

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM ANDERSON COUNTY
Court of Common Pleas

The Honorable R. Scott Sprouse, Circuit Court Judge

RECEIVED

JAN 07 2019

SC Court of Appeals

Appellate Case No. 2018-000468
Civil Action No. 2017-CP-04-09132

Hicks Unlimited, Inc., Respondent,

v.

UniFirst Corporation, a Massachusetts Corporation Appellant.

FINAL BRIEF OF APPELLANT

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STATEMENT OF ISSUES ON APPEAL

- I. Did the trial court err by denying the motion for summary judgment on the basis that the notice provision in the South Carolina Uniform Arbitration Act was not preempted by the Federal Arbitration Act?

- II. Did the trial court err by finding the respondent had sufficiently alleged unconscionability as a defense to the enforceability of the agreement to arbitrate?

STATEMENT OF THE CASE

On or about September 21, 2006, UniFirst Corporation and Hicks Unlimited entered into a Flame Resistant Garment Agreement, pursuant to which Hicks Unlimited paid UniFirst a weekly service fee for renting from UniFirst flame retardant garments for its business. (R. pp. 12-13). The initial term of the Agreement was 5 years. *Id.* Under the terms of the Agreement, the contract automatically renewed for additional 5-year terms unless Hicks Unlimited notified UniFirst in writing at least 90 days before the expiration of the then-current term that it did not intend to renew the contract. *Id.*

UniFirst is a corporation organized by the laws of the State of Massachusetts, with its principal place of business in Wilmington, Massachusetts. (R. p. 8, ¶ 2; p. 33). It serviced Hicks Unlimited through its facility in Simpsonville, South Carolina. (R. p. 58, line 1; p. 33).

As indicated by the language of the contract the Flame Resistant Garment Agreement is a standard form contract, used by UniFirst and its subsidiaries in numerous locations, including Canada (through UniFirst Canada) and Texas (through UniFirst Holdings, LP). (R., p. 13).

Consistent with the terms of the Agreement, UniFirst measured and sized the Hicks Unlimited employees, and then ordered flame retardant garments from its facility in Kentucky, and then shipped those garments from Kentucky to South Carolina. (R. p. 33).

In accordance with the provisions of the contract, UniFirst provided merchandise rental services to Hicks Unlimited from 2006 through 2011. (R. p. 9, ¶ 5). The contract automatically renewed in 2011; UniFirst continued to provide, and Hicks Unlimited continued to pay for merchandise rental services for an additional 5-year period from 2011 through 2016. *Id.*

Hicks Unlimited contends it terminated the Customer Service Agreement before September 21, 2016, which is when it claims the next 5-year term would have taken effect. (R. p. 9, ¶ 6). In response, on May 17, 2017, UniFirst Corporation commenced an arbitration

proceeding through the American Arbitration Association, arising out of Hicks Unlimited, Inc.'s breach of the Customer Service Agreement executed by the parties. That arbitration remains pending. (R. p. 9, ¶ 8).

On or about September 14, 2017, Hicks Unlimited commenced an action in the Court of Common Pleas in Anderson County, South Carolina, attempting to claim the dispute as framed by UniFirst's demand was not subject to arbitration. (R. p. 8).

More specifically, as alleged in the Complaint, Hicks Unlimited acknowledged it received and paid for service from UniFirst for 10 years, but claimed it properly terminated the contract. (R. p. 9, ¶¶ 5-6). Nevertheless, Hicks Unlimited argued the contract was "illegal, unconscionable, and unenforceable," and claimed UniFirst had failed to comply with the mandatory notice provision in S.C. Code Ann. § 15-48-10(a). (R. p. 9, ¶¶ 7; 10). Hicks Unlimited further argued it had never signed an agreement to arbitrate. (R. p. 10, ¶ 12).

On October 13, 2017, UniFirst Corporation answered the plaintiff's petition, asserted affirmative defenses, and filed its Motion to Compel Arbitration. (R. p. 16; R. p. 23). In response, Hicks Unlimited filed a Motion for Summary Judgment. On November 27, 2017, the trial court heard argument of counsel regarding UniFirst's Motion to Compel Arbitration, and on Hicks Unlimited's Motion for Summary Judgment. (R. p. 47) On December 1, 2017, the trial court advised the parties that both motions were denied. On January 9, 2018, the trial court entered its Order denying the relief requested. (R. p. 1).

On January 18, 2018, UniFirst Corporation filed a 59(e) motion to alter or amend the trial court's January 9, 2018 Order. (R. p. 31). On February 14, 2018, the trial court denied UniFirst Corporation's motion to alter or amend the January 9, 2018 Order. (R. p. 5). On March 15, 2018, UniFirst Corporation appealed to this Court the lower court's rulings.

STANDARD OF REVIEW

South Carolina law recognizes that a party may appeal an order denying an application to compel arbitration. *See* S.C. Code Ann. § 15-48-200(a)(1). This is consistent with the principle that when a trial court enters an order favoring litigation over arbitration, that order is immediately appealable. *See Towles v. United HealthCare Corp.*, 338 S.C. 29, 35; 524 S.E.2d 839, 842-43 (Ct. App. 1999). This Court is to review *de novo* the lower court's determination of arbitrability. *Gissel v. Hart*, 382 S.C. 235, 240; 676 S.E.2d 320, 323 (2009).

ARGUMENTS

I. The Parties Agreed by Contract the FAA Would Apply to Their Dispute

This Court has routinely held there is a strong presumption in favor of the validity of arbitration agreements because of the strong policy favoring arbitration. *Towles*, 338 S.C. at 36, 524 S.E.2d at 844. Consequently, it was Hicks Unlimited – the party resisting arbitration – that bore the original burden of proving the claims at issue were unsuitable for arbitration. *Green Tree Fin. Corp. – Ala. v. Randolph*, 531 U.S. 79, 91 (2000). The Supreme Court of South Carolina has stated that any doubts concerning the scope of arbitrability should be resolved in favor of arbitration. *Carolina Care Plan, Inc. v. United HealthCare Svcs., Inc.*, 361 S.C. 544, 550, 606 S.E.2d 752, 755 (2004). And unless the court can say with positive assurance that the arbitration clause is not susceptible to an interpretation that covers the dispute, the court should order arbitration of the dispute. *Id.*

While Hicks Unlimited may argue the question at bar is determining the applicability of the Federal Arbitration Act (FAA) to its dispute with UniFirst regarding its claim of breach of contract, UniFirst submits the parties have already decided by contract the FAA would apply to the dispute.

Specifically, the parties agreed:

All disputes of whatever kind between the Customer and UniFirst based upon past, present or future acts, whether known or unknown, and arising out of or relating to the negotiation, formation or performance of this Agreement shall be resolved exclusively by final and binding arbitration. The arbitration shall be conducted...pursuant to the Expedited Procedures of the Commercial Arbitration Rules of the American Arbitration Association **and shall be governed by the Federal Arbitration Act**... [emphasis added]

(R. p. 27).

Within the scope of the Flame Resistant Garment Agreement, the above passage constitutes an agreement to arbitrate by the parties. (R. p. 27). It is well-settled that arbitration agreements, like other contracts, are enforceable in accordance with their terms. *Munoz v. Green Tree Financial Corp.*, 343 S.C. 531, 539, 542 S.E.2d 360, 363-64 (2001). The terms of the contract at issue expressly require arbitration, and expressly state the arbitration procedure shall be governed by the FAA. *See Id.* In *Munoz*, the court's first inquiry was to the contract terms themselves, and in reviewing them, noted the parties had, just as in the case at bar, expressly agreed the FAA would apply. *Id.*

Here, the record shows the parties signed the Flame Resistant Garment Agreement; UniFirst provided services to Hicks Unlimited in accordance with the terms of the Agreement; Hicks Unlimited paid for the services UniFirst provided; and the parties continued this contractual relationship for at least 10 years, or at least 5 years longer than the initial term of this Agreement. (R. p. 9, ¶¶ 5-6; R. p. 56, lines 4-9; R. p. 56, line 17-p. 57, line 2).

Stated differently, the parties enjoyed the benefits and accepted the responsibilities of the contract. Further, the parties, by signing a contract that included an agreement to arbitrate, made the decision to resolve their disputes through arbitration, not litigation, and, more importantly, stipulated to the law that would govern their dispute. By agreeing to the FAA applying to the action, the parties also stipulated that their contractual relationship implicated interstate

commerce. Because the parties agreed by contract to the provisions of the FAA, UniFirst submits this should, as it was in *Munoz*, be the end of the Court's inquiry as to the FAA.

Because the FAA applies, the *Munoz* decision requires the Court reject Hicks Unlimited's defense that the contract failed to comply with the notice requirements contained in the South Carolina Arbitration Code. Section 2 of the FAA provides in relevant part that

A written provision in any...contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract...shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 2.

In *Munoz*, the party challenging the arbitrability of disputes raised the same defense as Hicks Unlimited did in the instant case. 343 S.C. at 539, 542 S.E.2d at 364. The court in *Munoz* noted that state laws will remain applicable if that law arose to govern issues concerning the validity, revocability, and enforceability of all contracts, not just arbitration agreements. *Id.* But if the state law placed arbitration clauses on unequal footing with general provisions in other contracts, the FAA would preempt the state law. *Id.*

The provision Hicks Unlimited asked the trial court to apply, and would ask this Court to apply, is Section 15-48-10(a) of the South Carolina Uniform Arbitration Act. While the beginning of section (a) contains the same language as section 2 of the FAA (*compare* S.C. Code Ann. § 15-48-10 *with* 9 U.S.C. § 2), Hicks Unlimited claims the following provision invalidates the parties' agreement to arbitrate in this case:

Notice that a contract is subject to arbitration pursuant to this chapter shall be typed in underlined capital letters, or rubber-stamped prominently, on the first page of the contract and unless such notice is displayed thereon the contract shall not be subject to arbitration.

S.C. Code Ann. § 15-48-10(a).

As drafted, Section 15-48-10 distinguishes arbitration clauses from other contract provisions, and, in effect, places them on different footing than general contract provisions. As a result, the court in *Munoz* held the FAA preempted the South Carolina Uniform Arbitration Act, and refused to invalidate the arbitration clause at issue in the case, even though it did not comply with Section 15-48-10. *Munoz*, 343 S.C. at 540, 542 S.E.2d at 364.

In this case, there is similarly no dispute the arbitration clause in the Flame Resistant Garment Agreement does not comply with the notice provision in the South Carolina Uniform Arbitration Act. But since the parties agreed in their covenant to arbitrate that the provisions of the FAA would control, they, in effect, agreed the FAA would preempt compliance with South Carolina state law. Because the FAA preempts in this case, Hicks Unlimited's defense of improper notice must fail.

At a bare minimum, Hicks Unlimited failed to meet its burden to show the trial court should not have applied the arbitration clause in the contract to require the parties to arbitrate its dispute. Thus, to the extent the trial court relied on the South Carolina Uniform Arbitration Act to deny arbitration of this dispute, the trial court erred. Accordingly, UniFirst Corporation requests the Court reverse the trial court's decision, and require the parties to complete the pending arbitration proceeding.

II. The Transaction at Issue Involved Interstate Commerce.

Though, as argued above, the parties' agreement to the provisions of the FAA conclusively establishes that the FAA applies to the parties' dispute, the trial court should have also applied the FAA to require the parties to arbitrate the issue of the continued enforceability of a contract that the parties both acknowledged had been in force for more than ten (10) years. If the parties did not specify in the contract the FAA would apply, the statute would nevertheless

apply to the dispute of the agreement evidenced a transaction involving interstate commerce. *Towles*, 338 S.C. at 35, 524 S.E.2d at 843.

The phrase “involving commerce” equates to “affecting commerce,” and reflects the intent to enforce Congress’s commerce clause power to the full. *Id.* at 36; 524 S.E.2d at 843. As a result, the FAA includes more transactions than those defined as actually “in commerce;” rather, it includes those “within the flow of interstate commerce.” *Thornton v. Trident Med. Ctr., L.L.C.*, 357 S.C. 91, 95, 592 S.E.2d 50, 52 (Ct. App. 2003). Thus, courts, when considering whether a transaction involves commerce, should broadly construe the standard so as to be coextensive with congressional power to regulate under the Commerce Clause. *Towles*, 338 S.C. at 35, 524 S.E.2d at 843 (citing *Mathews v. Fluor Corp.*, 312 S.C. 404, 407; 440 S.E.2d 880, 881 (1994)).

Commerce clause grants Congress the power to regulate 1) the use of channels of interstate commerce; 2) instrumentalities of interstate commerce, or persons or things in interstate commerce; and 3) activities having a substantial relation to interstate commerce. *U.S. v. Morrison*, 529 U.S. 598, 609 (2000). Commerce clause power may be exercised in individual cases without showing any specific effect upon interstate commerce if in the aggregate; the economic activity in question would represent a general practice subject to federal control. *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 56-58 (2003). Ultimately, the commerce requirement is satisfied where the transaction in fact involved interstate commerce, even if the parties did not contemplate an interstate commerce connection. *Munoz*, 343 S.C. at 538, 542 S.E.2d at 363.

Blanton v. Stathos is a prime example of how far this Court has gone to find there was interstate commerce in a business relationship. 351 S.C. 534, 570 S.E.2d 565 (Ct. App. 2002).

In *Blanton*, the parties entered into a contract whereby an architect agreed to provide design, drawing, and architectural services for a restaurant in Seneca, South Carolina. *Blanton*, 351 S.C. at 537, 570 S.E.2d at 567. The architect did her work in South Carolina; before construction began, and even before procurement of the materials had occurred, the parties' business relationship terminated. 351 S.C. at 538, 570 S.E.2d at 567.

In challenging arbitrability, the party who contracted for the architectural services asserted that since construction had not yet begun, and since all work was done, and had been done, by individuals residing in South Carolina, concerning a restaurant in South Carolina, the contract did not evidence interstate commerce. *See* 351 S.C. at 537-40, 570 S.E.2d at 567-69. In response, the architect averred that because she consulted with technicians outside South Carolina, her design and drawings contemplated the purchase and acquisition of materials and labor from states other than South Carolina. 351 S.C. at 541, 570 S.E.2d at 568-69. Even though none of the "purchases and acquisitions" had occurred at the time the parties' relationship ended, the Court concluded the transaction evidenced interstate commerce, and affirmed the arbitration award. 351 S.C. at 541, 570 S.E.2d at 569.

Courts in South Carolina have routinely agreed to extend interstate commerce to what appear to be intrastate disputes. *See Zabinski v. Bright Acres Associates*, 346 S.C. 580, 553 S.E.2d 110 (2001) (finding interstate commerce in a transaction involving a South Carolina partnership developing land on Hilton Head Island because the partnership utilized out-of-state materials, contractors, and investors); *Munoz*, 343 S.C. 531, 542 S.E.2d 360 (interstate commerce where both parties were domiciled in South Carolina, but one party assigned rights to a creditor in Minnesota); *Dean v. Heritage Healthcare of Ridgeway, LLC*, 408 S.C. 371, 759 S.E.2d 727 (2014) (interstate commerce applied to a nursing home residency agreement

involving a resident of South Carolina, where meals and medical supplies were shipped across state lines from out-of-state vendors); *Episcopal Hous. Corp. v. Fed. Ins. Co.*, 269 S.C. 631, 239 S.E.2d 647 (1977) (FAA applied to construction contract for project in South Carolina because materials from out-of-state would be used in project).

Here, while UniFirst provided service to Hicks Unlimited out of its facility in Simpsonville, South Carolina, it is a Massachusetts corporation, with decisions controlled by a board of directors in Massachusetts. (R. p. 8, ¶ 2; R. p. 33; R. p. 59, lines 23-24). Payments tendered by Hicks Unlimited to UniFirst in South Carolina would be forwarded to Massachusetts, and when UniFirst ordered merchandise to rent to Hicks Unlimited, it did so by purchasing garments in, and having them shipped from, Kentucky to South Carolina. (R. p. 33). On these facts, even if the parties had not expressly agreed to the FAA, the relationship implicated interstate commerce such that the FAA applied to the dispute, thereby exempting any requirement by UniFirst to comply with the notice requirements contained in the South Carolina Arbitration Act.

In sum, the trial court should have enforced the parties' express agreement to apply the provisions of the FAA to preempt requirement by UniFirst of the notice provisions of the South Carolina Arbitration Code, both because the parties agreed to the FAA in the contract, and because the transactions between the parties contemplated interstate commerce. By not doing so, the trial court erred. Therefore, the Court should reverse the finding of the trial court and enforce the parties' agreement to require them to arbitrate their dispute.

III. *Timms* No Longer States the Law in South Carolina.

In its Order denying UniFirst's summary judgment, the trial court made its findings of fact and concluded that based on the decision of *Timms v. Greene*, 310 S.C. 469, 427 S.E.2d 642

(1993), the FAA did not supersede section 15-48-10 of the South Carolina Uniform Arbitration Act. But the Supreme Court has expressly overruled *Timms*.

In *Timms*, the contract at issue stated that the “Uniform Arbitration Act” would apply to the dispute. 310 S.C. at 470-71, 427 S.E.2d at 643. The court then stated the contract for patient-residential service was “obscure, if not devoid, of any basis for holding that commerce was involved in the transaction between the parties.” *Id.* at 644, 310 S.C. at 472.

In 2014, through the *Dean* decision, the South Carolina Supreme Court overruled *Timms* in its entirety. 408 S.C. 371, 759 S.E.2d 727. In doing so, the court stated, “[W]e find *Timms* is a relic of the past, decided before the broad definition of interstate commerce....” As the *Dean* court noted, courts since then who have looked at nursing home residency contracts of the type discussed in *Timms* have noted that the nursing homes provide their residents items – such as meals and medical supplies – that are shipped across state lines from out-of-state vendors, just as the merchandise was shipped across state lines in this case. *See* 408 S.C. at 381, 759 S.E.2d at 732. Incidentally, nowhere in the contract in the *Dean* case did the parties agree to the application of the FAA to their dispute. As a result, *Timms* no longer expresses the state of the law in South Carolina on the applicability of the FAA to business disputes.

IV. Hicks Unlimited Failed to Meet its Burden on Unconscionability.

The trial court’s last basis for denying the motion for summary judgment was that Hicks Unlimited had alleged the contract was unconscionable and, thus, should be able to raise this defense in state court. In support of this position, the court cited to the case of *Smith v. D.R. Horton, Inc.*, 417 S.C. 42, 790 S.E.2d 1 (2016).

But in *Smith*, the Supreme Court of South Carolina found that in order for Hicks Unlimited to have asserted a defense of unconscionability that the trial court could have

considered, the Supreme Court of the United States had held that the nature of the defense had to apply to the arbitration agreement itself, not to the contract as a whole. 417 S.C. at 48, 790 S.E.2d at 4 (citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 406 (1967)). In other words, Hicks Unlimited was required to allege the arbitration agreement was unconscionable, not that the entire contract was unconscionable. 417 S.C. at 48, 790 S.E.2d at 4. And when conducting its review of the unconscionability defense, the Court's review is limited to evaluating the provisions of the arbitration agreement, not those of the whole contract. *Id.*

The *Prima Paint* doctrine is of a piece with the jurisprudence that has identified two types of challenges to the validity of arbitration agreements. *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 444 (2006). The first type specifically challenges the validity of the agreement to arbitrate – the specific language in the contract containing the arbitration clause. *Id.* The second type challenges the contract as a whole, on a ground that directly affects the entire agreement. *Id.* In *Buckeye Check Cashing*, the defendant challenged the enforceability of the arbitration agreement by claiming the entire contract was void because it charged illegal, usurious interest rates. *Id.* at 442. In reversing the lower court's denial of the motion to compel arbitration, the Supreme Court held that "a challenge to the validity of the contract as a whole, and not specifically to the arbitration clause, must go the arbitrator." *Id.* at 449.

In its Complaint, Hicks Unlimited's allegation concerning unconscionability was limited to the following: "Hicks is further informed and believes that the terms of the contract are illegal, unconscionable, and unenforceable." (R. p. 9 ¶ 7). Nowhere in its Complaint did Hicks Unlimited attack the purported unconscionability of the arbitration clause itself; to the contrary, as alleged, its attack was to the contract as a whole. Thus, Hicks Unlimited failed to properly assert the unconscionability defense in a manner sufficient to satisfy the *Prima Paint* doctrine,

and therefore, the trial court should have refused to consider the defense as a means to avoid the arbitrability of the parties' dispute.

As to the unconscionability defense itself, Hicks Unlimited was required to allege that it lacked a meaningful choice in entering into the arbitration agreement. *Simpson v. MSA of Myrtle Beach, Inc.*, 373 S.C. 14, 24-25, 644 S.E.2d 663, 668 (2007). In determining whether a party lacked a meaningful choice to arbitrate, the trial court should have considered the relative disparity in the parties' bargaining power, the parties' relative sophistication, whether the parties were represented by counsel, and whether the parties are business concerns. *Id.* at 26-27, 644 S.E.2d at 669-70.

In this case, Hicks Unlimited alleged no facts at all regarding the meaningful choice to arbitrate; it merely made a general statement that it believed the contract as a whole was unconscionable. (R. p. 9, ¶ 7). Even if it had made more than a general platitude as an allegation, the facts of this case show both parties are businesses, and based on Hicks Unlimited's allegations in its complaint, it knew about the obligations to which it had agreed, and yet acted in accordance with the terms of the Flame Resistant Garment Agreement for more than ten (10) years. As UniFirst alleged in its Answer, Hicks Unlimited, at the time it chose to sign with UniFirst, had the choice of several merchandise rental providers in the area, and, when Hicks Unlimited terminated UniFirst's services, it did so to choose one of those other providers to engage. (R. p. 19, ¶ 24).

Ultimately, as the Supreme Court of South Carolina stated:

c]ourts should not refuse to enforce a contract on grounds of unconscionability, even when the substance of the terms appear grossly unreasonable, unless the circumstances surrounding its formation present such an extreme inequality of bargaining power, together with factors such as lack of basic reading ability and the drafter's evident intent to obscure the term, that the party against whom enforcement is sought cannot be said to have consented to the contract.

Gladden v. Boykin, 402 S.C. 140, 145, 739 S.E.2d 882, 884-85 (2013). Moreover, the clause at issue provides for unbiased resolution of the parties' dispute by a neutral decisionmaker, which, according to *Simpson*, is the most important consideration in deciding whether unconscionability exists. *Simpson*, 373 S.C. at 25; 644 S.E.2d at 668 (2007). Hicks Unlimited fell far below what it was required to allege in order to properly bring the unconscionability defense before the trial court to consider. Because the trial court accepted Hicks Unlimited's general allegation directed at the contract as a whole, the trial court erred.

CONCLUSION

Based on the foregoing points and authorities, the appellant respectfully requests the Court reverse the trial court's orders denying the motion for summary judgment, direct the trial court to grant the motion to compel arbitration, and require the parties to complete the arbitration proceeding that was commenced and has been pending since 2017.

Respectfully submitted,

January 7, 2019

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CERTIFICATE OF COUNSEL

The undersigned certifies that the FINAL BRIEF OF APPELLANT and FINAL REPLY BRIEF OF APPELLANT comply with Rule 211(b), SCACR, as well as the South Carolina Supreme Court's Order dated April 15, 2014.

January 7, 2019

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