of course, may gain from a valid and unwaived nonassignability provision the prerogative to resist or even nullify the assignment. That does not mean, however, that the assignee cannot compel the assignor to stand by his bargain where the obligor has not seen fit to interfere. And perhaps nowhere has the rule that an assignment offending such a provision normally binds the assignor to the assignee seen greater application than where the assigned claim was for monies due or to become due under a contract.

Fox–Greenwald, 452 F.2d at 1351 (footnotes omitted and emphasis added). The holding in *Fox–Greenwald* has been codified in Restatement of Contracts (Second), Section 322(1), which states that "[u]nless the circumstances indicate the contrary, a contract term prohibiting assignment of 'the contract' bars only the delegation to an assignee of the performance by the assignor of a duty or condition." RESTATEMENT (SECOND) OF CONTRACTS § 322(1). Even more to the point is Section 322(2), providing that "[a] contract term prohibiting assignment of rights under the

contract, unless a different intention is manifested...is for the benefit of the obligor, and *does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition.*" *Id.* § 322(2)(c).

As the latest Restatement makes clear, the *modern trend* with respect to contractual prohibitions on assignments is to interpret these clauses narrowly, as barring only the delegation of duties, and not necessarily as precluding the assignment of rights from assignor to assignee. The rationale behind these cases is derived from the implicit recognition that the obligor, the party obligated to perform, would not suffer any harm by a mere assignment of payments under a contract. Harm to obligor would result, however, in cases involving personal services contracts or other situations where the duties owed to the parties may change depending on the identity of the assignee. *See Hy King Assocs. v. Versatech Manufacturing Industries,* 826 F.Supp. 231, 238 (E.D.Mich.1993)(Gadola, J.)(holding that under Michigan law, there was no valid assignment of exclusive sales representation contract between manufacturer and representative to corporation formed by representative).

The instant case does not involve a situation where significant harm would result to defendant Life or defendant INA by the proposed assignment of rights to future payments. Nor is this a situation involving a delegation of duties under a personal services contract. Nonetheless, defendants strenuously argue that when a beneficiary of a structured settlement agreement decides to sell all or a number of his future payments, "it requires a complicated review process" and that "defendants [would be required] to review substantial paper work, and [to] determine if the assignment appears to be legal...and/or whether any guarantees or releases provided by the assignor... are satisfactory to fully and completely protect [defendants]...." The Court is not persuaded. The reasons asserted by defendants in objecting to the proposed assignment do not appear to amount to substantial harm or actual prejudice to defendants' interests, but merely center upon the necessary administrative tasks associated with the assignment's implementation. As such, defendants have not submitted sufficient reasons to justify disregarding the modern trend of upholding assignments in the face of contractual anti-assignment clauses.

Plaintiff's position is further bolstered by several recent unpublished state court decisions recognizing a plaintiff's right to assign payments under a settlement agreement. *See Owen v. Continental Casualty Co.,* Docket No. L–3196–98 (Super.Ct.N.J. Sept. 23, 1998); *Horn v. Amica Mutual Ins. Co.,* Case No. 173646 (Super.Ct.Ca. Sept. 21, 1998); *JUA Funding Corp. v. CNA Ins.,* Docket No. L–10824–97 (Super. Ct. N.J. June 3, 1998); *In re Donna M. Meisinger,* Case No. 98MR45 (Chancery Div. Il. Apr. 2, 1998); *In re Joann Minson,* Case No. 98–P–104 (Probate Div. Il. Apr. 3, 1998); *Rusyn v. Travelers Casualty and Surety Co.,* Case No. RIC 311592 (Super.Ct.Ca. November 5, 1998). Although the *Owen* and *JUA Funding* decisions expressly rely upon New Jersey's version of Article 9, the other cases cited above ***944** do not specifically reference that provision. Most persuasively, the California state court in *Rusyn* allowed plaintiff to assign his interest in structured settlement benefits. The court held that the prohibition set forth in the settlement agreement regarding the assignment of the rights to periodic payments is "void and of no force or effect." *See Rusyn* ¶ 1(a).

At the hearing held on December 16, 1998, defendant was able to cite only one case wherein a court has prohibited assignment of periodic payments under a structured settlement agreement. *See Johnson v. First Colony Life Ins. Co.,* 26 F.Supp.2d 1227 (C.D.Ca.1998). In that case, the parties entered into an agreement containing a "non-assignability clause," in settlement of a personal injury claim. The district court ultimately granted defendants' motion for summary judgment, and thus denied plaintiffs' request to assign the periodic payments. Although the facts in *Johnson,* at first blush, appear similar to those of the instant case, there is a crucial difference which serves to distinguish the two cases. In *Johnson,* the court placed great weight on the fact that

> plaintiffs never explain how an express prohibition against assignment...is beneficial to them. To the contrary, it seems plain that, because the clause mirrors language in [Internal Revenue Code] § 130, relating to the tax treatment of the assignee of the liability, the clause was included solely for the benefit of the defendants.

Id. at 1229–30. In the case at bar, by contrast, plaintiff has been able to "overcome the presumption" that the nonassignability clause is for the benefit of defendants. *See id.* at 1230. As previously discussed, plaintiff was a nine

year old minor child at the time of the execution of the original settlement agreement. There has been no showing or suggestion that the anti-assignment clause in this case was designed as a tax benefit for defendants. Rather, it appears more likely to have been seen as a protective measure to safeguard the interests of plaintiff, until such time as he reached adulthood. Given this critical factual difference distinguishing the two cases, this Court is not persuaded to follow the *Johnson* court's rationale motivating its denial of plaintiffs' request to assign future periodic payments.

In light of plaintiff's strong showing of a modern trend in other jurisdictions favoring the assignment of periodic payments under structured settlement agreements, the prohibitions against such assignments having been held to be unfair restraints on alienation, this Court will grant plaintiff's motion for declaratory judgment. As discussed above, this is not a situation involving a delegation of duties under a personal services contract. Moreover, defendants' argument of prejudice allegedly resulting from the assignment is unconvincing. Accordingly, defendants Life Insurance Company of North America and Insurance Company of North America will be instructed to honor the proposed assignments of future payments to Singer Asset Financial Company, L.L.C.

ORDER

NOW, THEREFORE, IT IS HEREBY ORDERED that plaintiff Chad J. Wonsey's motion for declaratory judgment is **GRANTED**; a declaratory judgment in accordance with this order shall be entered forthwith.

SO ORDERED.

DECLARATORY JUDGMENT

The Court, having granted plaintiff Chad J. Wonsey's motion for declaratory judgment, and after a hearing conducted on December 16, 1998, the Honorable Paul V. Gadola, presiding,

It is hereby **ORDERED** that defendants Life Insurance Company of North America and Insurance Company of North America shall honor plaintiff's assignment of contract rights to Singer Asset Financial Company, L.L.C.;

It is further **ORDERED** that defendants shall honor and process plaintiff's change of beneficiary and mailing address;

It is further **ORDERED** that the respective parties shall be liable for their own costs and attorneys' fees.

All Citations

32 F.Supp.2d 939, 38 UCC Rep.Serv.2d 619

Footnotes

1 Plaintiff Chad Wonsey was born on September 11, 1974.

2 The following schedule of payments was agreed upon:

$9,000 at age 18; $10,000 at age 19; $11,500 at age 20; $13,000 at age 21; $20,000 at age 25; $30,000 at age 30; $44,000 at age 35; $63,500 at age 40; $94,500 at age 45; $149,750 at age 50.

Settlement Agreement dated December 8, 1983, Exh. A to plaintiff's motion.

3 The future payments subject to assignment were (1) the $20,000 payment due September 11, 1999, the $30,000 payment due September 11, 2004, and the $44,000 payment due September 11, 2009.

4 It should be noted that Article 9 “applies to security interests created by contract including pledge, *assignment,* chattel mortgage, chattel trust, trust deed, factor's lien, equipment trust, conditional sale, trust receipt, other lien or title retention contract, and lease or consignment intended as security.” M.C.L. § 440.9102(2)(emphasis added). In the instant case, as per the Purchase Agreement dated April 21, 1998, Wonsey has attempted to *assign* certain assets (i.e., the future payments) to Singer Asset Finance and thereby has attempted to grant Singer a security interest in said payments. *See* Exh. B to plaintiff's motion, ¶ 2.

 © 2020 Thomson Reuters. No claim to original U.S. Government Works.

5 "Proceeds" are defined as "whatever is received upon the sale, exchange, collection or other disposition of collateral, or proceeds. *Insurance payable by reason of loss or damage to the collateral is proceeds, except to the extent that it is payable to a person other than a party to the security agreement.*" M.C.L. § 440.9306 (emphasis added).

6 As one bankruptcy court in Minnesota noted,

> UCC section 9–104(g) provides that Article 9 does not apply to any "interest or claim in or under" an insurance policy. *See* Minn.Stat. § 336.9–104(g). The only exception is in the case of so-called "derivative insurance proceeds." The reason for the derivative insurance proceeds exception is that a creditor's Article 9 security interest normally extends to the proceeds of its collateral as well as the collateral itself. *See* Minn.Stat. § 336.9–306(2). Where the creditor requires the debtor to insure the collateral and the collateral is subsequently destroyed, the insurance proceeds are in essence proceeds from the disposition of the collateral. *See* *PPG Industries, Inc. v. Hartford Fire Ins. Co.,* 531 F.2d 58, 60–61 (2d Cir.1976); *In re Reda, Inc.,* 54 B.R. 871, 875 (Bankr.N.D.Ill.1985). In such a case section 9–306(1) makes clear that these "derivative insurance proceeds" are to be treated the same as any other proceeds of the collateral. Minn.Stat. § 336.9–306(1).

In re Investment and Tax Svs., Inc. v. Norwest Bank Minn., N.A., 148 B.R. 571, 573 (Bankr.D.Minn.1992).

End of Document

© 2020 Thomson Reuters. No claim to original U.S. Government Works.