THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

William H Seals, Jr., Circuit Court Judge

Appellate Case No. 2019-001419

Nancy Callaghan ..... Respondent

v.

Five Star Quality Care, Inc., Five Star Quality Care-OBX Operator, LLC d/b/a Sweetgrass Court Senior Living Community, Sweetgrass Village Assisted Community, Lisa McLeod and Derrick Defino ..... Appellants.

RESPONDENT'S INITIAL BRIEF

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1. Whether the long-standing "outrageous tort" exception, based on generally applicable contract interpretation principles, applies to a vulnerable adult's claim that the operators of the nursing home where she resided intentionally harbored a known sexual predator who assaulted her.
2. Whether the circuit court correctly applied the restrictive party definitions and highlighted language chosen by the nursing home to find an arbitration contract may not be enforced by non-parties.

STATEMENT OF THE CASE

Respondent Nancy Callaghan alleges claims for negligence, negligence per se, fraud/misrepresentation, and violations of the South Carolina Unfair Trade Practices Act ("SCUTPA") arising out of a sexual assault she suffered while a resident at Sweetgrass Village Assisted Living Community ("the Facility") in Mt. Pleasant, South Carolina. Her claims are asserted against multiple individuals or entities with decision making power over the Facility's operations including Appellants Five Star Quality Care, Inc. ("Five Star Inc."), Five Star Quality Care-OBX Operator, LLC d/b/a Sweetgrass Court Senior Living Community, Sweetgrass Village Assisted Living Community, Lisa McLeod, and Derrick Defino. (Compl. ¶¶ 2-7).

In October 2016, Ms. Callaghan's family began searching for an assisted living center for her since dementia and other health issues prevented Ms. Callaghan from continuing to live at home. (Compl. ¶¶ 17-18). Personnel at the Facility assured Ms. Callaghan and her family the Facility could provide the care and services she needed in an environment that allowed her to maintain her privacy and dignity. (Compl. ¶ 22). However, at the same time, Defendants knew a repeated sexual abuser was residing in the Facility. (Compl. ¶¶ 42-44; 49). This individual had assaulted residents twice in April 2016. (Compl. ¶ 44). The Facility's management-level personnel were aware of these prior attacks and that the perpetrator's own doctor recommended the perpetrator be removed from the facility. (Compl. ¶¶ 45-46).

Despite these dangers, Appellants did nothing to protect current residents or to warn potential residents and their families. (Compl. ¶ 47). In fact, Appellants allegedly took efforts to conceal the incidents by omitting them from medical records and refusing to report them to the South Carolina Department of Health and Environmental Control ("DHEC"). (Compl. ¶¶ 50-52). On November 24, 2017, just over a month after she moved to the Facility, Ms. Callaghan was

sexually assaulted by the same perpetrator. (Compl. ¶ 41). Ms. Callaghan alleges she suffered severe physical, emotional, and psychological losses as a result of the attack. Defendants served a joint Answer admitting the perpetrator was involved in prior "incidents" at the Facility (Answer ¶ 44) but denying Ms. Callaghan's allegations in other material respects.

On the same day as their Answer, Appellants filed a motion to dismiss and compel arbitration, relying on an arbitration contract ("Arbitration Agreement" or "the Agreement") signed by Ms. Callaghan's husband and a Five Star Inc. sales counselor. None of the other Appellants signed the Arbitration Agreement and none were included in the Agreement's definition of "Parties." (Arbitration Agreement at 1). The Agreement only requires arbitration for disputes "between the Parties" and the arbitration panel's rulings are only "binding upon the Parties." (Arbitration Agreement ¶¶ 1, 2). The Arbitration Agreement also purports to prohibit arbitrators from awarding "punitive or exemplary damages." (Arbitration Agreement ¶ 2).

The Honorable William H. Seals, Jr. held a hearing a motion on Appellants' motion on March 14, 2019, and issued an order denying the motion on July 23, 2019. (Order denying motion to compel arbitration). Appellants filed a timely notice of appeal.

STANDARD OF REVIEW

A circuit court's order denying arbitration is immediately appealable. Cape Romain Contractors, Inc. v. Wando E., LLC, 405 S.C. 115, 121, 747 S.E.2d 461, 464 (2013). Arbitrability determinations are subject to *de novo* review. Dean v. Heritage Healthcare of Ridgeway, LLC, 408 S.C. 371, 759 S.E.2d 727 (2014) (citing Bradley v. Brentwood Homes, Inc., 398 S.C. 447, 453, 730 S.E.2d 312, 315 (2012)). However, the circuit court's factual findings may not be reversed on appeal if "any evidence reasonably supports the findings." Id. While both federal and South Carolina policy favors arbitration of disputes, "a party cannot be

required to submit to arbitration any dispute which he has not agreed so to submit." Int'l Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH, 206 F.3d 411, 416 (4th Cir. 2000). Ultimately, arbitration "is a matter of consent, not coercion." Volt Information Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ., 489 U.S. 468, 479 (1989).

ARGUMENT

Appellants ignored DHEC regulations and willfully harbored a known sexual predator ("the Perpetrator") in the Facility inhabited by elderly women powerless to protect themselves. (Compl. ¶¶ 24-26; 31; 43). Appellants retained the Perpetrator in the Facility against his own doctor's wishes so Appellants could continue profiting from his presence. (Compl. ¶¶ 46-47). Appellants defied their regulatory duty to report the Perpetrator's known history of abuse both to avoid scrutiny and possible sanction from the state but also to falsely portray a façade of safety to the next family considering the Facility as their vulnerable loved one's new home. (Compl. ¶¶ 50-52). Respondent Nancy Callaghan was the latest of the Perpetrator's victims, sexually assaulted after his previous offenses were well-known but unreported by Appellants and after Appellants specifically represented the Facility was a safe place for Ms. Callaghan to live with the difficult realities of her dementia diagnosis. (Compl. ¶¶ 37, 41).

The key question before the circuit court was whether these allegations against Appellants would constitute an "outrageous tort." The circuit court correctly concluded they would. In asking the Court to force Ms. Callaghan into arbitration (and to prevent her from even seeking punitive damages), Appellants do not so much contest the outrageousness of the allegations against them as they attack the legitimacy of South Carolina's "outrageous tort" exception to arbitration. But, that exception, recently reaffirmed by the Supreme Court, is well grounded in core contract interpretation principles. Courts interpret every contract in a manner

that carries out the parties' expectations for the relationship they intend to form. Drawing on South Carolina precedent applying the exception as well as a wide body of persuasive authority, the circuit court correctly concluded that turning a blind eye to sexual predation could not have fallen within any party's expectation for the ordinary business relationship Appellants formed with Ms. Callaghan. Accordingly, the circuit court properly applied state law and properly respected federal law when ruling even the most broadly worded arbitration provision could not have intended to capture Ms. Callaghan's current claims.

Additionally, the circuit court correctly found the Arbitration Agreement could not be enforced by Appellants Sweetgrass Village Assisted Living Community, Lisa McLeod, or Derrick Defino because none of them were parties to the Agreement. While each points to one portion of the Arbitration Agreement, claiming it extends the contract to related entities, the contract overall does not support that interpretation because only the Agreement's narrowly-defined "Parties" would be bound by an arbitrator's ruling and the bolded, underlined text right above Ms. Callaghan's signature block assures her arbitration may be enforced "by the parties." At best for these Appellants, this form contract of adhesion is ambiguous on this point and was properly interpreted in Ms. Callaghan's favor.

1. The Circuit Court Correctly Concluded that Willfully Harboring a Known Sexual Abuser would be an Outrageous Tort.

Nursing home residents' claims typically make allegations of negligence related to resident care errors such as preventable falls, malnutrition, or the development of painful bedsores. As Ms. Callaghan's counsel told the circuit court, were those the claims Ms. Callaghan alleged here, she would not have raised a scope objection to arbitration. (Hearing Tr. at 9, line 23 – 10, line 5). However, Appellants' wrongful retention of a known sexual abuser in contravention of his doctor's wishes was legally distinct from the contractual relationship they

formed with Ms. Callaghan. Moreover, no reasonable person in Ms. Callaghan's position could conceive she would suffer a sexual assault in Appellants' facility as a result of such bizarre and egregious misconduct.

Appellants take issue with the manner in which the circuit court determined Ms. Callaghan's claims were not within the Arbitration Agreement's scope. But, the circuit court correctly applied South Carolina contract law which is in no way at odds with the Federal Arbitration Act (9 U.S.C. § 1 to 16) ("FAA"). No matter how broadly worded an arbitration contract is written, generally applicable contract law holds that its scope cannot be unbounded. Landers v. Fed. Deposit Ins. Corp., 402 S.C. 100, 115, 739 S.E.2d 209, 217 (2013) ("even the broadest of [arbitration] clauses have their limitations"). Not even the broadest arbitration provision applies when the claim and the parties' contract lack a "significant relationship." Aiken v. World Fin. Corp. of S.C., 373 S.C. 144, 151, 644 S.E.2d 705, 709 (2004). In defining "significant relationship," the South Carolina Supreme Court adopted, and later affirmed, a rule holding that, at the very least, the relationship does not exist for "outrageous torts that are unforeseeable to a reasonable consumer in the context of normal business dealings." Id.; Parsons v. John Wieland Homes & Neighborhoods of the Carolinas, Inc., 418 S.C. 1, 791 S.E.2d 128 (2016).

Appellants err in arguing this "outrageous tort exception" violates the FAA because in reality the exception is grounded in generally applicable contract interpretation principles applied by many other courts just using different labels. In fact, as some courts have held, reading arbitration provisions as broadly as Appellants suggest would itself violate the FAA. The Court should also reject Appellants' contention that the circuit court's application of the exception is an unreasonable expansion of the doctrine beyond its roots in Aiken and progeny. Appellants have

not shown how intentionally harboring a sexual abuser is significantly related to a nursing home's relationship with its resident.

a. The Outrageous Tort Exception is a Valid Component of South Carolina Contract Law and Consistent with the FAA.

Appellants brand the outrageous tort exception as a facially anti-arbitration anomaly of South Carolina law that violates the FAA's "equal-treatment principle." Appellants Br. at 7 n. 5 (citing Kindred Nursing Ctrs., Ltd. P'ship v. Clark, 137 S. Ct. 1421, 1426 (2017) and AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 339 (2011)). Appellants go on to argue Aiken and Parsons should both be overturned. Appellants Br. at 7 n. 5; at 8 n. 8. These arguments against precedent are misguided because they misunderstand where the exception comes from and what the "equal-treatment principle" truly means. As Justices Hearn, Beatty, and Toal explained in Parsons, the outrageous tort exception is borne out of the intent and mutual assent considerations courts apply to every contract. 418 S.C. at 13-14, 17, 791 S.E.2d at 135-36. Additionally, calling these considerations an "exception" to arbitration does not violate the equal-treatment principle which permits courts to "announc[e] a new, generally applicable rule of law in an arbitration case" so long as the rule is in fact generally applicable. Kindred Nursing, 137 S. Ct. at 1428 n. 2.

Ms. Callaghan agrees with Appellants that the core of contract interpretation is effectuating the parties' intent. But, before interpreting a contract, a court must first be satisfied a contract was formed by the parties—i.e. the formation of a "meeting of the minds" in which the parties mutually assented to all of the contract's material terms. Anderson Mem'l Hosp., Inc. v. Hagen, 313 S.C. 497, 498 n. 1, 443 S.E.2d 399, 400 n. 1 (Ct. App. 1994). The outrageous tort exception is a natural outgrowth of the intent rule and the mutual assent requirement. In Aiken, employees of a consumer lender were accused of taking borrowers' personal identifying information (e.g. social security numbers and dates of birth) and misappropriating them to obtain

sham loans in the borrowers' name. 373 S.C. at 146-47, 644 S.E.2d at 707. Borrowers alleged negligent and intentional tort claims against the lender, which defended by citing an arbitration provision in the lender's legitimate loan contract with each borrower. Id. The Court was tasked with determining whether the admittedly broad arbitration provision from the borrower-lender contract extended to cover the borrower's claims based on the brazen but unrelated misconduct of the lender's employees. Id. at 147, 644 S.E.2d at 708.

Accordingly, Aiken presented a garden-variety contract interpretation question and was resolved using standard contract interpretation rules. Id. at 151, 644 S.E.2d at 709 (couching its holding in "general principles of contract law"). The Court first evoked the mutual assent requirement to conclude a person "cannot be required to submit to arbitration any dispute which he has not agreed to submit." Id. at 149, 644 S.E.2d at 708 (citing Zabinski v. Bright Acres Assocs., 346 S.C. 580, 596, 553 S.E.2d 110, 118 (2001)). Thus, fully crediting state and federal pro-arbitration policy, Aiken held that "even the most broadly-worded arbitration agreements still have limits." Aiken, 373 S.C. at 151, 644 S.E.2d at 709; see also Landers, 402 S.C. at 115, 739 S.E.2d at 217. The "significant relationship" test[1] Aiken applied for determining a broadly worded arbitration contract's limits is simply an application of the mutual assent rule that applies to every contract regardless of its subject matter. Since the outrageous tort exception is just an elaboration of the significant relationship test, it too is directly connected to the mutual assent requirement of contract formation. Aiken, 373 S.C. at 151, 644 S.E.2d at 709 (describing exception as a "more definitive rule" for applying significant relationship test).

[1] The "significant relationship" test is not a South Carolina-specific rule. Many other jurisdictions use this analysis to determine the boundaries of a broadly worded arbitration provision. See e.g. Wachovia Bank, N.A. v. Schmidt, 445 F.3d 762, 767 (4th Cir. 2006) (quoting J.J. Ryan & Sons v. Rhone Poulenc Textile, S.A., 863 F.2d 315, 321 (4th Cir. 1988)); Jackson v. Shakespeare Found., Inc., 108 So.3d 587, 593 (Fla. 2013); Griggs v. Evans, 43 A.3d 1081, 1088 (Md. App. 2012).

The connection between core contract rules and the outrageous tort exception is further evidenced by the three post-Aiken cases applying the exception. All three held the exception was nothing more than an application of the rule requiring courts to interpret a contract consistently with its parties' intent. In Chassereau v. Global Sun Pools, Inc., 373 S.C. 168, 644 S.E.2d 718 (2007), a woman who financed a swimming pool was not compelled to arbitrate her claim that the pool seller's agents defamed and harassed her when she fell behind on her payments. Chassereau examined the broadly worded arbitration provision carefully but, given the lack of connection between the sales contract and the defamation claim, the court was left with "no doubt that [the woman] *did not intend to arbitrate*" the claim. 373 S.C. at 172, 644 S.E.2d at 721 (emphasis added); see also Partain v. Upstate Automotive Group, 386 S.C. 488, 689 S.E.2d 602 (2010) (holding that a car buyer "did not intend to submit" to arbitration his claim that a dealer maliciously switched the agreed-upon car with an inferior model).

Similarly, this Court has held that an arbitration provision in a financial services contract between investor and advisor did not cover negligence or consumer fraud claims because the prospect of an advisor converting his client's funds for personal use was "not within the parties' contemplation" when the contract was formed. Hatcher v. Edward D. Jones & Co., L.P., 379 S.C. 549, 554, 666 S.E.2d 294, 297 (Ct. App. 2008) (finding misconduct underlying negligence claim was "completely outside the expectations of the parties at the time the contract was entered"). Hatcher went one step further, holding that to interpret a broadly worded arbitration provision to apply to claims wholly unforeseeable at contract formation would be inconsistent with pro-arbitration policy by contravening the parties' intentions. Id.

The exception's proven pedigree as a general contract law principle is what led the majority of the Court in Parsons to reject the equal-treatment principle argument Appellants raise

here. Both Justice Hearn (joined by Justice Beatty) and Acting Justice Toal believed the "exception" may be inartfully named but its underlying legal principles "are equally applicable to contracts and arbitration agreements." 418 S.C. at 13 n. 9, 791 S.E.2d at 134 n. 9; Id. at 17, 791 S.E.2d at 136 (Toal, A.J., dissenting) (describing "exception" as "merely a label" for "effectuating the parties' contractual expectations"). Along with the intent and assent principles discussed above, Justice Hearn made special reference to courts' refusal to interpret contracts in a way that could lead to an absurd result and cited non-arbitration cases where the same principle was applied. 418 S.C. at 14 n. 9, 791 S.E.2d at 135 (citing Koon v. Fares, 379 S.C. 150, 155, 666 S.E.2d 230, 233 (2008) and Auto Owners Ins. Co. v. Rollison, 378 S.C. 600, 609, 663 S.E.2d 484, 488 (2008)).

In sum, the outrageous tort exception fully comports with the FAA's equal-treatment principle because it is derived from general contract law rules applying beyond arbitration contracts. If there has been any mistake in Aiken and its progeny, it has been in stating or implying that refusing to force arbitration for wholly unforeseeable torts was either new in Aiken or is an "exception" to arbitration. As the majority held in Parsons, this principle is not new or arbitration-specific but merely a means to accomplish the core goal of contract law which is to make parties' expectations and intent the top priority.

b. The Outrageous Tort Exception was Properly Applied to Ms. Callaghan's Claims.

Appellants next argue that, even if the outrageous tort exception is valid, it does not apply here because Appellants choosing to retain the Perpetrator against his doctor's recommendation and to effectively grant the Perpetrator access to the Facility's female residents was "central" to the contractual relationship Appellants formed with Ms. Callaghan. Appellants Br. at 9. However, as alleged in the Complaint, the required connection between claim and contract is

even weaker here than in previous cases applying the exception. In fact, the circuit court cited a number of analogous cases finding sexual assaults to be outside the scope of broad arbitration agreements. Thus, while the alleged assault on Ms. Callaghan happened when she was a resident of Appellants' Facility, the misconduct leading to it bears little connection to the contractual relationship the parties formed and was beyond what any reasonable person could have foreseen when the relationship began.

Ms. Callaghan agrees with Appellants that the exception requires consideration of factors including whether the claim arises from behavior that was (1) beyond the contemplation of the parties at contract formation; (2) "legally distinct" from the contractual relationship the parties formed; and (3) "wholly unexpected." Appellants Br. at 8-9 (citing Parsons, 418 S.C. at 14, 791 S.E.2d at 135 and Aiken, 373 S.C. at 151, 644 S.E.2d at 709). Appellants argue Ms. Callaghan's claims do not meet these standards because both her claims and the parties' relationship are related to resident safety. Appellants' Br. at 9. Appellants also assert that previous cases applying the exception are distinguishable because Ms. Callaghan does not allege intentional misconduct. Id. Finally, Appellants contend the circuit court conflated their conduct with the Perpetrator's, improperly charging them with the outrageous acts of this "unrelated third-party." Appellants' Br. at 10. Appellants' arguments fail to fully credit Ms. Callaghan's Complaint allegations and to properly apply the applicable law. Each argument will be addressed in turn.

Appellants first point to Ms. Callaghan's Complaint, arguing she alleges a specific connection between her claims and her relationship with Appellants by asserting the parties' relationship was based on Appellants making a promise to provide Ms. Callaghan a safe environment which Appellants breached by maintaining an unsafe environment. Appellants' Br. at 9. This argument misconstrues and oversimplifies the Complaint allegations. Ms. Callaghan

does not allege the Facility was the typical unsafe nursing home environment with, for example, slippery floors, defective bed rails, or malfunctioning bed alarms. Instead, the Complaint alleges Appellants created danger for all residents in their interactions with the Perpetrator through administrative decisions of top-level executives in violation of state law and regulatory requirements. Appellants knew since the Perpetrator's admission that his proclivities meant the Facility could not properly care for him. (Compl. ¶ 42). After improperly admitting the Perpetrator, Appellants compounded their error by ignoring two instances when he sexually assaulted other residents and multiple incidents of inappropriately touching staff members. (Compl. ¶ 44, 54). Appellants did not note these incidents in the Perpetrator's file or change their approach for caring for him. (Compl. ¶¶ 50-51).

What followed was a bureaucratic failure grounded in profit-motivated decisions. The Facility's middle and upper management knew of the Perpetrator's actions. (Compl. ¶ 45). Appellant Derrick Defino, the Facility's regional director, was briefed on the incidents and specifically told a doctor concluded the Perpetrator could no longer safely remain in the Facility. (Compl. ¶ 46). Defino chose to retain the Perpetrator, effectively overruling the doctor and ignoring a similar recommendation from the Facility's residential services director. Id. Appellants calculated that it was to their financial benefit to keep the Perpetrator in the Facility rather than transferring him to an institution with more security and a higher level of care. (Compl. ¶¶ 43, 55). Admitting the Perpetrator, retaining him in the Facility, and refusing to alter his care plan in response to his sexual assaults all violated state statutory or regulatory requirements. (Compl. ¶¶ 31, 51). These errors were a direct and proximate cause of the assault on Ms. Callaghan. (Compl. ¶¶ 56, 62, 68, 78-79, 87).

Since the Complaint's allegations center on Appellants' series of bad choices and regulatory violations relative to the Perpetrator's serial sexual misconduct, the Court should reject Appellants' argument that Ms. Callaghan's claims "are the very essence of arbitrable claims in this context." Appellants' Br. at 9. Appellants cannot show a "significant relationship" between the claims and the Arbitration Agreement simply by noting Ms. Callaghan sought safety at Appellants' facility and that she alleges the odd sequence of events leading to her assault were safety violations. Aiken found such an overly broad view of the required causal connection would be "illogical and unconscionable." 373 S.C. at 150, 644 S.E.2d at 708 (citing Seifert v. U.S. Home Corp., 750 So.2d 633, 638 (Fla. 1999) ("the mere fact that the dispute would not have arisen but for the existence of the contract relationship between the parties is insufficient by itself to transform a dispute into one 'arising out of or relating to' the agreement"); see also Hatcher, 379 S.C. at 553, 666 S.E.2d at 297 (quoting Aiken).

Similarly, the Court should reject Appellants' simple syllogism implying Ms. Callaghan's claims cannot be "legally distinct" from those covered by the Arbitration Agreement because her claims relate to her time at Appellants' Facility and the Arbitration Agreement was signed in connection with her admission to the Facility. The "legally distinct" element of the outrageous tort exception analysis, when read in full, provides that arbitration may not be compelled when the alleged misconduct is "legally distinct from the *contractual* relationship between the parties." Aiken, 373 S.C. at 151, 644 S.E.2d at 709 (emphasis added). None of Ms. Callaghan's claims are based on breaches of contractual duties. Compl. ¶¶ 19-20 (alleging Appellants had "special relationship" with Ms. Callaghan and "voluntarily undertook a duty"); see also Hodge v. UniHealth Post-Acute Care of Bamberg, LLC, 422 S.C. 544, 563, 813 S.E.2d 292, 302 (Ct. App.

2018) (refusing to compel arbitration in part because nursing home resident did not sue for breach of contract and did not attempt to enforce contracts relating to her admission).

To show the exception was improperly applied here, Appellants must go an additional step and show why harboring a known sexual abuser against his doctor's recommendation is less outrageous than a lender defaming a borrower during debt collection (Chassereau), a finance company stealing its customer's identity (Aiken), or a car dealer pulling a "bait and switch" to trick a buyer into purchasing a less desirable vehicle (Partain). The only argument Appellants offer on this point is that cases applying the exception limit it to intentional misconduct. Appellants' Br. at 9. This argument is inaccurate. Aiken, 373 S.C. at 147, 644 S.E.2d at 707 (refusing arbitration of claims including negligence and negligent hiring and supervision); Hatcher, 379 S.C. at 552, 666 S.E.2d at 296 (applying exception to negligence claim against investment advisor).[2] Plus, the Complaint does allege intentional misconduct. Ms. Callaghan alleges Appellants knew the Perpetrator was dangerous and that they could not care for him but consciously chose to retain him in violation of a doctor's recommendation and state law. (Compl. ¶¶ 31, 46). The Complaint also states a fraud/misconduct cause of action, alleging Appellants "purposefully disseminated" false statements regarding the Facility's regulatory compliance and safety. (Compl. ¶¶ 70-72); see also Compl. ¶ 83 (c) (alleging fraudulent concealment to support UTPA claim).

Appellants then argue the circuit court erred in citing a line of persuasive authority finding torts related to sexual assault are not covered by broadly worded arbitration provisions. Appellants' Br. at 10-11 and nn. 9-10. The most factually analogous ruling cited in the circuit

[2] Appellants also cite Wilson v. Willis, 416 S.C. 395, 419, 786 S.E.2d 571, 584 (Ct. App. 2016). The Supreme Court overturned that ruling and held the claims in question were not subject to arbitration. Wilson v. Willis, 426 S.C. 326, 827 S.E.2d 167 (2019).

court's order held that a hospital could not compel arbitration of claims related to a sexual assault suffered by its patient. Victoria v. Superior Court, 710 P.2d 833 (Cal. 1985). While the arbitration provision in Victoria is slightly different than the Arbitration Agreement, Victoria is key precedent showing sexual assault in a hospital has "noting to do with providing . . . services" to hospital patients. Id. at 839. When the patient was admitted to the hospital for brain surgery and signed a contract with an arbitration provision, neither of the parties could have contemplated the relationship memorialized in that contract could ever include sexual assault. Reaching back to basic contract rules, the California Supreme Court held it was "difficult to conclude that the parties *intended and agreed*" to arbitrate claims arising from a sexual assault. Id. (emphasis added).

Noting many of the other cases cited by the circuit court considered arbitration provisions in employment contracts, Appellants insist this case is different because the Perpetrator was not Appellants' employee and to apply the employment cases here would conflate the Perpetrator's misdeeds with the more indirect misconduct alleged against Appellants. Appellants' Br. at 10-11 and n. 10. But, the sexual assault cases cited by the circuit court alleged misconduct against the employers similar to what Ms. Callaghan alleges against Appellants. In Arnold v. Burger King, an Ohio appellate court refused to compel arbitration for an employee's claims based not only on the sexual assault committed by her coworker but also on her employer's indifference despite actual or constructive knowledge that the coworker had a history of sexual assault. 48 N.E.3d 69, 84 (Ohio App. 2015). Similarly, in Smith ex rel. Smith v. Captain D's, LLC, the Mississippi Supreme Court held broadly worded arbitration provisions did not apply to claims by a restaurant employee arising from both the sexual assault committed by her supervisor and the employer's

negligence in hiring, supervising, and retaining the supervisor. 963 So.2d 1116, 1117 (Miss. 2007).

The fact that the Perpetrator was not Appellants' employee is also a distinction without a difference here. Appellants make this argument presumably to claim Appellants had no control over the Perpetrator and should not be faulted for his independent misconduct. However, the Complaint alleges Appellants had absolute power to prevent the attack on Ms. Callaghan by transferring the Perpetrator out of the Facility after his previous sexual assaults were made known to them. The law required Appellants to do so and both the Perpetrator's doctor as well as the Facility's residential services director recommended a transfer. (Compl. ¶¶ 31, 46). Appellants' profit-motivated choice to retain the Perpetrator without changing his treatment plan (Compl. ¶¶ 43, 51, 55) is not substantively different than the allegation in Arnold that an employer knew its employee was dangerous to female coworkers but chose to continue his employment.

In short, the circuit court properly applied the outrageous tort exception to Ms. Callaghan's claims because Appellants' alleged misconduct is as severe and unrelated to the parties' contractual relationship as in previous cases where the exception applied. In line with binding precedent and persuasive authority, the circuit court correctly held that the parties did not contemplate their relationship could possibly include the type of misconduct Ms. Callaghan alleges.

c. The Outrageous Tort Exception and Other Small Limitations on Seemingly Boundless Arbitration Provisions Further the Goal of Upholding the Parties' Intent.

Appellants' final argument against the outrageous tort exception is that, as applied here, it contravenes the Arbitration Agreement's unbounded arbitration provision which is meant to

apply to every conceivable claim that could ever arise between them and Ms. Callaghan. Appellants' Br. at 11-13. More broadly, Appellants insist the exception's core component—determining whether a potential claim was foreseeable to the parties at contract formation—is something South Carolina contract law does not permit and South Carolina courts would never consider in non-arbitration contexts. Appellants Br. at 8 n. 8. These arguments must fail for two reasons. First, South Carolina courts have repeatedly held that an arbitration provision cannot be *fully* limitless. Second, while they do not call their analysis the "outrageous tort exception," a number of courts look past facially unbounded arbitration language to consider the scope of foreseeable future disputes because failing to do so would not effectuate the parties' intent.

There is no disputing the Arbitration Agreement's scope provision reads broadly. In this form contract of adhesion, Appellants crafted a provision presuming to force arbitration for "any claims, controversies, or disputes arising between" the contract's parties.[3] Appellants contend "any" means all conceivable claims and is unbounded in either content or time. They insist this language is conclusive evidence Ms. Callaghan intended to arbitrate all legal claims against Appellants even if they bear no connection to the services Appellants provided her as the Facility's resident. For example, if Ms. Callaghan's condition improved such that she was able to move out of the Facility, Appellants would argue the Arbitration Agreement would apply to any random future claims that may arise. If, in ten years, Ms. Callaghan (now residing at home with her husband) was rear-ended by a transport vehicle driven by the Facility's employee, Appellants would argue the Arbitration Agreement would cover her negligence claim. See Hearn v.

[3] As discussed in Argument 2, the Arbitration Agreement's parties are defined to include only Ms. Callaghan, her husband John, Sweetgrass Court, and Five Star. Appellants Sweetgrass Village, Lisa McLeod, and Derrick Defino are not parties.

Comcast Cable Comm'cns, LLC, ___ F. Supp. 3d ___, 2019 WL 5305460, at * 5 (N.D. Ga. Oct. 21, 2019) (posing the unrelated car crash hypothetical).

It is precisely this type of interpretation that has led our Supreme Court to repeatedly hold such arbitration provisions must be subject to some form of intent-based limitation regardless of their limitless terms. Aiken, 373 S.C. at 151, 644 S.E.2d at 709 ("even the most broadly-worded arbitration agreements still have limits founded in general principles of contract law"); Landers, 402 S.C. at 115, 739 S.E.2d at 217; Partain, 386 S.C. at 492, 689 S.E.2d at 604; see also Parsons, 418 S.C. at 17, 791 S.E.2d at 136 (Toal, A.J., dissenting). As the unanimous court held in Partain, the fact that a claim is "encompassed by language of the arbitration clause" does not uniformly exempt the claim from further scrutiny as to the parties' intent. 386 S.C. at 493-94, 689 S.E.2d at 604-05. To mechanically compel arbitration for truly outrageous claims not contemplated by the parties when the contract was formed would violate courts' obligation to prioritize contractual intent above all other considerations. Id.

The outrageous tort exception is South Carolina's effort to carry out this obligation in the limited circumstances where there is a clash between a contract's language and the relationship its parties intended to form. Our courts may be unique in describing this effort as an arbitration "exception" but they are not alone in either recognizing these circumstances or in considering foreseeability[4] to impose limits on seemingly limitless arbitration provisions. Even after the U.S.

[4] See e.g., Bachus & Stratton, Inc. v. Mann, 639 So.2d 35, 36 (Fla. App. 1994) (quoting Fleck v. E.F. Hutton Group, Inc., 891 F.2d 1047, 1053 (2d Cir. 1989) (determining whether arbitration provision in employment contract applied by considering whether claims related to "foreseeable post-employment communications"); see also T-Mobile USA, Inc. v. Montijo, Case No. C12-1317RSM, 2012 WL 6194204, at * 5 (W.D. Wash. Dec. 11, 2012) (citing Fujian Pac. Elec. Co. v. Bechtel Power. Corp., No. 04-3126, 2004 WL 2645974, at * 8 (N.D. Cal. Nov. 19, 2004) ("To compel arbitration, it must be foreseeable that [party] is subject to arbitration with [opponents] on this matter")); Complete Personnel Logistics, Inc. v. Patton, No. 86857, 2006 WL 2243075 (Ohio App. June 29, 2006) (affirming trial court order denying arbitration because "arbitration

Supreme Court reiterated the FAA's equal-treatment rule, numerous federal district courts have "declined to compel arbitration of claims unrelated to the parties' contractual relationship, even though the arbitration provisions at issue lacked language tethering them to the underlying agreements." Hearn, 2019 WL 5305460, at * 5 (citing In re Jiffy Lube Int'l, Inc. v. Text Spam Litig., 847 F. Supp. 2d 1253 (S.D. Cal. 2012); Wexler v. AT&T Corp., 211 F. Supp. 3d 500 (E.D.N.Y. 2016); Revitch v. DirecTV, LLC, No. 18-CV-01127-JCS, 2018 WL 4030550 (N.D. Cal. Aug. 23, 2018); Cordoba v. DirecTV, LLC, 347 F. Supp. 3d 1311 (N.D. Ga. 2018)).

These cases declined arbitration using many of the generally applicable contract law doctrines cited above. In Hearn, the focus was on contract formation. 2019 WL 5305460 at * 7 (citing Wexler). The plaintiff in Hearn alleged his cable operator damaged his credit rating by conducting an unrequested full credit check when the plaintiff called to inquire about a potential new service. Id. at * 1. The provider moved to dismiss the suit based on an arbitration provision in an unrelated contract signed two years earlier which purported to apply to "any claim or controversy related to" the provider. Id. The court found the claim was not covered by the arbitration provision because, for all contracts governed by Georgia law, the parties' intent controls using an objective theory of intent. Id. at * 7.

In other words, the intent of a contract's language is determined by what a reasonable man in the position of the other contacting party would ascribe to the first party's manifestations of assent. Id. at * 7 (quoting Cox Broad. Corp v. Nat'l Collegiate Athletic Ass'n, 297 S.E.2d 733 (Ga. 1982)). No reasonable person could believe the two-year-old contract's arbitration provision applied to an unrelated future claim. Id.; see also Wexler, 211 F. Supp. 3d at 504 (noting state law required court to determine what "objective, reasonable" person interpreted contract

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clause does not contemplate that the claims raised by [plaintiffs] are reasonably foreseeable as to be arbitrated under the agreement").

language to mean and declining to enforce arbitration to unrelated claim "[n]otwithstanding the literal meaning of the [arbitration] clause's language"). South Carolina contract law takes a similar objective approach for determining contractual intent. Laser Supply & Servs., Inc. v. Orchard Park Assocs., 382 S.C. 326, 334, 676 S.E.2d 139, 143-44 (Ct. App. 2009) (holding that contract interpretations are "governed by the objective manifestations of the parties' assent . . . rather than the subjective, after-the-fact meaning one parties assigns to it"). Our courts also use the objective reasonable person standard to determine the scope of an arbitration provision. Aiken, 373 S.C. at 151 n. 6, 644 S.E.2d at 709 (holding that outrageous tort exception considers the reasonable man standard applied in tort law).

In Revitch, the focus was on the rule against interpreting contracts in a way that leads to absurd results. 2018 WL 4030550, at *2-3.[5] South Carolina applies a similar rule, and Parsons cited it as part of the basis for the outrageous tort exception. 418 S.C. at 134-35, 791 S.E.2d at 14. The Georgia district court's order in Cordoba goes a step further to undercut Appellants' equal-treatment principle argument. 347 F. Supp. 3d at 1320-21. Rather than read DirecTV's arbitration provision to apply to a wholly unrelated claim, Cordoba held that a claim must bear some substantial relationship to the underlying transaction because to read an arbitration provision as unbounded would itself violate the FAA. Specifically, the FAA applies only to claims "arising out of" the underlying contract or transaction. Id. (quoting 9 U.S.C. § 2). Thus, the circuit court's rejection of an unbounded reading of the Arbitration Agreement's scope is consistent with South Carolina contract law and compelled by the FAA.

[5] Revitch also rejected an equal-treatment principle argument, finding that the rule against absurd results is general applicable and, therefore, provides equal treatment to arbitration contracts. 2018 WL 4030550, at * 16 (citing Kindred Nursing).

Finally, the In re Jiffy Lube decision held that to read an "any and all claims" arbitration provision to lack a scope restriction "would clearly be unconscionable." 847 F. Supp. 2d at 1262-63. Aiken at least hinted that reading a South Carolina arbitration contract to cover unforeseeable, outrageous torts could be unconscionable. 373 S.C. at 151 n. 4, 644 S.E.2d at 709 n. 4. Under South Carolina law, unconscionability is defined as "the absence of meaningful choice on the part of one party, due to one-sided contract provisions, together with terms that are so oppressive that no reasonable person would make them and no fair and honest person would accept them." Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 25, 344 S.E.2d 663, 668 (2007). If a contract provision is unconscionable, it may be invalidated or its application limited so as to prevent an unconscionable result. Id. Here, Appellants ask the Court to hold the Arbitration Agreement's scope extends to their intentional choice to harbor a known sexual abuser because doing so would benefit Appellants financially. Even accepting the strained premise that the arbitration provision can be read to include Ms. Callaghan's claim, it is hard to imagine how any fair and honest person in Appellants' position would propose an arbitration demand that extends so far beyond the parties' contemplated relationship. On top of all this, no reasonable and fair nursing home operator would present an arbitration contract that both covered a claim for the operator's intentional retention of a known sexual predator and then categorically barred an assaulted nursing home resident from even asking for punitive damages (Arbitration Agreement ¶ 2) for the egregious misconduct.

Therefore, the Court should reject Appellants' argument that the Arbitration Agreement's plain language is wholly boundless and compels arbitration even if Ms. Callaghan alleges outrageous, unforeseeable torts. South Carolina contract law requires some limitation on the Arbitration Agreement's scope and the outrageous tort exception is similar to how a number of

other courts apply generally applicable contract principles to prevent arbitration on similar claims.

2. The Arbitration Agreement is Limited to Claims Between its Narrowly-Defined Parties.

Appellants Sweetgrass Village, Lisa McLeod, and Derrick Defino are not parties to the Arbitration Agreement. South Carolina law presumes a contract's duties and benefits are exclusive to its parties, and the circuit court correctly determined these Appellants' claims do not meet the limited circumstances when a non-party can enforce contract provisions. To make these Appellants third-party beneficiaries with enforcement rights, the Arbitration Agreement would have to unambiguously extend its benefits to them and unambiguously subject to arbitration Ms. Callaghan's claims against them. Since the Arbitration Agreement's language does not meet these requirements, the circuit court's ruling should be affirmed.

By its very nature, a contract is a voluntary agreement between (usually) two specifically identified parties. What separates contractual duties from their statutory or tort-based counterparts is that they are imposed only on parties that affirmatively manifest assent to them. Accordingly, South Carolina law presumes contracts may only be enforced by their parties. Touchberry v. City of Florence, 295 S.C. 47, 48-49, 367 S.E.2d 149, 150 (1988). This presumption may be overcome only if the contract's language unambiguously extends its benefits to third parties. Thompson v. Pruitt Corp., 416 S.C. 43, 57, 784 S.E.2d 679, 687 (Ct. App. 2016). Here, the Arbitration Agreement includes what appears in isolation as a third-party beneficiary provision. Arbitration Agreement ¶ 8. But, when read in full, the Arbitration Agreement does not extend to third parties because it limits the scope of arbitrable claims to its narrowly defined "Parties" and because it does not extend any of arbitration's supposed finality benefits to non-parties like Sweetgrass Village, Lisa McLeod, and Derrick Defino. As this Court

recently held, a contract provision on third-party beneficiaries must not be read in isolation and may not hold up when inconsistent with other substantive provisions.[6]

Appellants argue the circuit court overlooked the rule requiring courts interpret contracts as a whole. Appellants Br. at 15. However, Appellants do not actually ask the Court to interpret the contract as a whole. Instead, they cite one arguably favorable contract provision and ignore all others. Admittedly, Paragraph 8 in isolation could be read to extend the contract's effects to related entities, but the rest of the contract undermines that reading. The sentence preceding the signature blocks is the language the contract's drafters (Appellants Five Star and Sweetgrass Court) highlight most as it is the only substantive provision in bold type, underlined, and printed in all capital letters. Arbitration Agreement at 3. This key sentence references enforcement only "**BY THE PARTIES**," not any related entities. Id. This assertion prompts a diligent reader to search back for the meaning of "Parties," a term the Arbitration Agreement specifically and narrowly defines. In the Arbitration Agreement's opening paragraph, "Parties" is defined to include only Ms. Callaghan, her husband John, Sweetgrass Court, and Five Star. Arbitration Agreement at 1. From that first sentence forward, the reader is compelled to interpret "Parties" to correspond with only those four individuals and entities. Then, in its first substantive provision, the Arbitration Agreement further clarifies arbitration rights extend only to "a dispute aris[ing] between the Parties." Arbitration Agreement at ¶ 1.

Given the narrow definition of "Parties" Five Star and Sweetgrass Court chose, allowing Sweetgrass Village, Lisa McLeod, and Derrick Defino to force Ms. Callaghan to arbitrate her claims could lead to a grossly unfair outcome. The Arbitration Agreement later states that any

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[6] Beverly v. Grand Strand Reg'l Med. Ctr., LLC, Op. No. 5708 (S.C. Ct. App. filed Jan. 15, 2020) (Shearouse Adv. Sh. No. 3 at 12-13) (refusing to enforce contract's third-party beneficiary exclusion that proved inconsistent with the remaining twenty pages of the contract).

arbitration ruling is "binding upon the Parties," meaning that it may not be appealed and may form the basis for a judgment entered by a court. Arbitration Agreement ¶ 2. The negative implication from this plain language, therefore, is that an arbitration ruling is not binding on non-Parties like Sweetgrass Village, McLeod, and Defino. In other words, these Appellants seek an interpretation of the Arbitration Agreement that allows them to force Ms. Callaghan into arbitration while reserving for themselves the right to appeal any unfavorable ruling and to argue a court has no power to formalize such ruling in a legally-enforceable judgment against them. Limiting arbitration to the "Parties" is the only way to avoid this overtly inequitable outcome. Sweetgrass Village, McLeod, and Defino may argue the Court could simply choose to find an arbitration ruling would be binding on them. But, the Court would have to rewrite the contract to reach that result, and doing so would violate another long-standing contract interpretation rule. Poynter Invs., Inc. v. Century Builders of Piedmont, Inc., 387 S.C. 583, 588, 694 S.E.2d 15, 18 (2010) (quoting MailSource, LLC v. M.A. Bailey & Assoc., 356 S.C. 363, 369, 588 S.E.2d 635, 639 (Ct. App. 2003) (rejecting party's interpretation that would require disputed contract to be rewritten because that is "a service the courts of South Carolina do not perform").[7] Thus, reading the Arbitration Agreement as a whole supports the circuit court's ruling.

Since there is no way to reconcile Arbitration Agreement ¶ 8's reference to "related parties" and the multiple other provisions limiting arbitration to the narrowly defined "Parties," the best argument Sweetgrass Village, Lisa McLeod, and Derrick Defino can make is that the Arbitration Agreement is ambiguous. Jordan v. Sec. Grp., Inc., 311 S.C. 227, 230, 428 S.E.2d

[7] As further evidence the parties did not intend for arbitration to apply to non-parties like Sweetgrass Village, McLeod, and Defino, the contract provides no guidance on who would pay for arbitration proceedings involving them. This omission stands in sharp contrast to disputes between "Resident" (Mr. and Mrs. Callaghan) and "Five Star" (Five Star and Sweetgrass Court) for which the contract includes specific provisions on costs and on how payment of costs affects the process for selecting arbitrators.

705, 707 (1993) (defining contract ambiguity as language that "may fairly and reasonably be understood in more ways than one"). Since Appellants Five Star and Sweetgrass Court were the Arbitration Agreement's sole drafters, this ambiguity should be resolved in Ms. Callaghan's favor. Frewil, LLC v. Price, 411 S.C. 525, 530, 769 S.E.2d 250, 253 (Ct. App. 2015).[8]

In sum, in addition to correctly concluding the Arbitration Agreement's parties did not intend for its provisions to cover Ms. Callaghan's outrageous tort claims, the circuit court was correct in its alternative ruling that the Arbitration Agreement cannot be applied to Sweetgrass Village, Lisa McLeod, and Derrick Defino because they are not parties to it or otherwise empowered to enforce its provisions.

CONCLUSION

Based on the arguments stated above, Ms. Callaghan respectfully requests the Court affirm the circuit court's order denying Appellants' motion to compel arbitration. Ms. Callaghan's allegations that Appellants willfully harbored a sexual predator against his doctor's advice and in violation of state law is far removed from the relationship the parties intended to formed and, therefore, there is no valid arbitration contract. This ruling does not contravene the FAA's equal treatment principle because it applies South Carolina's generally applicable contract formation and interpretation rules. In the alternative, the Court should affirm the circuit

[8] Appellants argue the rule on resolving ambiguities does not apply here because of the state and federal pro-arbitration policy. Appellants' Br. at 14. This argument is misguided for a couple reasons. The FAA's pro-arbitration policy is intended to place arbitration contracts on equal footing with other contracts, not place them *above* the rules applied to contracts in other contexts. See Prima Paint Corp. v. Flood Conklin Mfg. Co., 388 U.S. 395, 404 n. 12 (1967) (finding intent of FAA was "to make arbitration agreements as enforceable as other contracts, but not more so"). Accordingly, "general contract principles of state law apply to arbitration clauses governed by the FAA." Munoz v. Green Tree Fin. Corp., 343 S.C. 538, 539, 542 S.E.2d 360, 364 (2001). Plus, the South Carolina Supreme Court has applied the rule on resolving ambiguities to reject a nursing home operator's interpretation of an arbitration contract. Coleman v. Mariner Health Care, Inc., 407 S.C. 346, 355, 755 S.E.2d 450, 455 (2014).

court's ruling Appellants Sweetgrass Village, Lisa McLeod, and Derrick Defino may not enforce the Arbitration Agreement because they are not its parties or third-party beneficiaries.

Respectfully submitted,

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Columbia, SC
February 4, 2020

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

William H Seals, Jr., Circuit Court Judge

Appellate Case No. 2019-001419

Nancy Callaghan ..... Respondent

v.

Five Star Quality Care, Inc., Five Star Quality Care-OBX Operator, LLC d/b/a Sweetgrass Court Senior Living Community, Sweetgrass Village Assisted Community, Lisa McLeod and Derrick Defino ..... Appellants.

PROOF OF SERVICE

I certify that I have served Respondent's Initial Brief, by depositing a copy of it in the United States Mail, postage prepaid, on February 4th, 2020, addressed to attorneys for Appellants, G. Mark Phillips and Robert W. Whelan, of Nelson Mullins Riley & Scarborough, LLP, Post Office Box 1806, Charleston, SC, 29402-1806.

< SIGNATURE LINE TO FOLLOW >

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February 4th, 2020

Via Hand Delivery
The Honorable Jenny A. Kitchings
South Carolina Court of Appeals
1220 Senate Street
Columbia, SC 29201

Re: Nancy Callaghan v. Five Star Quality Care, Inc., Five Star Quality Care-OBX Operator, LLC d/b/a Sweetgrass Court Senior Living Community, Sweetgrass Village Assisted Community, Lisa McLeod and Derrick Defino
Appellate Case No.: 2019-001419

Dear Ms. Kitchings:

Enclosed please find the original and one (1) copy of Respondent's Initial Brief; Proof of Service of Respondent's Initial Brief; Respondent's Designation of Matter to be Included in the Record on Appeal; and Proof of Service of Respondent's Designation of Matter to be Included in the Record on Appeal.

Please file in your customary manner and return a stamped copy to us via our courier. By copy of this letter and enclosures, we are serving all counsel of record.

With best regards, I am

Sincerely,

John G. Felder, Jr.

JGF/klw
Enclosures

cc: Robert W. Whelan, Nelson Mullins Riley & Scarborough, LLP (Via U.S. Mail)
cc: G. Mark Phillips, Nelson Mullins Riley & Scarborough, LLP (Via U.S. Mail)