IN THE SUPREME COURT OF MISSOURI

NO. SC86855

NETCO, INC., ET AL.,
Respondents,

v.

JIMMY V. DUNN, ET AL.,
Appellants.

ON APPEAL FROM THE CIRCUIT COURT OF GREENE COUNTY, MISSOURI

HONORABLE J. MILES SWEENEY
CIRCUIT COURT JUDGE

APPELLANTS' SUBSTITUTE OPENING BRIEF

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JURISDICTIONAL STATEMENT

All Appellants moved to compel arbitration and to stay this litigation under the Missouri Uniform Arbitration Act ("MUAA"), sections 435.350-435.470 RSMo, and the Federal Arbitration Act ("FAA"), 9 U.S.C. § 1, *et seq*. On September 17, 2003, the Circuit Court of Greene County issued a letter opinion denying the motion. The Circuit Court then entered an order denying Appellants' motion for rehearing on January 22, 2005.

Under RSMo § 435.440.1(1), "an appeal may be taken from . . . an order denying an application to compel arbitration made under section 435.355." The FAA also provides that such an order denying arbitration is subject to appellate review. *See* 9 U.S.C. § 16(a)(1)(B).

Appellants filed a timely notice of appeal to the Missouri Court of Appeals, Southern District. On April 15, 2005, the Court of Appeals issued a unanimous decision reversing the trial court's judgment. On May 6, 2005, the Court of Appeals denied Respondents' motion for rehearing and application for transfer.

Respondents filed an application for transfer under Rule 83.02 with this Court, which was granted on June 21, 2005. Under Mo. Const. art. V, § 10, the Court has jurisdiction as if this case were being heard on original appeal.

STATEMENT OF FACTS

A. Preliminary Statement

This dispute arises from business relationships between Appellants and Respondents in multi-level sales and distribution networks for consumer goods manufactured and sold by Amway Corporation, now known as "Alticor" and "Quixtar," and for business tools and motivational materials sold to support these sales and distribution networks. Respondent Netco was an Amway distributor, selling Amway products and related "business support materials" ("BSMs"). Respondent Schmitz Associates "facilitated the Amway-related rally, convention and function business for Charlie and Kim Schmitz (Netco), and operated in tandem with Netco to build, support and enhance the Amway business." (A0004.) Respondents, which have common ownership, officers, offices, e-mail and letterhead, refer to themselves, along with their principals, Charlie and Kim Schmitz, as the "Schmitz Organization." Nine of the Appellants are Amway distributors or principals of Amway distributors, and the remaining two (Pro Net and Global Support Services) distribute Amway-related business support materials. The Schmitz Organization (including Respondents) was a member of Pro Net, an association that supported the Amway-related BSMs businesss of its members.

Respondents claim in this action that Appellants conspired to deprive them of the full business and financial benefits of the Amway business and the Amway-related BSMs business. At issue before this Court is whether Respondents must comply with two

written arbitration agreements. The first agreement binds all Amway distributors and their principals to arbitrate all Amway-related disputes. The second agreement, the Pro Net Terms and Conditions, binds all Pro Net members to follow the Amway Rules (including its arbitration provisions) and includes a separate arbitration agreement for all Pro Net-related disputes.

B. The Amway Business

Amway, a nonparty corporation, is a multi-level marketing business that administers a worldwide network of independent distributors selling consumer goods and products. (A3761-62.)[1] Amway's distributors, sometimes called Independent Business Owners, or "IBOs," earn money by selling Amway-related goods to customers, and by sponsoring new distributors, who in turn sell products and sponsor new, "downline" distributors. (A3762.) There are more than 700,000 independent Amway distributors in North America. (A2741.)

Amway maintains its structure through establishing and enforcing the Amway Rules of Conduct (the "Amway Rules" or the "Rules of Conduct"), which govern the conduct of Amway-related businesses. (A1197; A1200.) All Amway distributors are required to sign a Distributor Application agreeing to "comply with the Amway Sales and Marketing Plan as set forth in official Amway literature and to observe the spirit as well

[1] References to Appellants' Legal File are denominated in this Brief as "A___." For the Court's convenience, the decisions below, excerpts from the Uniform Arbitration Act, and relevant record material are included in the accompanying appendix.

as the letter of the Amway Code of Ethics and Rules of Conduct." (A0062-63.) Amway distributorships were and are required to be renewed each year, and renewal always includes an agreement to abide by the current Rules of Conduct. (A0063.)

The Amway network of distributors is organized by "lines of sponsorship" that maintain relationships between higher-tier or "upline" distributors and their lower-tier or "downline" distributors. These lines of sponsorship are established by the Rules of Conduct. (A0017.)

An important part of the "Amway Business" is the training, guidance and motivation of a distributor's "downline" sales force. (A0012.) To provide this support, many Amway distributors participate in the Amway-related "tool" and "function" business. "Tools," which often are referred to as business support materials, or BSMs, include audio and video tapes, printed literature, books, and electronic literature. (A0011-12.) "Functions" include events such as motivational seminars, rallies, and conventions. (*Id.*) Various Amway distributors sell BSMs and sponsor meetings and functions, which can also generate profits.

C. Respondents' Amway-Related Businesses

Charlie Schmitz, the President of Netco and of Schmitz Associates, first applied to become an Amway distributor in 1984, and signed an Automatic Renewal Form in 1985. (A0073; A0106.) In signing the automatic renewal form, Mr. Schmitz agreed "to comply with the Amway Sales and Marketing Plan and to observe and abide by the Code of Ethics and Rules of Conduct of Amway Distributors, and all other rules, requirements and regulations as they are set forth from time to time in official Amway literature." (*Id.*)

In 1990, Charlie and Kim Schmitz ("the Schmitzes") "assigned" Mr. Schmitz's Amway distributorship to Netco. (A0153.) In 1991 they completed a corporate Distributor Application for Netco. (A0067-70.) Netco continued the business under the same Amway distributorship number and with the same "line of sponsorship." (A3072-73.) In their "Application for Amway Distributor Authorization (Corporate)," Netco and its principals, the Schmitzes, agreed to "comply with the Amway Sales and Marketing Plan and Code of Ethics and Rules of Conduct for Amway distributors." (A0069.) In so doing, the Schmitzes agreed as individuals and as Netco officers to comply with the Amway Rules of Conduct. (*Id.*) Additionally, Netco and its principals, the Schmitzes, acknowledged that "all Amway distributors must apply for and receive Amway Distributor Authorization yearly." (A0068.)

The Netco/Schmitz Amway and Amway-related BSMs business prospered. Successful Amway distributors are sometimes recognized as having attained various "pin levels" of achievement, and the Amway distributorship operated through Netco was a "Diamond" distributor, one of the highest levels of distributorship. (A0011.)

In addition to selling Amway products and sponsoring an active downline of distributors, Netco was also involved in the Amway-related "tool and function" business, including sponsoring "major functions" and selling business support materials (A0020-21.)

Respondent Schmitz Associates, also owned by the Schmitzes, "facilitated the Amway-related rally, convention and function business for Charlie and Kim Schmitz (Netco), and operated in tandem with Netco to build, support and enhance the Amway

business." (A0004.) Netco and Schmitz Associates engaged in "the promotion of Amway through the independent efforts of Amway distributors," including sponsoring of functions and distribution of literature, tapes and other BSMs or "tools." (A0003; A0011-12.) Netco and Schmitz Associates worked "in concert" at "developing their Amway and/or Amway-related businesses, which included selling Amway products and BSMs." (A0021.) Respondents' principals acknowledge that from 1984 to 1999 they were "building Netco and Schmitz Associates, making Amway their full-time jobs and relying on their Amway-related income as their primary means of support."[2] (A0018.)

[2] Many of the cited background facts were pled by Respondents in their June 27, 2000 Petition. (A0001-42.) These statements of fact are "admissible as evidence in the proceeding in which it was originally filed to show an admission against interest or for impeachment purposes." *Bank of America, N.A. v. Stevens*, 83 S.W.3d 47, 56 (Mo. App. S.D. 2002) (citing *Wahl v. Cunningham*, 56 S.W.2d 1052, 1059 (Mo. banc 1932)). Respondents' view of the world changed radically after Appellants sought arbitration, and Respondents' First Amended Petition, was carefully "scrubbed" of factual assertions that would support Appellants' Motion. (A0544-620.) *Compare* A0012 (BSMs business is "**an integral part** of the Amway business") (emphasis added) *with* A0569 (**"BSMs industry is not a part of the Amway business"**) (emphasis in original). Such dramatic factual surgery illustrates Respondents' awareness that the actual facts are wholly inconsistent with their argument that they need not arbitrate their disputes.

Sales of BSMs and attendance at "functions . . . served as an integral part of the Amway business" for Respondents. (A0012.) Respondents claim that "Amway requires distributors to 'train' and 'motivate' the downline distributors in their line of sponsorship," and "has sanctioned the use of BSMs within and by the Amway distributorship network." (*Id*.) Amway also required "content approval" of the materials, even those not produced by Amway. (*Id*.) Respondents assert and admit that "the Schmitz Network of downline distributors served as a lucrative market for the sale of Amway-related instructional and motivational materials." (A0561.) *Both* Netco and Schmitz Associates "purchased and resold independently-produced BSMs." (A0021.)

Respondents worked "[w]ithin this framework" by "developing their respective Amway distributorships, as well as promoting and selling BSMs to their respective downline groups." (A0012.) Respondents admit that the rules for the "tools" business were intended to be consistent with the Amway Rules of Conduct for distributors, and that "strict adherence to the [Amway] lines of sponsorship [was] recognized within these rules and the course of dealings for BSMs." (A0014.) Indeed, Respondents assert that Amway itself "prescribed" the system for selling business support materials "to recognize and honor the essential lines of sponsorship." (A0015.)

Netco and Schmitz Associates are both solely owned and controlled by the Schmitzes, who are officers of both entities. (A0004; A0910; A3032.) The Schmitzes are Netco's only employees, as well as its only directors and shareholders. (A0910.)

Schmitz & Associates, operating "in tandem" with Netco, (A0004), appears to operate essentially as a shell, with the Schmitzes as its only officers and directors.

(A0910.) Schmitz never had any employees; instead, it pays Netco a management fee to perform its operations. (A3032.) While "working in concert . . . buying and selling Amway products and BSMs," (A0021) both Respondents operated out of the same office in St. Joseph, Missouri, sharing office equipment, a fax number, letterhead and the same e-mail address. (A3067-68.)

The Schmitzes, Netco, and Schmitz & Associates refer to themselves collectively as the "Schmitz Organization." (A0550-51.)

D. Appellants' Amway-Related Businesses

Appellants (other than Pro Net and Global Support Services, Inc.) are Amway distributors, Amway-related businesses, or principals of Amway businesses.[3]

[3] *See* (A0682; A0702) (Gooch operates an Amway distributorship); (A0702) (Gooch Support purchases and resells Amway-related business support materials); (*id.*) (Gooch Enterprises operates as the "functions portion" of Gooch's Amway and Amway-related businesses); (A0737) (Dunn operates an Amway distributorship); (*id.*) (Dunn Associates purchases and resells Amway-related business support materials and organizes seminars and functions for Amway distributors); (A0666) (Childers is the principal of a distributor of Amway products); (*id.*) (TNT purchases and resells Amway-related business support materials); (A1824) (Evans is an Amway distributor); (A0553) (Evans Associates purchases and resells BSMs); (A0772) (Pro Net is an association whose members are distributors of Amway products and Amway-related BSMs with the purpose of promoting the common business interests of its members); (A0805-06) (Global Support

(footnote continued on next page)

Respondents admit that all Appellants other than Pro Net and Global "are/were upline distributors to [Respondents] in their respective Amway lines of sponsorship." (A0010.)[4] Appellants also participated in the motivation and training function, producing "tools" and "BSMs" and sponsoring meetings, conventions and rallies.

E. The Amway BSMs Rules

The Amway Rules of Conduct contain specific rules pertaining to the sale and distribution of BSMs. (A1245.) The Rules state: "Some distributors offer for sale to other distributors in their line of sponsorship a variety of non-Amway-produced sponsoring and merchandising aids," and require that "distributors who choose to sell, purchase, or utilize such Materials must comply with these Rules." (*Id.*)

Respondents admit Amway's "prescribed" rules are applied in order to avoid "unwarranted and unreasonable interference in the business of other Amway distributors." (A0015.) Respondents also acknowledge that sales of BSMs are "inextricably connected" with the Amway business. (A0016.)

(footnote continued from previous page)

"is in the business of warehousing, selling, and distributing business support materials for use by Amway distributors").

[4] Appellants Gooch, Gooch Support, Childers, TNT, Pro Net, and Global Support Services filed a motion to dismiss for lack of personal jurisdiction, which has been withdrawn without prejudice (A0453-55), but joined the motion to compel arbitration and stay litigation to the extent the jurisdictional motion was denied. (A0049.)

When this dispute first arose between the parties, Respondents invoked Amway's Rules of Conduct, asserting that the Rules of Conduct apply to "prohibit Amway distributors from selling tools to other Amway distributors whom the selling distributor did not personally sponsor." (A0017.)

F. The Amway Arbitration Rules

In September 1997, Amway's Rules of Conduct were amended to include an arbitration provision. (A0064.) These dispute resolution procedures, involving an informal conciliation process, a formal conciliation process, and arbitration were included in the Rules of Conduct beginning in 1998. (A1262-67.) If the conciliation processes do not resolve disputes, Amway distributors are required:

> to submit any remaining claim(s) arising out of or relating to their Amway Distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct (including any claim against another Amway distributor, or any such distributor's officers, directors, agents, or employees or against Amway Corporation or any of its officers, directors, agents, or employees) to binding arbitration in accordance with the Amway/ADA Arbitration Rules.

(A1268; *see also* A1338-39.) The Rules of Conduct also state that the United States Arbitration Act shall govern the arbitration provisions. *Id.*

Respondents claim ignorance of the Amway arbitration provision. However, Amway informed all of its distributors, including Respondents, of this change in several Amway publications including the September 1997 issue of the *Amagram*, the company's monthly distributor magazine through which it routinely announces such rule changes. (A0096-97.) Mr. Schmitz is familiar with the *Amagram* and knows that changes in the Amway Rules were published in that publication. (A3086.) Amway also mailed at least three letters to all its distributors, including Netco, during 1997 and 1998 highlighting the changes to Amway's rules, including the adoption of the binding arbitration provisions. (A2733; A2735; A2737.)

Accordingly, Respondents were repeatedly and directly informed of the Amway arbitration requirement (A2733; A2735; A2737 & A3511.) It is indisputable that Netco in fact received this information, since Netco produced a complete copy of the Amway Rules of Conduct, including the arbitration provision, in discovery. (A3267; A3398-3533 & A3511.)

G. The Formation of Pro Net

Appellant Pro Net is an association of organizations engaged in the Amway business and the Amway-related business of selling BSMs. (A0772.) Pro Net was formed to support the Amway-related "tool and function" businesses of its members, and to facilitate the sale of Amway-related business support materials. (A2311.) The founders of Pro Net, Appellants Hal Gooch and Billy Childers, and nonparties Ken Stewart, Steve Woods and Tim Foley, set up Pro Net to facilitate the sale and marketing of BSMs by Pro Net members. (A2329; A2346; A2087; A2311-12.)

Pro Net developed terms and conditions of membership, including a requirement that members transfer the copyright and intellectual property rights in their tapes to Pro Net. (A2088-89.) Pro Net, in turn, would make the members' tapes available for sale and distribution to all other Pro Net members through Global Support Services. (A2090.) In this way, Pro Net created a large pool of BSMs for purchase and re-sale by Pro Net members.

H. Respondents' Membership in Pro Net

On or about December 9, 1998, Charlie Schmitz, in the name of "Netco, Inc. (Charlie and Kim Schmitz)" submitted a Pro Net Membership Application Form. (A2136.)[5] Immediately above the space for "member name" was the statement "The undersigned applicant agrees to abide by all Terms and Conditions of Association Membership." (*Id.*) Mr. Schmitz signed the application, but wrote on it: "I sign this with the understanding that I am not giving up my right to buy-sell or produce business support materials from other suppliers or manufacturers." (*Id.*)[6]

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[5] Appellants Childers, Gooch and Dunn also submitted applications to Pro Net agreeing to be bound by the Pro Net Terms and Conditions of Membership. (A2131 (Childers); A2324 (Gooch); A2667 (Dunn).) The applications covered both the individuals and their respective organizations. (A2313; A2089; A2663-64.)

[6] Although there was some initial reluctance by Pro Net to accept this reservation, Pro Net then accepted Netco's application as submitted, and Netco and the Schmitzes became members of Pro Net and were granted full membership benefits. (A2091; A2315;

(footnote continued on next page)

Netco also submitted a check for membership in Pro Net, which was accepted and deposited by Pro Net into its bank account (A2137; A2091), and the Schmitzes attended several Pro Net functions in 1998 and 1999. (A2091.) As part of its membership in Pro Net, Netco also purchased more than 100,000 Pro Net tapes and other BSMs from Global in 1998 and 1999. (A2516-17; A2520.) Pro Net also offered for sale to all other Pro Net members the tapes and speeches of the Schmitzes through Global Support. (A2517-18.)

By applying for Pro Net membership, paying the membership fee, attending Pro Net functions, and purchasing thousands of Pro Net BSMs, the Schmitz Organization, including Netco and its principals, Charlie and Kim Schmitz, and their BSMs business Schmitz & Associates, became members of Pro Net, and agreed to abide by the Pro Net Terms and Conditions. (A2091; A2315; A2332; A2350.)

I. The Pro Net Arbitration Provision

When the Pro Net Steering Committee was developing the Terms and Conditions of Pro Net membership, one of the issues the committee focused on was alternative dispute resolution. (A2087-88; A2330; A2360-61.) The Pro Net Terms and Conditions included, in pertinent part, the following arbitration agreement:

(footnote continued from previous page)

A2332; A2350.) Netco and the Schmitzes accepted those membership benefits, participating in Pro Net functions and buying over 100,000 tapes and other BSMs through the Pro Net system. (A2516-17; A2520.)

> Any dispute, controversy, or claim arising out of, relating to, or concerning the interpretation or performance of the contract created by acceptance of the Membership Application, or the breach thereof, or any dispute, controversy, or claim between one or more members of the Association or between the Association and any of its members which cannot be resolved through negotiation (each, a "Dispute") shall be submitted to mediation administered by the Association. Each party to the dispute shall name a mediator who shall be an Association Member at the diamond level or higher of Amway. Upon the selection of two mediators, the two chosen mediators shall select a third mediator who shall be an Association Member at the diamond level or higher of Amway. ***If agreement is not reached by the parties by mediation, any Dispute shall be submitted to and settled by binding arbitration administered by the American Arbitration Association under its Commercial Arbitration Rules in effect at that time, and judgment on the award rendered by the arbitrator(s) may be entered in any court having jurisdiction***.

(A2141; emphasis added.) All members of Pro Net, including Respondents, were required to agree to this arbitration agreement. (A0108; A2141.)

In addition to the arbitration language contained in the Membership Terms and Conditions, Pro Net members were also notified of the Pro Net arbitration agreement at a kick-off meeting for Pro Net in Myrtle Beach, South Carolina, in May of 1998. (A2090.) At that meeting, a summary of the Pro Net benefits and obligations was distributed. (*Id.*) Under the heading "**Dispute Resolution**," the summary states:

> The Association recognizes that conflicts and disputes can occur in any association relationship. The Association is intended to further the interests of its members and to address disputes fairly. Thus, the Association has put into place procedures to avoid litigation, and to encourage resolution of disputes among Amway distributors in the most private and cost effective manner. Accordingly, by joining the Association, Member acknowledges that, pursuant to the Terms and Conditions incorporated into this Membership Application, Member is agreeing to participate and abide by Association dispute resolution procedures consisting of Association mediation procedures, ***and use of American Arbitration Association arbitration procedures if the dispute is not resolved through internal Association mediation***.

(A2096; emphasis added.)

As Diamond Amway distributors in the Gooch line of sponsorship, the Schmitzes were invited to and did attend this 1998 "kick off" meeting. (A2090; A2314.)

J. Respondents' Lawsuit and Appellants' Motion to Compel Arbitration

On June 27, 2000, Netco and Schmitz & Associates filed this action, alleging, *inter alia*, that the Appellants had breached an implied in fact contract concerning "tools" used and "functions" attended by Amway distributors.[7] (A0001-44; A0037; A0039.)

Appellants moved the Circuit Court to compel arbitration and stay litigation, arguing that the Respondents were bound to arbitrate their claims under the Amway Rules of Conduct, and also under the Pro Net Arbitration Terms and Conditions. (A0049-123.)

In December 2000, this action was transferred to the Circuit Court of Greene County. (A0301-02.) On September 17, 2003, after extensive briefing, discovery, and a hearing on Appellants' motion to compel arbitration, the Greene County Circuit Court issued a one-page letter opinion denying the Appellants' motion to compel arbitration. (A3748-49.)

The trial court began its opinion noting that it had "studied the wonderfully detailed opinion" regarding the arbitration agreements under both the Amway Rules of Conduct and the Pro Net Terms and Conditions that had been issued by the Florida Circuit Court in *U-Can-II, Inc. v. Setzer*, No. 02-2535-CA CV-B (Fla. Cir. Ct., Apr. 23, 2003) ("*U-Can-II*"), *aff'd in pertinent part, rev'd in part,* 870 So. 2d 99 (Fla. Dist. Ct.

[7] Joanne Schmitz d/b/a Schmitz & Co. and R.K. Kelm Co., L.L.C. were originally plaintiffs in this action, but voluntarily dismissed their claims, and claims against four additional Appellants were dropped. (A0301; A0523.)

App. 2003) (A3833-51), a case involving substantially identical Amway-related claims brought by a different Amway distributor against many of the Appellants in this case. (A3849.) In *U-Can-II*, the Florida Circuit Court ordered arbitration under ***both*** the Amway Rules of Conduct and the Pro Net Terms and Conditions. (A3849-50.) That ruling was upheld on appeal, except for an "agency/alter ego" issue not relevant here. 870 So. 2d at 100. (A3852-53.)

The trial court below noted that it "agree[ed] with many of the conclusions" reached by the Florida Circuit Court. (A3749.) However, the court below denied Respondents' arbitration motion, solely on its view that the Amway arbitration procedures were "unconscionable":

> [Amway Distributor Association] board members, some of whom are actual parties to this litigation, have veto power over the retention of these arbitrators in their jobs. That, coupled with the fact that Amway is not bound by its own arbitration requirements and the fact that all proceedings are held in secret leads me to believe that the Amway arbitration provisions are, both substantively and procedurally unconscionable.

(A3749.)

The trial court also declined to order arbitration under the Pro Net Terms and Conditions but never mentioned that separate arbitration agreement in any way, even

though it provided for arbitration administered by the American Arbitration Association ("AAA") rather than the Amway arbitration procedures. (*Id.*)

Appellants timely moved for a rehearing of the Circuit Court's ruling, which was denied on January 22, 2004. (A3756; A3914.) On February 2, 2004, Appellants filed their Notice of Appeal with the Court of Appeals. (A3915-31.)

After briefing and oral argument, the Court of Appeals, in a unanimous opinion, ordered arbitration of all of Respondents' claims under the Pro Net Terms and Conditions. After unsuccessfully moving the Court of Appeals from rehearing or transfer, Respondents applied to this Court for an Order of Transfer. This Court granted the application on June 21, 2005.

POINTS RELIED ON

I. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration, because (1) the Arbitration Agreement in the Amway Rules of Conduct bound Respondents and all of the parties to arbitration, and (2) Respondents' claims were within the scope of the Amway Arbitration Agreement

Fru-Con Constr. Co. v. Southwestern Redev. Corp. II, 908 S.W.2d 741 (Mo. App. E.D. 1995)

Tractor-Trailer Supply Co. v. NCR Corp., 873 S.W.2d 627, 631 (Mo. App. E.D. 1994)

Houlihan v. Offerman & Co., 31 F.3d 692 (8th Cir. 1994)

II. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration, because the Trial Court erred as a matter of law in concluding that the Amway Arbitration Procedures were unconscionable, and erred as a matter of law in failing to recognize that allegedly unconscionable procedures should be severed from the Amway Rules of Conduct

Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79 (2002)

Gannon v. Circuit City Stores, Inc., 262 F.3d 677 (8th Cir. 2001)

Morrison v. Amway Corp., 49 F. Supp. 2d 529 (S.D. Tex. 1998)

III. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration, because the Trial Court failed to address the separate arbitration clause in the Pro Net Terms and Conditions, which independently bound all of the parties to arbitrate all issues in this case under the unimpeachable Rules of the American Arbitration Association ("AAA")

Fru-Con Constr. Co. v. Southwestern Redev. Corp. II, 908 S.W.2d 741 (Mo. App. E.D. 1995)

Tractor-Trailer Supply Co. v. NCR Corp., 873 S.W.2d 627 (Mo. App. E.D. 1994)

Bob Schultz Motors, Inc. v. Kawasaki Motors Corp., U.S.A., 334 F.3d 721 (8th Cir. 2003)

ARGUMENT

I. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration, because (1) the Amway Arbitration Agreement in the Amway Rules of Conduct bound Respondents and all of the parties to arbitration, and (2) Respondents' claims are within the scope of the Amway Arbitration Agreement

A. Standard of Review

The trial court's denial of the motion to compel arbitration is reviewed *de novo*. *Dunn Indus. Group, Inc. v. City of Sugar Creek*, 112 S.W.3d 421, 428 (Mo. banc 2003).

B. Respondents are not entitled to a jury trial as to the making of the arbitration agreements at issue

As a preliminary matter, the appropriate procedure to be applied in the determination of a motion to compel arbitration has been raised as an issue in this case. In sum, any claim of a right to a jury trial on Appellants' motion to compel arbitration must fail because the procedures embedded in the Missouri Uniform Arbitration Act ("MUAA") provide that a court, sitting without a jury, should "proceed summarily" to decide such a motion.

The Missouri procedural requirement of a summary procedure determining arbitrability is fully consistent with the federal policy set forth in the FAA that arbitrations should be conducted quickly and efficiently. The summary procedure requirement is fully consistent with the Missouri Constitution because Appellants'

motion for an order compelling arbitration is an action for specific performance under a contract – an equitable remedy not triable to a jury. Any manufactured "right" to a jury trial on arbitrability – in order to determine whether Respondents have a right to a jury trial on the merits – would undermine the purposes of the FAA, create conflict among states that have adopted the Uniform Arbitration Act, and vitiate the right and the ability of Missouri businesses to agree to arbitrate disputes.

This Court also should not permit Missouri procedural law to be replaced by the procedures of FAA § 4. As we show below, even if the procedural aspects of FAA § 4 were applied to this Missouri action, there would be no right to a jury trial under this federal procedure because there are no genuine issues of material fact regarding the existence or scope of the arbitration provisions at issue. Any attempt to graft federal procedure into this case should nonetheless be rejected. A fundamental principle of federalism is that, except in rare situations, "[t]here has been no surrender by the states of the right to establish their own courts, to define and limit their jurisdiction and functions, and to regulate and control them in all respects." *Ex parte Gounis*, 263 S.W. 988, 990 (Mo. 1924). It is "settled constitutional law" that "Congress cannot . . . regulate or control their modes of procedure." *Id.*

Under established Missouri motions practice, it is within the sound discretion of the Circuit Court to determine whether to hold an evidentiary hearing on a motion to compel arbitration. Regardless of how this issue is resolved, and indeed even if the procedures of FAA § 4 are applied, the outcome is the same under the facts of this case

because Respondents cannot show a genuine issue of material fact, and the motion to compel arbitration should be granted.

1. Missouri law provides for a court, without a jury, to decide whether to grant specific performance on a motion to compel arbitration

a. The MUAA provides for a court to "proceed summarily"

In June 1980, Missouri enacted the MUAA as a modified version of the Uniform Arbitration Act of 1955 ("UAA"), which, in turn, was based on Congress's passage of the FAA in 1925. All three Acts are intended to allow parties to resolve their disputes in an easier and less expensive manner than by litigation. *See generally* 1 Larry E. Edmondson, *Domke on Commercial Arbitration* § 22:13, at 22-41 (3d ed. 2003).

The MUAA provides opportunities for judicial intervention at various stages of the arbitration process. Under section 435.425 (UAA § 16), all such applications to the court are to be "heard in the manner and upon the notice provided by law or rule of court for the making and hearing of motions." This provision is similar to FAA § 6, which "expedite[s] judicial treatment of matters pertaining to arbitration." *World Brilliance Corp. v. Bethlehem Steel Co.*, 342 F.2d 362, 365-66 (2d Cir. 1965).

The first opportunity to apply to a court under the MUAA arises when disputes to arbitrability arise. *See* RSMo § 435.355.1 (UAA § 2(a)). Under this provision, "if the opposing party denies the existence of the agreement to arbitrate, the court ***shall proceed summarily to the determination of the issue so raised*** and shall order arbitration if found for the moving party; otherwise, the application shall be denied." *Id.* (emphasis added).

This Court has explained that under section 435.355.1 "a court may order parties to proceed to arbitration on the application of a party showing an agreement to arbitrate as provided in section 435.350."[8] *Murray v. Missouri Highway & Transp. Comm'n*, 37 S.W.3d 228, 233 (Mo. banc 2001).

Conversely, under section 435.355.2 (UAA § 2(b)), a court may stay arbitration that is either threatened or pending on a showing that there is no such agreement. "***Such an issue, when in substantial and bona fide dispute, shall be forthwith and summarily tried*** . . . ." *Id.* (emphasis added.) In *St. Luke's Hosp. v. Midwest Mechanical Contractors, Inc.*, 681 S.W.2d 482 (Mo. App. W.D. 1984), it was found as a matter of first impression that, under section 435.355.2, "***[t]he court is authorized to summarily and forthwith try the issue and render its decision upon the evidence submitted by the parties***." *Id.* at 487 (emphasis added).

Thus, in either case, when disputes regarding arbitrability arise, "upon application of a party to enforce the agreement, or alternatively to stay a proceeding, the provision is

[8] Under section 435.350, "[a] written agreement to submit any existing controversy to arbitration or a provision in a written contract, except contracts of insurance and contracts of adhesion, to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable and irrevocable, save upon such grounds as exist at law or in equity for the revocation of any contract." Other than its exclusion of "contracts of insurance and contracts of adhesion," this language tracks UAA § 1.

to be taken up by a court having jurisdiction[] and decided promptly. *State ex rel. Telecom Mgmt. v. O'Malley*, 965 S.W.2d 215, 219 (Mo. App. W.D. 1998).

Therefore, while Missouri courts have not addressed the specific question of a party's right to a jury under section 435.355.1, the statutory language and existing case law clearly show that the section should not be read to include such a right.

Moreover, this understanding of "proceed summarily" is consistent with this Court's longstanding definition of "summary manner" as "forthwith and without regard to the established course of legal proceeding." *Birmingham Drainage District v. Chicago, B. & Q. R. Co.*, 202 S.W. 404, 408 (Mo. 1917). Citing this case, the Eastern District Court of Appeals recently noted that "***the term 'summary manner' does not envisage the use of standard discovery mechanisms or jury trials***." *In re Fabius River Drainage Dist.*, 35 S.W.3d 473, 485 (Mo. App. E.D. 2000) (emphasis added).

The *Fabius* court also cited this Court's guidance in *Semple's Estate v. Travelers Indem. Co.*, 603 S.W.2d 942 (Mo. 1980), that "***trial court proceedings that include a jury trial are not conducted in a 'summary manner.'***" 35 S.W.3d at 485 (emphasis added). In *Semple's Estate*, the Court, while affirming a judgment under the probate code, noted that section 435.207 is "a summary procedure" and that, contrary to this section, the party's "liability was not determined in a summary manner, but in a jury trial." 603 S.W.3d at 945. In language similar to the MUAA, section 435.207 provides that "[o]n breach of the obligation of the bond of the personal representative, ***the court*** . . . ***may summarily determine the damages*** . . . ." (Emphasis added.) Thus, this Court's

observation in *Semple* that summary proceedings do not include jury trials is particularly relevant here.

b. Other states and the National Conference of Commissioners have found that a motion to compel arbitration is subject to a bench determination

Uniform construction among the states adopting the UAA is one of the primary purposes of the uniform statute, and the MUAA – in section 435.450 (UAA § 21) – provides that it "shall be so construed as to effectuate [this] general purpose." This statutory directive "gives special value to the precedents of other states on the same issue." *State ex rel. Tri-City Constr. Co. v. Marsh*, 668 S.W.2d 148, 150 (Mo. App. W.D. 1984).

It is therefore highly significant that other state supreme courts hold that proceeding "summarily" under the UAA means simply and without a jury. Most recently, on June 28, 2005, the Supreme Court of Oklahoma set out the "summary procedures" whereby a court, alone, is to decide a motion to compel arbitration under the Oklahoma Uniform Arbitration Act. *Rogers v. Dell Computer Corp.*, No. 99,991, 2005 Okla. LEXIS 49 (Ok. June 28, 2005).

This holding is consistent with high court decisions in California and Texas mandating such bench determinations. *See, e.g., Rosenthal v. Great Western Fin Secs. Corp.*, 926 P.2d 1061, 1072 (Cal. 1996) ("A party opposing contractual arbitration of a dispute does not have the right to a jury trial of the existence or validity of the arbitration agreement."); *Jack B. Anglin Co. v. Tipps*, 842 S.W.2d 266 (Tex. 1992) ("When Texas

courts are called on to decide if disputed claims fall within the scope of an arbitration clause under the Federal Act, Texas [summary] procedure controls that determination.").

In contrast to the wealth of authority and logic supporting the notion that "summary" procedures do not include jury trials, we are not aware of *any* court holding that the UAA mandates a jury trial on a motion to compel arbitration. This understanding is reflected in the Revised Uniform Arbitration Act ("RUAA") adopted by the National Conference of Commissioners on Uniform State Laws ("NCCUSL") in 2000. *See generally* Timothy J. Heinsz, *Arbitration Law: Is There a RUAA in Missouri's Future?*, 57 Mo. B.J. 53 (2001).

While not yet binding in Missouri, the RUAA provides a useful lens through which to examine the MUAA. RUAA § 5, for instance, is based on UAA § 16 (section 435.425) and provides that arbitration-related applications are to be made by motion. Official Comment 1 to this section notes, in part, that "***legal actions to a court involving an arbitration matter under the RUAA will be by motion and not by trial***." (Emphasis added.) Official Comment 2 further observes: "Legal actions under both the UAA and FAA generally are conducted by motion practice and are not subject to the delays of a civil trial. This system has worked well and the intent of Section 5 is to retain it."

Perhaps most importantly, RUAA § 7 retains the language of UAA § 2(a) (section 435.355.1) providing that, if a party opposes arbitration, "the court shall proceed summarily to decide the issue . . . ." The Official Comment notes:

> ***The term "summarily" in Section 7(a) and (b) is presently in UAA Section 2(a) and (b) [and section 435.355]. It has been***

> ***defined to mean that a trial court should act expeditiously and without a jury trial to determine whether a valid arbitration agreement exists. . . .***

Official Comment to RUAA § 7 (citations omitted) (emphasis added). In reviewing RUAA § 7, two scholars noted:

> ***Significantly, the RUAA drafters . . . reiterate[d] the UAA rule that application for judicial relief (for enforcement of the arbitration agreement or otherwise) is to be made and decided as a motion, rather than by trial as provided in the FAA.*** As a result, state actions to enforce arbitration agreements under the RUAA are not complicated by jury trial rights, as is true under the FAA.[9]

Stephen L. Hayford & Alan R. Palmiter, *Arbitration Federalism: A State Role in Commercial Arbitration*, 54 Fla. L. Rev. 175, 216 (2002) (footnote omitted) (emphasis added).

[9] As discussed in detail below, even under the FAA, these "jury trial rights" attach only upon a showing that there are genuine issues of material fact regarding the making of the arbitration agreement. *See, e.g.*, *Third Millennium Techs., Inc. v. Bentley Sys., Inc.*, No. 03-1145-JTM, 2003 U.S. Dist. LEXIS 14662, at *6 (D. Kan. Aug. 21, 2003).

c. The MUAA codifies the constitutional principle that there is no right to a jury trial or the equitable remedy of specific performance

As this Court has explained, an agreement to forego the use of litigation is enforceable under the Missouri Constitution:

> Our courts have held that a party may contractually relinquish fundamental and due process rights. ***Arbitration agreements are an example where the courts have upheld the parties' right to contractually agree to relinquish substantial rights. In every arbitration agreement, the parties not only agree to waive a jury trial but also to give up their right to present their claim to any judicial tribunal deciding the case.***

Malan Realty Investors, Inc. v. Harris, 953 S.W. 2d 624, 626 (Mo. banc 1997) (footnote omitted) (emphasis added).

Enforcement of an arbitration agreement does not touch upon these "substantial rights" because a court has "no business weighing the merits of the [underlying] grievance" when deciding a motion to compel arbitration. *Village of Cairo v. Bodine Contracting Co*., 685 S.W.2d 253, 260 (Mo. App. W.D. 1985) (quoting *United Steelworkers of Am. v. Am. Mfg. Co.*, 363 U.S. 564, 567 (1960)). Indeed, section 435.355.5 (UAA § 2(e)) specifically provides that "[a]n order for arbitration shall not be refused on the ground that the claim in issue lacks merits or bona fides . . . ."

Therefore, "[a]n order compelling arbitration is in fact an order for specific performance, the duty to arbitrate arising from, and being governed by, the contract creating it." *Pettinaro Constr. Co. v. Harry C. Partridge, Jr. & Sons, Inc.*, 408 A.2d 957, 962 (Del. 1979); *see also Rosenthal*, 926 P.2d at 1070 ("A petition to compel arbitration is in essence a suit in equity to compel specific performance of a contract.") (quotation omitted).

These holdings are consistent with the long line of decisions by this Court that "[t]o decree specific performance of certain contracts has long been a function of courts of equity. It is purely an equitable remedy and therefore governed by equitable principles." *Hoover v. Wright*, 202 S.W.2d 83, 86 (Mo. 1947). As this Court explained just last year: "[L]abeling an action as equitable or legal in the modern sense typically bespeaks the type of relief being sought. Equitable remedies are coercive remedies like declaratory judgments and injunctions, the latter of which includes ***specific performance*** and some types of restitution." *State ex rel. Leonardi v. Sherry*, 137 S.W.3d 462, 470 (Mo. banc 2004) (citations omitted) (emphasis added).

After analyzing the equitable nature of specific performance, the California Supreme Court held in its leading *Rosenthal* decision: "We find no violation of state constitutional rights in the summary procedure for decision, without jury, of whether a valid arbitration agreement exists." 926 P.2d at 1070. "The plaintiff is not impermissibly denied a jury trial when the superior court decides only the facts necessary to determine specific enforceability of an arbitration agreement, an equitable question as to which no jury trial right exists." *Id.* at 1071.

The same conclusion should be reached here because "Missouri's constitutional guarantee to a jury trial has never been applied to claims seeking equitable relief." *Sherry*, 137 S.W.3d at 472; *see also State ex rel. Diehl v. O'Malley*, 95 S.W.3d 82, 85 (Mo. banc 2003) ("An action that is equitable in nature, as viewed in historical perspective and with respect to the equitable remedy sought, does not come within the jury trial guarantee.").

2. The procedures of FAA § 4 do not preempt those of section 435.355.1

Although the FAA creates a substantive arbitration right applicable in state as well as federal courts, it also includes procedural provisions prescribing rules applicable only in federal courts or arbitrations themselves. *See, e.g., Cronus Inv., Inc. v. Concierge Servs.*, 107 P.3d 217, 225-26 (Cal. 2005). This dichotomy has been noted several times by the U.S. Supreme Court, including in *Southland Corp. v. Keating*, 465 U.S. 1 (1984):

> In holding that the [FAA] preempts a state law that withdraws the power to enforce arbitration agreements, we do not hold that §§ 3 and 4 of the Arbitration Act apply to proceedings in state courts. Section 4, for example, provides that the Federal Rules of Civil Procedure apply in proceedings to compel arbitration. The Federal Rules do not apply in such state-court proceedings.

Id. at 15 n.10.

Consistent with these principles, this Court should enforce the substance of the FAA while applying the appropriate Missouri procedure. "States may apply their own neutral procedural rules to federal claims, unless the rules are pre-empted by federal law." *Howlett v. Rose*, 496 U.S. 356, 372 (1990). For the reasons below, there is no such preemption here because the neutral MUAA procedures at issue are fully consistent with the FAA.

As a threshold matter, we note that reverse *Erie* analysis – that is, an argument that federal procedure should displace state rules – is guided by the principle that the *lex fori* (the "law of the forum") governs procedure. This principle recognizes the "importance of state control of state judicial procedure" and the basic fact "that federal law takes the state courts as it finds them." *Id.* (citations and quotations omitted). Missouri has "great latitude to establish the structure and jurisdiction of [its] own courts," *id.*, and any argument that FAA § 4 supersedes section 435.355.1 would face a high federalism hurdle.

State law can be preempted under the Supremacy Clause in three circumstances. Although these circumstances are commonly analyzed separately, each reflects that "the purpose of Congress is the ultimate touchstone of pre-emption analysis." *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 516 (1992) (quotation omitted).

First, Congress can define explicitly the extent to which an enactment such as the FAA preempts state law. *See, e.g., Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 299 (1988). The FAA "contains no express pre-emptive provision." *Volt Info. Sciences, Inc. v. Stanford Univ.*, 489 U.S. 468, 477 (1989).

Second, "[i]n the absence of explicit statutory language . . . Congress implicitly may indicate an intent to occupy a given field to the exclusion of state law." *Schneidewind*, 485 U.S. at 299. Such intent must be "clear and manifest" to supersede an area of law "traditionally occupied by the States." *English v. Gen. Elec. Co.*, 496 U.S. 72, 79 (1990) (quoting *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977)).

In *Volt*, the U.S. Supreme Court clarified that the FAA does *not* "reflect a congressional intent to occupy the entire field of arbitration." 489 U.S. at 477. To the contrary, "[t]here is no federal policy favoring arbitration under a certain set of procedural rules; the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate." *Id.* at 476.

The literal terms of FAA § 4 – the specific federal provision raised by Respondents – reflect that state authority over arbitration has not been displaced entirely. The section, for instance, addresses the "Federal Rules of Civil Procedure," which clearly do not control Missouri state actions. "By its literal language, § 4 is applicable only to United States District Courts." *United Nuclear Corp. v. Gen. Atomic Co.*, 597 P.2d 290, 308 (N.M. 1979). Indeed, the Supreme Court of New Mexico "found no authority which indicates that a party may petition a state court for an order to compel arbitration under § 4 of the Federal Arbitration Act." *Id.* (citation omitted).[10]

[10] Since *United Nuclear Corp.*, a few state courts have applied FAA § 4's procedures in state-filed actions. Most of these decisions are short and assume, without analysis, that FAA § 4 applies. *See, e.g.*, *England v. Dean Witter Reynolds*, 811 S.W.2d 313, 314 (Ark.

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As noted above, the U.S. Supreme Court in *Southland* expressed doubt that the mechanisms of FAA § 4 apply in state court. Similarly, the *Volt* Court found "some merit" in the argument that FAA §§ 3 and 4 do not apply to state proceedings and noted, *inter alia*, that the Court had "***never held*** that §§ 3 and 4, which by their terms appear to apply only to proceedings in federal court . . . are nonetheless applicable in state court." 489 U.S. at 477 & n.6 (citations omitted) (emphasis added).

In *Dunn Indus. Group, Inc. v. City of Sugar Creek*, 112 S.W.3d 421, 433 (Mo. banc 2003), this Court cited *Volt* while "also find[ing] it unnecessary to resolve" whether FAA § 3 provides a party in a state proceeding with a right of appeal from an order denying a motion to stay litigation pending arbitration. Nonetheless, we note that the Court ordered that "[o]n remand, the trial court will comply with all relevant statutory provisions, ***including section 435.355.4.***" *Id.* (emphasis added).[11]

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1991) (fewer than two full pages). Most importantly, these decisions do not rest on the notion that federal procedures would result in a different substantive outcome in those cases. *See, e.g., id.* at 315 ("Substantively, the lower court made the correct decision.").

[11] In a July 5, 2005 opinion, the Court of Appeals held that it had jurisdiction under section 435.440.1 and cited *Dunn* and *Volt* while noting "we need not determine whether Sections 3 and 4 [of the FAA] are applicable to a circuit court in this State." *Whitney v. Alltel Comm., Inc.*, No. WD64196, 2005 Mo. App. LEXIS 1016, at *6-7 (Mo. App. W.D. July 5, 2005).

Third, it is well established that state law is preempted to the extent that it actually conflicts with federal law. Thus, as this Court has explained, "[a]ny requirement of state law which adds a burden not imposed by Congress [under the FAA] is in derogation of the Congressional power." *Bunge Corp. v. Perryville Feed & Produce, Inc.*, 685 S.W.2d 837, 838 (Mo. banc 1985).

Section 435.355.1 is therefore preempted only if its procedures "defeat the rights granted by Congress" under the FAA, *Strain-Japan R-16 Sch. Dist. v. Landmark Sys.*, 51 S.W.3d 916, 920 (Mo. App. E.D. 2001), or otherwise "stand[] as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Volt*, 489 U.S. at 477 (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)).

No such tension is present here. The MUAA procedural rule providing for a bench determination of an equitable remedy clearly does not undermine the intent of Congress in enacting the FAA "to overrule the judiciary's longstanding refusal to enforce agreements to arbitrate." *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 219-20 (1985).

Nor does this state procedure run afoul of the congressional intent "to place an arbitration agreement upon the same footing as other contracts, where it belongs." *Id.* (quoting omitted). As discussed above, Section 435.355.1 simply applies longstanding equitable procedures to an application for specific performance. Thus, the "same footing" requirement would be violated only if the MUAA provided for a jury to sit in equity.

Federalism aside, and even if Missouri procedure were not applied here, under FAA § 4 (which itself provides that "the court shall proceed summarily to the trial thereof"), "[a] party resisting arbitration cannot obtain a jury trial merely by demanding one." *Doctor's Assocs., Inc. v. Stuart*, 85 F.3d 975, 983 (2d Cir. 1996). FAA § 4 "requires a trial on the question of the existence of an agreement to arbitrate only if there is a genuine factual issue as to the existence of a contract." *In re McDonald's Corp. Promotional Game Litig.*, No. 02 C 1345 (MDL No. 1437), 2004 U.S. Dist. LEXIS 4471, at *6 (N.D. Ill. Mar. 22, 2004). As demonstrated throughout this brief, that is a showing that Respondents are simply unable to make.

In fact, without its summary procedures, the MUAA would raise a constitutional red flag because a "full trial" requirement for every motion to compel arbitration would undermine the policy of the FAA by, in effect, imposing exorbitant arbitration fees in the form of litigation costs. *Cf. Mendez v. Palm Harbor Homes, Inc.*, 45 P.3d 594, 607 (Wash. Ct. App. 2002) ("If the up front costs of arbitration have the practical effect of deterring a consumer's claim, the arbitration agreement should not be enforced.").

"The function of arbitration is to be a speedy, efficient and less expensive alternative to court litigation, which is a cornerstone of both the federal and state acts." *In re Estate of Sandefur*, 898 S.W.2d 667, 669-70 (Mo. App. W.D. 1995). Because section 435.355.1 furthers these objectives, its summary nature, alone, does not violate the supremacy clause. *See, e.g., Jack B. Anglin Co.*, 842 S.W.2d at 269 (approving summary bench procedure because, *inter alia*, "the main benefits of arbitration lie in expedited and less expensive disposition of a dispute").

In the end, then, the case for preemption under FAA § 4 must rest on the slender reed that having Missouri judges determine arbitrability is unconstitutional. But this argument itself has been rejected summarily. *See, e.g.*, *Rogers*, 2005 Okla. LEXIS 49, at *12 (finding that bench determination of a motion to compel arbitration "does not frustrate the purposes underlying the FAA"). The California Supreme Court, for instance, unanimously held that summary adjudication is an acceptable state method:

> [T]he summary procedure provided, in which the existence and validity of the arbitration agreement is decided by the court in the manner of a motion, is designed to further the use of private arbitration as a means of resolving disputes more quickly and less expensively than through litigation. Finally, having a court, instead of a jury, decide whether an arbitration agreement exists will not frequently and predictably produce different outcomes.

Rosenthal, 926 P.2d at 1069-70 (citations and footnote omitted). Indeed, having lay juries making such an essentially equitable determination would be contrary to longstanding law and undermine the coherent development of arbitration, thus frustrating the strong federal policy in favor of arbitration.

There is no reason for this Court to reach a contrary conclusion from the supreme courts of California and Oklahoma. The MUAA – like the laws in California and

Oklahoma – is adopted from the UAA.[12] In this regard, the preemption analysis benefits from the extensive work done by the NCCUSL in preparing the RUAA. The reporter to the drafting committee – and the late dean of the University of Missouri School of Law – observed that the NCCUSL gave particular attention to preemption concerns: "[T]he strong policy of federal preemption under the FAA acted as a backdrop to all the discussions of the Drafting Committee while it deliberated the RUAA." Timothy J. Heinsz, *The Revised Uniform Arbitration Act: Modernizing, Revising, and Clarifying Arbitration Law,* J. Disp. Resol. 1, 5 (2001). Therefore, "[t]o avoid federal preemption problems for the RUAA, the Drafting Committee worked diligently to write provisions consistent with the FAA's pro-arbitration policy and not to treat law regarding state arbitration statutes different from the general state law of contracts." *Id.* (footnote omitted).

In light of this preemption "backdrop," it is telling that (as discussed above) the UAA/MUAA provisions at issue here emerged from the recent revision process substantively unchanged. RUAA § 7(a)(2), UAA § 2(a) *and* section 435.355.1 all provide that a "court shall proceed summarily to decide the issue . . . ." Not only did the NCCUSL find no need to alter this language, the drafting committee was comfortable

[12] By contrast, one of the few MUAA provisions not found anywhere in the UAA – section 435.460's notice of arbitration requirement – has been held by this Court to be inapplicable to a contract within coverage of the FAA because its inclusion conflicts with federal policy favoring arbitration. *See Bunge*, 685 S.W.2d at 838-39.

adding the Official Comment quoted in full above that "[t]he term 'summarily' . . . has been defined to mean that ***a trial court should act expeditiously and without a jury trial*** to determine whether a valid arbitration agreement exists." (Emphasis added.)

3. The only procedural question presented is when should a bench evidentiary hearing be held on a motion to compel arbitration

As noted above, section 435.425 (UAA § 16) specifically provides that an application under the MUAA is to be heard in the same manner and on the same notice as a motion in a civil case. *See Doyle v. Thomas*, 109 S.W.3d 215, 219 (Mo. App. E.D. 2003). These motion practices, of course, are codified in Rule 55. *Cf. St. Luke's Hosp. v. Midwest Mech. Contractors, Inc.*, 681 S.W.2d 482, 487 (Mo. App. W.D. 1984) (describing how the MUAA provides for a court to "entertain an application" to stay arbitration and "[u]pon a showing that there exists such an agreement, the court merely denies the application for the stay of arbitration proceedings").

The only question under these procedures is when, or if, an evidentiary hearing should be held by a Missouri court deciding a motion to compel arbitration. Although other jurisdictions have reached various conclusions, their general tenor was set four decades ago when the Second Circuit held in a widely cited case that the FAA is intended "to expedite judicial treatment of matters pertaining to arbitration." *World Brilliance Corp. v. Bethlehem Steel Co.*, 342 F.2d 362, 365 (2d Cir. 1965). Therefore:

> ***Motions [under FAA § 6] may be decided wholly on the papers, and usually are, rather than after oral examination and cross-examination of witnesses. . . .*** A district court may,

> in its own discretion, order a trial-like hearing . . . but under the Federal Arbitration Act it is not an abuse of discretion for a district court, as here, to decline to do so.

Id. at 365-66 (emphasis added).

Generally speaking, state decisions approaching this issue under the UAA have taken two approaches. Some cases find that a trial court does not abuse its discretion by resolving evidentiary conflicts as to the making of an arbitration agreement without a hearing. *See, e.g., United Nuclear Corp.*, 597 P.2d at 308; *Rosenthal*, 926 P.2d at 1069-70. Other courts hold that an evidentiary hearing should be held if a court finds a genuine issue of material fact. *See, e.g., Jack B. Anglin Co.*, 842 S.W.2d at 269; *Haynes v. Kuder*, 591 A.2d 1286, 1290 (D.C. App. 1991).

The recent decision by the Supreme Court of Oklahoma suggests a guideline, holding: "The decision to grant a hearing will be in the discretion of the district court. However, if the existence of an agreement to arbitrate is controverted, then the better procedure is for the district court to conduct an evidentiary hearing." *Rogers*, 2005 Okla. LEXIS 49, at *14 (citations omitted). "In making its decision, the district court should be mindful of the FAA's policies favoring arbitration; ambiguity falls on the side of the existence of an agreement to arbitrate." *Id.*

Significantly, under none of these approaches is there a right to a jury trial, and under established Missouri motions practice the decision to conduct an evidentiary hearing is within the sound discretion of the Circuit Court.

4. In any event, the same result occurs in this case under the FAA or MUAA procedures

In the final analysis, the outcome of this case would not be different even if this Court were to apply the procedures of FAA § 4 or conclude that a party is entitled to an evidentiary hearing under the MUAA.[13] *Compare Topf v. Warnaco, Inc.*, 942 F. Supp. 762, 766-67 (D. Conn. 1996) ("A party moving for a jury trial under § 4 must show the existence of a genuine issue involving the making of the arbitration agreement.") *with Ameristar Jet Charter, Inc. v. Dodson Int'l Parts, Inc.*, 155 S.W.3d 50, 58 (Mo. banc 2005) ("Summary judgment is only proper [under Missouri law] if there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law.").

As discussed above, the parties were given ample opportunity below to conduct discovery, and they created an ample record, including extensive affidavits, numerous business records and other documentary evidence. Extensive briefing and several hours of oral argument were then conducted. As demonstrated in detail above, this well-developed record shows that Respondents cannot show a *genuine* issue of *material* fact as to the making of the Amway and Pro Net arbitration agreements. No credibility determinations are needed to hold that Netco and Schmitz Associates are bound to

[13] In *Haynes*, the D.C. Court of Appeals concluded that the question of "whether a jury trial is available under the District of Columbia Uniform Arbitration Act on the issue of existence of an agreement to arbitrate" had been "moot[ed]" by its holding that "the trial judge correctly granted what amounts to summary judgment." 591 A.2d at 1290 n.7.

arbitrate under the Amway Rules and the Pro Net Terms and Conditions, and that they are estopped from arguing otherwise. Respondents' own pleadings and admissions, the annual Amway distributorship renewals, the signed Pro Net application, and the undisputed business records show that there are no genuine questions of material fact as to the making of these arbitration agreements. As a result, there is no need for either an evidentiary hearing (under the MUAA) or a jury trial (under the FAA).

C. The Amway Rules of Conduct require arbitration of Respondents' dispute with Appellants

On review, this Court should reverse the decision of the Circuit Court below and order arbitration under both the Amway Rules of Conduct and the Pro Net Terms and Conditions.

Under the FAA and the Missouri Act, this Court should "engage in a limited inquiry to determine [1] whether a valid agreement to arbitrate exists between the parties and [2] whether the specific dispute falls within the scope of that agreement." *Houlihan v. Offermant & Co.*, 31 F.3d 692, 694-95 (8th Cir. 1994); *see also Village of Cairo v. Bodine Contracting Co.*, 685 S.W.2d 253, 258 (Mo. App. W.D. 1985) (under Missouri and federal law, "[i]f the court finds agreement to arbitrate, and that the dispute is encompassed, the court must order arbitration"); *accord Gannon v. Circuit City Stores*, 262 F.3d 677, 681 (8th Cir. 2001); *Telectronics Pacing Sys., Inc. v. Guidant Corp.*, 143 F.3d 428, 433 (8th Cir. 1998). To the extent Respondents have defenses to arbitration, procedural objections to the arbitrations, or other matters that do not relate strictly to

these two "gateway issues" of arbitrability, they should be reserved for the arbitrator. *See Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 84 (2002).

In addressing these two, highly limited questions, the Court should recognize that "[t]he federal policy favoring arbitration requires [courts] to construe arbitration clauses as broadly as possible," and that "[a]mbiguities as to the scope of the arbitration are resolved in favor of arbitration." *Fru-Con Constr. Co. v. Southwestern Redev. Corp II.*, 908 S.W.2d 741, 744 (Mo. App. E.D. 1995) (quotation omitted). Indeed, the Supreme Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24-25 (1983), held that, under the FAA, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability."

Where, as here, there is an agreement to arbitrate, and the dispute at issue is within the scope of the agreement, defenses to arbitration, such as issues regarding confidentiality, selection and retention of arbitrators, or even if there were, unlike here, limitations on damages, are for the arbitrator; they need not and should not be addressed by the court. *See Hawkins v. Aid Ass'n for Lutherans*, 338 F.3d 801, 807 (7th Cir. 2003) (multiple claims of unconscionability in arbitration agreement did not go to the existence or scope of the agreement, and thus were for the arbitrator to decide), *cert. denied*, 540 U.S. 1149 (2004); *Bob Schultz Motors, Inc. v. Kawasaki Motors Corp., U.S.A.*, 334 F.3d 721, 726 (8th Cir. 2003) ("If the parties have agreed to arbitration, the [Federal Arbitration] Act requires that a district court order them to proceed to that forum, where

they must address all other claims to the arbitrator"), *cert. denied*, 540 U.S. 1149 (2004). *See generally Howsam*, 537 U.S. at 84 ("The presumption is that the arbitrator should decide allegation[s] of waiver, delay, or a like defense to arbitrability.") (quote omitted).

In the litigation below, there was an enormous amount of effort expended in discussing whether the standard arbitration agreements at issue should be avoided because of allegations of unconscionability and other alleged defenses to arbitrability. In fact, under the law of this federal circuit, "a court compelling arbitration should decide only such issues as are essential to defining the nature of the forum in which a dispute will be decided." *Larry's United Super, Inc. v. Werries*, 253 F.3d 1083, 1085 (8th Cir. 2001) (quoting *Great W. Mortgage. Corp. v. Peacock*, 110 F.3d 222, 230 (3d Cir. 1997)).

In *Larry's United*, the Eighth Circuit clarified that claims that an arbitration agreement involve a waiver of federal or state substantive rights should not be addressed by a court prior to the arbitration, but rather such claims raise issues that "may be raised when challenging an arbitrator's award." *Id.* at 1086. Accordingly, "[o]nce a dispute is determined to be validly arbitrable, all other issues are to be decided at arbitration." *Id.* (quoting *Peacock*, 110 F.3d at 230).

Proper narrow and limited review of the arbitration agreements contained in the Amway Rules of Conduct and in the Pro Net Terms and Conditions, furthers the "public policy of actively enforcing private arbitration agreements under both the Federal and Missouri arbitration acts so that disputes might be resolved without resort to the courts." *Greenwood v. Sherfield*, 895 S.W.2d 169, 173 (Mo. App. S.D. 1995). Indeed, in reviewing both arbitration agreements, "there is a presumption of arbitrability in the

sense that 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." *AT&T Techs., Inc. v. Communications Workers of Am.*, 475 U.S. 643, 650 (1986) (quotation omitted). Respondents, as the parties seeking to avoid arbitration, bear the burden of proof to make such a showing. *State ex rel. PaineWebber v. Voorhees*, 891 S.W.2d 126, 128 (Mo. banc 1995). They cannot do so here.

Under the standards set forth above, the Court should conclude that both the Amway Rules of Conduct and the Pro Net Terms and Conditions contain valid arbitration clauses, and that Respondents' claims are within the scope of both agreements. Accordingly, the Court should reverse with instructions that the Circuit Court "must send the case for arbitration, without reaching any issue concerning the merits of the underlying grievance." *Local 781 v. City of Independence*, 996 S.W.2d 112, 115 (Mo. App. W.D. 1999).

D. Netco, an Amway distributor, is bound by its agreement to arbitrate disputes relating to the Rules of Conduct

Netco, as an Amway distributor, agreed to abide by Amway's Rules of Conduct as amended from time to time. (A0062-63.) Amway distributors must renew their distributorships each year and agree to be bound by the Rules of Conduct as they exist at the time. (A0063.) Beginning in 1985, Charlie Schmitz began renewing his Amway distributorship annually, as required, through the "auto-renewal" process. (A0106.) This process continued when the distributorship was assigned to Netco. (A0065; A0067.)

Since 1998, Amway's Rules of Conduct have provided for binding arbitration of disputes among distributors and their organizations. (A0063-64.) If conciliation efforts fail, the dispute is required to be submitted to binding arbitration. Specifically, Amway distributors and their organizations agree:

> to submit any remaining claim(s) arising out of or relating to their Amway Distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct (including any claim against another Amway distributor, or any such distributor's officers, directors, agents, or employees or against Amway Corporation, or any of its officers, directors, agents, or employees) to binding arbitration in accordance with the Amway/ADA Arbitration Rules.

(A1268; *see also* A1338-39.)

Accordingly, any Amway distributor that renewed its distributorship in any manner for 1998 and thereafter was bound by the arbitration provisions in the Amway Rules of Conduct. (A0063-64.)

The Amway renewal process was discussed at length in *Morrison v. Amway Corp.*, 49 F. Supp. 2d 529 (S.D. Tex. 1998). In that case, a group of Amway distributors sued Amway and other distributors over issues relating to BSMs. The court found that distributors who used the "auto renew" process were bound by the Rules of Conduct, including the arbitration provision. *Id.* at 533-34.

The Respondents previously have suggested that Netco's distributorship was not auto-renewed – despite the fact that Netco remained an Amway distributor until July 1999 – because the Schmitzes apparently never submitted an auto-renewal form in the name of Netco. Mr. Schmitz, however, testified that he fully understood the renewal requirement, and that the auto-renewal process continued without objection as to Netco after he incorporated the distributorship. (A3071; A3075-76.) As assignee, Netco assumed the obligations of the Schmitz distributorship - including the ongoing obligation to abide by the Amway Rules, as changed from time to time. "Missouri law is well-settled that an assignee acquires no greater rights than the assignor had at the time of the assignment." *Citibank (South Dakota), N.A. v. Mincks*, 135 S.W.3d 545, 556 (Mo. App. S.D. 2004) (quoting *Carlund Corp. v. Crown Center Redev.*, 849 S.W.2d 647, 650 (Mo. App. W.D. 1993). Thus, Netco "stands in [Mr. Schmitz'] shoes, and can occupy no better position." *Id.* at 557.

Netco simply cannot dispute that, after being informed of the inclusion of the binding arbitration provision in the Amway Rules of Conduct, it renewed its distributorship with Amway. (A0065.) In fact, Netco renewed its distributorship with Amway after repeatedly being informed about Amway's arbitration provisions. (*Id.*; A3075-76.) Consequently, Netco has consented to the broad arbitration provisions contained in the Amway Rules of Conduct.[14]

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[14] Respondents also cannot be excused from the Amway Arbitration Agreement by claiming that they were not aware of the agreement. One who assents to a contract is

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Moreover, Netco clearly accepted the benefits of being an Amway distributor for many years, including in 1998 and 1999, when the Amway Arbitration Agreement was in force. Indeed, according to Mr. Schmitz, the Schmitz Organization made "hundreds of thousands of dollars" per year, qualifying for the prestigious Diamond level "every single month." (A3094.) And, when Netco and the Schmitzes had complaints about other distributors, they invoked the Rules of Conduct in demanding relief from Amway. (A2830-33.)

In filing this action, Netco and the Schmitzes are now attempting to pick and choose what provisions of the Rules of Conduct they like, and which ones they do not. The fact is they operated their Amway distributorship for more than 14 years, and they benefited financially from this arrangement. They cannot accept the benefits of this contractual relationship with Amway and its distributors, and walk away from contractual obligations they would prefer not to meet. A fundamental rule of contracts is that "[a] party cannot affirm a contract in part, and repudiate it in part. He cannot accept its benefits on the one hand, while he shirks its disadvantages on the other. He cannot play

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presumed to be aware of its contents and accepted its terms. *Warren Supply Co. v. Lyle's Plumbing, LLC*, 74 S.W.3d 816, 819 (Mo. App. W.D. 2002). That the term of the contract is an arbitration agreement does not compel a different result. *See Curtis v. Newhard, Cook & Co.*, 725 F. Supp. 1072, 1075 (E.D. Mo. 1989) (arbitration agreement enforced over objection of party claiming to be unaware of it).

fast and loose in the matter." *Schurtz v. Cushing*, 146 S.W.2d 591, 594 (Mo. 1941); *see also In re Marriage of Carter*, 862 S.W.2d 461, 468 (Mo. App. S.D. 1993) ("[A] party will not be allowed to assume the inconsistent position of affirming a contract in part by accepting or claiming its benefits**,** and disaffirming it in part by repudiating or avoiding its obligations or burdens."). Netco and the Schmitzes cannot renounce their promise to arbitrate merely because the promise now seems inconvenient. They are bound to arbitrate under the Amway Rules of Conduct.

E. Schmitz Associates is also bound by the Amway Arbitration Agreement

Respondent Schmitz Associates is not itself a signatory to the Amway Rules of Conduct, but is equally bound by the agreement to arbitrate disputes with Appellants for three related reasons. First, Schmitz Associates is a third-party beneficiary of Netco's Amway distributorship. Second, having benefited from Netco's Amway distributorship, Schmitz Associates is equitably estopped from arguing that it is not bound by the arbitration agreement in the Rules of Conduct. Third, Schmitz Associates acted as an agent of Charlie and Kim Schmitz, its principals, by acting "in tandem with" Netco and by facilitating "the Amway-related rally, convention and function business for Charlie and Kim Schmitz" (A0004). It is bound to the arbitration agreement in the Amway Rules of Conduct under general rules of agency.

1. Schmitz Associates is a third-party beneficiary of Netco's Amway distributorship

Respondents' Petition is replete with statements that show how Schmitz Associates benefited from Netco's Amway distributorship. Schmitz Associates admits that it "facilitated the Amway-related rally, convention and function business for Charlie and Kim Schmitz (Netco) and operated in tandem with Netco to build, support and enhance the Amway business." (A0004.) The BSMs business in which Schmitz Associates engaged was "inextricably connected to Amway." (A0016.) Indeed, Respondents assert that the income that a "Diamond Amway distributor can potentially derive from the BSMs industry is vastly superior to that income that can be derived from the sale of Amway products alone," and that "Schmitz Associates utilized Netco's downline network in sponsoring, organizing and holding these major functions, which regularly drew over 2000 Amway distributors in attendance." (A0016; A0020.) Schmitz Associates therefore was dependent upon and "inextricably connected" with Netco's Amway distributorship.

In an even more basic sense, Schmitz Associates relied on Netco's relationship with Amway to sell BSMs. It states that "Beginning in 1993, Netco and Schmitz Associates began conducting their own major functions with the consent of Netco's upline, including Appellants Childers, Gooch, Evans and Dunn." (A0020.) In doing so, they relied directly on "the Amway Rules of Conduct for distributors, which require recognition of and adherence to the lines of [Amway] sponsorship." (A0014; emphasis omitted.) Moreover, as "only Diamond distributors were allowed to sponsor major

functions," (*id*.), Schmitz Associates would not have been able to engage in the BSMs business at all but for its reliance on Netco's Amway distributorship. In plain terms, and in Respondents' words: "Any Diamond or Emerald distributor's downline network had intrinsic value to that distributor as a participant within the BSMs industry. A Diamond distributor [such as Netco], having the right to organize and run their [sic] own major function, had the opportunity to garner significant profits from these major functions." (*Id*.) Schmitz Associates even claims that the "rules governing the tool and function business became known and understood by participants within the Amway network" to the extent that "this long-standing course of dealing for all participants in the BSMs industry constituted an implied in fact contract." (A0015; emphasis omitted.) Indeed, Respondents allege that they created "a massive downline organization numbering approximately 8000 Amway distributors," and their "networks of downline distributors served as lucrative markets for the sale of Amway products and Amway-related motivational materials." (A0018; A0011.) Schmitz Associates even blames its failure on Pro Net's alleged "failure or refusal to respect the lines of sponsorship," which it claims "is contrary to Amway's Rules of Conduct pertaining to BSMs." (A0022.)

Given Schmitz Associates' repeated claims that it relied on and profited from Netco's Amway relationship, a relationship predicated on the Amway Rules of Conduct and Netco's status as an Amway distributor, there can be no doubt but that Schmitz Associates is indeed a third-party beneficiary of Netco's distributorship. Any lingering doubt is resolved by Respondents' claim that the alleged "damage to Netco's downline" was reflected in a "profound decline in attendance at Netco and Schmitz Associates'

functions beginning in 1996," and eventually resulted in a decision by Respondents to "cease[] their efforts to sponsor major functions." (A0028; A0029.) In sum, Respondents admit over and over that their successes relied principally on retaining a downline of Amway distributors – something that can be accomplished only through an Amway distributorship. Schmitz Associates, as a beneficiary of Netco's Amway distributorship contract, has even made claims against Appellants under the Amway Rules of Conduct. As a third-party beneficiary of the Rules, Schmitz Associates is required to arbitrate its claims.

It is well established that a third-party beneficiary of an agreement is bound to arbitrate under that agreement. Schmitz Associates cannot "claim a right to maintain an action based on [its] status" as a member of the Schmitz Organization of Amway-related businesses selling to Netco's downline of Amway distributors, "and, at the same time, disavow this relationship for the purposes of arbitration." *Tractor-Trailer Supply Co. v. NCR Corp.*, 873 S.W.2d 627, 631 (Mo. App. E.D. 1994); *see also Foster v. Sears Roebuck & Co.*, 837 F. Supp. 1006, 1008 (W.D. Mo. 1993) ("a party cannot have it both ways; it cannot rely on the contract when it works to its advantage and then repute it when it works to its disadvantage") (quoting *A.L. Williams & Assoc. v. McMahon*, 697 F. Supp. 488, 494 (N.D. Ga. 1988)).

2. Schmitz Associates is equitably estopped from arguing that it is not bound to arbitrate under the Amway Rules of Conduct

Schmitz Associates is also equitably estopped from arguing that it is not bound by the arbitration agreement contained in the Amway Rules. Schmitz Associates cannot

assert rights under an agreement but disavow the obligations that the agreement imposes. *See, e.g.*, *Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.*, 10 F.3d 753, 757-58 (11th Cir. 1993); *Hughes Masonry Co. v. Greater Clark County Sch. Bldg. Corp.*, 659 F.2d 836, 838-39 (7th Cir. 1981); *see also Ex parte Lovejoy*, 790 So. 2d 933, 937 (Ala. 2000) (equitable estoppel applies "where the plaintiff alleges conspiracy or agency between a non-signatory and a signatory to a contract containing an arbitration clause"). Accordingly, Schmitz Associates is bound by the arbitration agreement in the Amway Rules.

3. Schmitz Associates is bound as an agent of the Schmitzes

Schmitz Associates is also bound under the Amway Arbitration Agreement as an agent of Charlie and Kim Schmitz. Under Missouri law, "non-signatory agents [are] bound by arbitration agreements signed by their principals." *Byrd v. Sprint Communications Co., L.P.*, 931 S.W.2d 810, 815 (Mo. App. W.D. 1996); *Nesslage v. York Sec., Inc.*, 823 F.2d 231 (8th Cir. 1987).

A principal-agent relationship has three elements: (1) the agent must hold the power to alter legal relations between the principal and third parties, (2) the agent must be a fiduciary with respect to matters within the scope of its agency, and (3) the principal must have the right to control the conduct of the agent with respect to matters with which it is entrusted. *See Byrd*, 931 S.W.2d at 815. Respondents' description of the Schmitz Organization demonstrates that the Schmitzes have created a principal-agent relationship with Schmitz Associates.

Schmitz Associates had the power to alter legal relationships on behalf of the Schmitzes. The Petition explains in detail how Schmitz Associates developed and operated the tool and function business for the Schmitz Organization, selling BSMs to Netco's enormous downline of Amway distributors. As such, Schmitz Associates necessarily has the authority to enter into obligations and obtain benefits for the entire Schmitz Organization, including the Schmitzes.

Second, Schmitz Associates is a fiduciary of the Schmitzes. A fiduciary is "one who has a duty, created by his own undertaking, to act primarily for another's benefit in matters connected with such an undertaking." *Farmers Ins. Co. v. McCarthy*, 871 S.W.2d 82, 86-87 (Mo. App. E.D. 1994). The very purpose of Schmitz Associates' existence was to "facilitate[] the Amway-related rally, convention and function business for Charlie and Kim Schmitz (Netco)." (A0004.) As such, Schmitz Associates is a fiduciary of the Schmitzes.

Third, Charlie and Kim Schmitz control Schmitz Associates through their sole ownership. Schmitz Associates existed primarily on paper – it had no employees but paid a fee to the Schmitz's Amway distributorship for conducting its operations, and shared its officers, office space, stationary, telephone and fax numbers, and its email address. (A3032; A3067-68.) Throughout its existence, and until the 1999 sale of the Schmitz's Amway-related businesses (i.e. the Amway distributorship and the Amway-related BSMs businesses) Schmitz Associates catered to Schmitz's downline Amway organization. As Charlie and Kim Schmitz had the ability to choose their downline Amway distributors, they chose the parties with whom Schmitz Associates would deal.

Moreover, when Charlie and Kim Schmitz left the Amway business, Schmitz Associates ceased to conduct functions and sell BSMs, an action that illustrates their complete control over it.

F. All Appellants are entitled to compel arbitration under the Amway Rules of Conduct

All Appellants are entitled to compel arbitration against Respondents under the Amway Rules of Conduct. The Amway Arbitration Agreement, in addition to covering any "claim(s) arising out of or relating to [Respondents'] Amway distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct," also specifically covers "any claim against another Amway distributor, or any such distributor's officers, directors, agents, or employees." (A1268.) It is undisputed that nine of the eleven named Appellants are either Amway distributors, officers of Amway distributors, or agents of Amway distributors, and thus are directly within the scope of the Amway Arbitration Agreement.[15]

The two remaining Appellants, Pro Net and Global Support Services, are entitled to compel arbitration of Respondents' disputes because they arise out of or relate to Respondents' Amway Distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct, and also because Pro Net and Global Support Services, Inc.

[15] These Appellants are Jimmy V. Dunn; Jimmy V. Dunn & Associates, Inc.; Harold Gooch, Jr.; Gooch Support Systems, Inc.; Gooch Enterprises, Inc.; Billy S. Childers; TNT, Inc. of Charlotte, N.C.; Jim Evans, and J.L. Evans & Associates, Inc.

are admitted to be intimately involved in Respondents' Amway-related claims and disputes alleged in this case. For example, Respondents allege Pro Net founders Appellants Hal Gooch (who was the Pro Net Chief Executive Officer) and Billy Childers (who was Pro Net's President), both of whom are principals of their respective Amway distributorships, acted in concert with Pro Net, Global Support, and others to monopolize BSM sales within the "Gooch Network" and deprive Respondents of their Amway-related BSMs business. (A0609-12.) Respondents specifically allege that these actions violated the Amway Rules of Conduct. (A2830.)

Moreover, other Appellants, including Jimmy V. Dunn, Jimmy V. Dunn & Associates, Inc.; Gooch Support Systems, Inc.; Gooch Enterprises, Inc. and TNT, Inc. are also Pro Net members. (A2131; A2324; A2667; A2313; A2089; A2663.) This Pro Net connection underscores that Respondents' claims fall within the Amway Rules of Conduct. As part of the Pro Net Terms and Conditions, Pro Net members agree "to adhere to the Amway Corporation's Code of Ethics and Rules of Conduct." (A2140.) As the Circuit Court of Florida recently found in *U-Can-II*, addressing these same Pro Net Terms and Conditions, "Paragraph 3 of the Pro Net Terms specifically provide[s] that "Member agrees to adhere to the Amway Corporation's Code of Ethics and Rules of Conduct for Distributors . . . By agreeing to comply with the Amway Rules, [a Pro Net member] contractually assumed the duty to arbitrate provided in those Rules." (A3846 (finding that Pro Net members must arbitrate under the Amway Rules as well as the Pro Net arbitration provisions).)

Respondents essentially admit that their claims are within the ambit of the Amway Rules of Conduct. Netco and Schmitz Associates President Charlie Schmitz, who in the name of "Netco, Inc. (Charlie and Kim Schmitz)," became a member of Pro Net (A2091; A2136), and bought thousands of tapes, literature, books and other BSMs from Global Support through their Pro Net membership. (A2517; A2520.) When a dispute arose, both Respondents invoked the Amway Rules of Conduct, claiming that "Amway Rule 4.14 governs the sale of privately-produced BSMs." (A2830.)

The Florida Circuit Court in *U-Can-II* (A3833-51), which carefully addressed the scope of the Amway Rules, including identical arguments involving nearly identical claims brought by another Amway distributor by Respondents' counsel against many of the Appellants in this action, reached the same conclusion:

> Plaintiffs' argument that BSMs are not governed by the Amway Rules of Conduct . . . is disproven by the language of Amway Rule 4.14, which governs the sale of non-Amway products, specifically including BSMs. Further, the language of the Amway Rules is a "broad form" arbitration agreement . . . in which <u>only the most forceful evidence</u> of the purpose to exclude a claim from arbitration can prevail.

(A3846; citations and quotations omitted; emphasis in original.)

Global Support, an order fulfillment company, likewise is also alleged to be intimately involved in Respondents' claims, and was sued because of its relationship with

Pro Net. Respondents allege that Global Support "worked in tandem with Pro Net," and conspired with Pro Net and the other Appellants. (A0554-55.) Moreover, Global Support is alleged to have a direct relationship with Netco's Amway-related BSMs business, in that Netco ordered BSMs from Global Support, pursuant to Global Support's order fulfillment contract with Pro Net (A2516), and Global Support ultimately shipped more than 100,000 tapes and other BSMs to Netco. (A2517; A2520.) Moreover, Global Support offered for sale to other Pro Net members the tapes and speeches made by the Schmitzes. (A2517-18.)

There is yet another reason why these Appellants demand arbitration: All claims "arising out of or relating to [an] Amway Distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct" must be submitted to arbitration. (A1268.) There are no exceptions to that broad agreement for claims brought by a signatory. Where, as here, non-signatories, such as Appellants Pro Net and Global Support are third party beneficiaries of the arbitration agreement, they may compel arbitration of claims within the scope of the agreement. *See Pritzker v. Merrill Lynch*, 7 F.3d 1110, 1122 (3d Cir. 1993) (non-signatory may demand arbitration under an agreement if non-signatory's interests are "directly related to, if not predicated upon, [the signatory's] conduct"); *see also Spear, Leeds & Kellogg v. Cent. Life Assurance Co.*, 85 F.3d 21, 26 (2d Cir. 1996); *John Hancock Life Ins. v. Wilson*, 254 F.3d 48, 55 (2d Cir. 2001). To hold otherwise would permit plaintiffs, through skillful pleading, to circumvent arbitration requirements:

> [I]f [a plaintiff] can avoid the practical consequences of an agreement to arbitrate by naming nonsignatory parties as [defendants] in his complaint, or signatory parties in their individual capacities only, the effect of the rule requiring arbitration would, in effect, be nullified.

Arnold v. Arnold Corp., 920 F.2d 1269, 1281 (6th Cir. 1990) (citation omitted).

G. Respondents' disputes with Appellants are within the scope of the Arbitration Agreement in the Amway Rules of Conduct

The Court should conclude that Respondents' Petitions – all of which relate to the production and sale of Amway-related BSMs and functions – are within the scope of the arbitration agreement in the Amway Rules of Conduct, which encompasses "claim(s) arising out of or relating to their Amway Distributorship, the Amway Sales and Marketing Plan, or the Amway Rules of Conduct." (A1268; *see also* A1338-39.)

Respondents' claims against other Amway distributors and their organizations and Amway-related entities involve claims that Appellants circumvented the Amway "prescribed" lines of sponsorship, and directly implicate the Amway Rules of Conduct. For example, Rule 4.14 states that no distributor who "sells literature or sales aids not produced by the Corporation . . . will induce another [distributor] whom he has not personally registered to sell such products, literature, sales aids or services, nor shall he or she offer to sell such products, literature, sales aids or services to any [distributor] except those personally registered by him or her." (A1312.) Rule 7 of the Amway Rules

of Conduct, entitled "Business Support Materials," states that distributors "who choose to sell, purchase or utilize such BSM[s] must comply with this Rule," and also states that Amway can review BSMs "for the determination of compliance with its Rules of Conduct and business practices and policies." (A1327.)

Indeed, when Netco and Schmitz Associates first raised their claims against the Appellants in 1999, they submitted their complaint to Amway under the Amway Rules of Conduct. (A2827.) In response to telephone complaints made by Mr. Schmitz, a senior manager at Amway, Mr. Gary VanderVen, wrote Mr. Schmitz on September 17, 1999, and clarified that Amway's Rules "cover the solicitation for purchase of non-Amway produced products or services, limiting such solicitation to one's personally sponsored." (A2827; emphasis omitted.) Mr. VanderVen sent Mr. Schmitz an additional letter on September 28, 1999, again stating that the Amway Rules of Conduct preclude Amway distributors from soliciting distributors whom they have not personally sponsored. (A2845.)

On October 20, 1999, another Amway executive, Ron Mitchell, wrote another letter to Mr. Schmitz, quoting Rule 4.14 for the proposition that distributors "may not actively solicit the patronage of other [distributors] who are not personally registered by them," but concluding that "we have no evidence of a rule violation." (A2828.)

On May 16, 2000, Mr. Schmitz responded with an extensive letter to Amway. (A2830-33.) Specifically invoking the Amway Dispute Resolution Procedures set forth in Rule 11 (A1136), Mr. Schmitz complained of "interference by certain members of our upline with our downline regarding the sale of privately produced Business Support

Materials (BSMs), **in violation of Rule 4.14.**" (A2830; emphasis added.) Stating bluntly that "Rule 4.14 governs the sale of privately produced BSMs," Mr. Schmitz requested an immediate investigation "as well as enforcement of both the spirit and the letter of the Rules of Conduct and Code of Ethics." (A2830-31.)

Mr. Schmitz, citing Rule 4.1 more than 10 times, requested "that Amway take formal and immediate action against uplines Dunn, Evans, Childers and Gooch pursuant to Amway's authority under the Rules of Conduct." (A2832-33.) Amway's November 16, 2000 reply confirmed that Amway considers solicitation of non-personally sponsored distributors to be violations of the Rules of Conduct, but found no violation. (A2835.)

The Netco/Schmitz Associates letter shows clearly that Mr. Schmitz, Netco and Schmitz Associates and their counsel[16] all believed that the Amway Rules of Conduct controlled Appellants' claims. Furthermore, Amway, which promulgates and enforces the Rules of Conduct, has stated to Respondents several times that the claims in this action are subject to arbitration under the Rules of Conduct. On September 26, 2000, Amway wrote to former plaintiff Joanne Schmitz, reminding her that her Amway distributorship required her to "submit any unresolved claim or dispute arising out of . . . Amway's Rules of Conduct . . . including any claim against another Amway [distributor] . . . to binding arbitration," and that the lawsuit was "in direct contradiction of your contractual obligations." (A2840; emphasis omitted.) Likewise, on September 4, 2002, Amway wrote another letter stating that "the claims alleged by Netco, and by

[16] Mr. Schmitz "had legal review" of the May 16 Netco/Schmitz letter. (A3098.)

Charlie and Kim Schmitz on behalf of Netco, in the *Netco* lawsuit are subject to the conciliation and arbitration procedures of the [Amway] Rules of Conduct." (A2842.) Indeed, Amway reviewed the Motion to Compel Arbitration pending before the Circuit Court, and concluded that "the motion is well taken and this dispute is required to be arbitrated." (A2843.)

II. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration because the Trial Court erred as a matter of law in concluding that the Amway Arbitration Procedures were unconscionable, and erred as a matter of law in failing to recognize that allegedly unconscionable procedures should be severed from the Amway Rules of Conduct

A. Standard of Review

The trial court's denial of the motion to compel arbitration is reviewed *de novo*. *Dunn Indus. Group*, 112 S.W.3d at 428.

B. The Amway Rules of Conduct are not unconscionable and, in any event, any allegedly unconscionable arbitration procedures should have been severed from the Amway Rules of Conduct

1. The Trial Court erred in concluding that the Amway Arbitration Rules were unconscionable

Respondents raised a number of arguments below regarding arbitration under the Amway Rules, including that the arbitration provision is unconscionable or illusory or lacking in consideration. As demonstrated below, these arguments are without merit.

As a threshold matter, it should be noted that the doctrine of substantive unconscionability is not likely to be applicable where, as here, the plaintiffs are sophisticated parties. The *Morrison* court made a similar observation:

> Plaintiffs are not unsophisticated parties that were beguiled into entering a fundamentally outrageous contract they now wish to avoid. To the contrary, the Plaintiffs are rather sophisticated business people who have for some time operated an Amway distributorship.

Morrison v. Amway Corp., 49 F. Supp. 2d 529 534 (S.D. Tex. 1998).

Certainly, this analysis applies to Netco and Schmitz Associates, whose president billed the Schmitz Organization as "one of your top distributors in the history of the business," (A3094), and crowed that his departure from the roster of Amway distributors is "like Shaq not playing anymore." (*Id.*) An organization whose president bills himself as one of Amway's "top distributors in the history of the business" (out of more than 700,000 distributors in North America) (A2741; A3094), qualifies as a sophisticated business. Netco and Schmitz Associates were successful, wealthy "players" in the Amway world, and should not be heard to complain that they were somehow "tricked" into agreeing to arbitration. The real issue is that, have benefited richly from these contacts, they seek to avoid honoring their contractual obligations.

The alleged unconscionability of the Amway arbitration provision was discussed at length in *Morrison* and as in this case, the distributorship agreements of the some of

the plaintiffs in *Morrison* were updated by amendment. The *Morrison* court held that these plaintiffs were bound by the Rules of Conduct, including the arbitration provision, and rejected arguments that the adoption of an arbitration provision by amendment was procedurally unconscionable, and that the clause itself was substantively unconscionable. 49 F. Supp. 2d at 533-34. Accordingly, the trial court's contrary conclusion below was error.

a. Members of the Board of Directors of the Amway Distributor Association did not have "veto power" over the retention of arbitrators

The trial court erroneously concluded that Amway's arbitration procedures was unconscionable because the Amway's Rules provide for both Amway and the Board of Directors of the Independent Business Owners International Association (on which some of the Appellants sit) to establish a roster of neutral arbitrators for three-year terms, with additional terms to be added by unanimous vote of Amway and the board of the distributor association. (A3828-29.)

While a process in which both Amway and its independent distributors mutually choose a roster of potential arbitrators is a commendable rather than an unconscionable practice, the particular Rule that troubled the trial court has never been applied and no longer exists. (A3813.) Since 1998, when binding arbitration became a part of the Amway Rules, Amway and the distributor association voted on whether to retain any arbitrator on the roster of potential arbitrators. (*Id*.) Realizing that the provision was not being used and served no purpose, Amway modified the Rules of Conduct to eliminate

voting on the retention of arbitrators. (*Id.*) Because any arbitration involving Respondents will include the Rules in force at the time of arbitration, the "voting" rule will not be a part of any arbitration involving the parties to this action, and any alleged unconscionability therefore no longer exists.

The fact that Amway never enforced and eventually eliminated the "voting" rule from the Rules of Conduct was brought to the attention of the trial court on rehearing. (*Id*.) The trial court refused to reconsider, which was also error. *See Gannon v. Circuit City, Inc.*, 262 F.3d 677, 679, 681 (8th Cir. 2001) (trial court erred in declining to reconsider decision striking down allegedly unconscionable term, even though allegedly offending rule was never enforced and was eventually dropped, and arbitration provision contained an explicit severability provision).

Moreover, the Rule requiring a vote to retain an arbitrator never reposed "veto power" in any Appellant or in any member of the board of the distributor association. (A3815.) As explained by Jody Victor, a member of the distributors' board, the "unanimous vote" requirement refers to unanimity of the distributor's board, which had one vote, and Amway, which had one vote. *Id.* Although the board never took a vote on any arbitrator, each of the 30 board members would have been entitled to vote on the retention of an arbitrator, with the majority of votes determining the board's single vote. *Id.* Thus, there was never any veto power vested in any board member or in any Appellant who may have served a term on the distributor association board.

b. Amway is bound by its own Arbitration Agreement in the Rules of Conduct

The trial court also erroneously held that "Amway is not bound by its own arbitration requirements." (A3749.) This holding is simply wrong. As demonstrated to the trial court, Amway ***is*** bound to arbitrate disputes under the Amway Rules of Conduct. Amway's Director of Global Business Conduct and Rules/Business Support Materials Administration testified in an affidavit that:

> Amway is also bound to arbitrate disputes under [the Amway Rules] as part of its contract with distributors. It has always been understood at Amway that the requirement to arbitrate is reciprocal. Amway has filed no suit against a distributor since binding arbitration was added to the Rules. Instead, when Amway has a claim against a distributor, it follows the dispute resolution procedures, including binding arbitration.

(A3812.)

This testimony resolves the trial court's concerns, because to the extent that there was any ambiguity regarding the Amway Arbitration Agreement, it has been cured by the parties' course of performance. *See Royal Banks of Mo. v. Fridkin*, 819 S.W.2d 359, 362 (Mo. banc 1991) (a court may consider "the practical construction the parties have placed on the contract by their acts and deeds"). Moreover, since the Amway Rules of Conduct

were amended to include an arbitration provision, Amway has never taken the position that it is not bound to arbitrate. (A3812.)[17]

2. The confidentiality provisions cited by the Trial Court are a hallmark of commercial arbitration, and in any case the Amway Arbitration Provision specifically provides for public hearings if the court requires

Remarkably, the trial court also found that the confidentiality provision in the Amway Rules was unconscionable. This was error, as the provision actually provides that:

> the Arbitrator shall maintain the confidentiality of the hearings in the proceeding and shall have the authority to make appropriate rulings to safeguard confidentiality, ***unless the law provides to the contrary***.

Rule 11.5.31 (A1345; emphasis supplied).

Amway and the distributors board wanted the arbitration rules to provide for confidentiality to safeguard distributors' proprietary business information and to encourage distributors to make appropriate claims. (A3812-13; A3816.) However, if the

[17] Further, Amway is not a party to this case. Consequently, the issue of whether Amway is bound to arbitrate does not address the mutuality of obligation of the parties before the Court, and it is clear that Respondents and the Appellants are equally bound by the Amway Arbitration Rules.

law requires a public hearing the confidentiality rule specifically provides that confidentiality does not apply. (A1345.)

Such confidentiality protection is standard in business disputes, whether in arbitration or before a court. Indeed, the trial court entered a protective order in the case below. Similarly, the AAA, a nationally respected arbitration organization, also provides that arbitrations are generally to be considered confidential. AAA Commercial Arbitration Rule 23, which is nearly identical to the confidentiality rule cited by the trial court, states that "[t]he arbitrator and the AAA shall maintain the privacy of the hearings unless the law provides to the contrary." AAA Commercial Arbitration Rule 23, *available at* http://www.adr.org. Appellants respectfully submit that such a rule, which is strictly for the protection of the parties to the arbitration, and clearly provides that it does not apply if the law in a particular jurisdiction states otherwise, is not an unconscionable term.

3. The Trial Court erred in failing to sever allegedly unconscionable arbitral provisions, as provided for in the Amway Arbitration Rules and supported by federal law

In addition, the trial court erred in not applying the severability provision in the Amway Arbitration Rules. The rules state that:

> if any of these Rules, or part thereof, is discovered to be in conflict with a mandatory provision of applicable law, the provision of law will govern, and no other Rule will be affected. If any Rule, or part thereof, is found to be invalid

> by a court of competent jurisdiction, these Rules will be interpreted as though the invalid portion were not part of these Rules.

Rule 11.5.3. (A1339.)

The purpose of this provision is to ensure that, if some aspect of the arbitration rules is ruled to be invalid, the rest of the rules will remain and the right to arbitrate will be preserved. (A3816.) Indeed, this particular provision was important both to the distributor's board and to Amway. (A3816; A3813.) In light of the severability provision in the Amway Arbitration Rules, the trial court's decision to strike down the entire arbitration process because of its concerns with a few isolated provisions of the Arbitration Rules was misguided.

In reviewing the trial court ruling, this Court should be guided by the ruling of the Eighth Circuit in *Circuit City*. In that case, the trial court found unconscionable a provision that limited punitive damages. 262 F.3d at 679. The Eighth Circuit reversed, finding that striking the punitive damages provision would not disturb the "primary intent" of the parties to arbitrate their disputes, *id.* at 681-82, and that severing the offending damages clause was consistent with the terms of the contract, the intent of the parties, Missouri contract law, and the federal policy favoring enforcement of arbitration agreements. *Id.* at 683.

The *Circuit City* court also strongly cautioned that invalidating entire arbitration agreements because isolated terms are offensive undermines the strong federal policy favoring arbitration:

> [I]f we were to hold entire arbitration agreements unenforceable every time a particular term is held invalid, it would discourage parties from forming contracts under the [Federal Arbitration Act] and severely chill parties from structuring their contracts in the most efficient manner for fear that minor terms eventually could be used to undermine the validity of the entire contract. Such an outcome would represent the antithesis of the "liberal federal policy favoring arbitration agreements."

Id. at 682 (quoting *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24).

In sum, the trial court's conclusion that certain terms of the Amway Rules of Conduct were unconscionable was error. First, the cited provisions are not unconscionable. Second, the rule regarding "veto power" on retention of arbitrators that was cited by the court was incorrectly read, and in any case is no longer part of the Rules of Conduct. Third, any of the provisions cited by the trial court, even if they were unconscionable, should be severed from the rest of the Rules of Conduct, either under the severability provision of Rule 11.5.3, or through common-law severability.

4. The defenses to arbitrability raised by Respondents should be addressed by an arbitrator

While much was made in the court below about allegedly unconscionable terms, the court erred not only in the way those questions were resolved, but in resolving them at all. Likewise, Respondents' arguments below that the contract containing the Amway

arbitration clause was illusory, lacked good faith and was unenforceable for lack of mutual consent are addressed to the contract as a whole and thus should also be addressed to the arbitrator. As discussed above, the arbitrator is solely responsible for resolving issues concerning the validity of a contract that contains an arbitration clause, because such issues go to the merits of the parties' dispute. *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 402-04 (1967) (arbitrator must resolve claim for fraud in the inducement of a contract containing arbitration clause); *Coleman v. Prudential Bache Secs. Inc.*, 802 F.2d 1350, 1352 (11th Cir. 1986) ("[c]laims alleging unconscionability, coercion, or confusion in signing the agreement" go the formation of the entire contract and are for the arbitrator); *Hall v. Prudential-Bache Secs., Inc.*, 662 F. Supp. 468, 471 & n.1 (C.D. Cal. 1987) ("[C]laims concerning duress, unconscionability, coercion, or confusion in signing should be determined by an arbitrator because those issues go to the formation of the contract."); *St. Paul Fire and Marine Ins. Co. v. Courtney Enter., Inc.*, 270 F.3d 621, 624-25 (8th Cir. 2001) (claim of fraud in the inducement of contract with arbitration clause "goes to the merits" and is for the arbitrator); *Houlihan*, 31 F.3d at 696 n.5 (defense of failure of consideration "applies to the contract as a whole" and is for the arbitrator); *Creson v. Quickprint of Am., Inc.*, 558 F. Supp. 984, 987-88 (W.D. Mo. 1983) (duress is "of the same remedial character" as fraud in the inducement, and therefore should be decided by the arbitrator).

The public policy favoring arbitration also requires that Respondents' attacks on the Amway arbitration procedures and to the contract as a whole be addressed by the arbitrator rather than the Court. *See Hawkins*, 338 F.3d at 806-07; *Bob Schultz Motors*,

334 F.3d at 726. "Once a dispute is determined to be validly arbitrable, all other issues are to be decided at arbitration." *Larry's United Super*, 253 F.3d at 1085-86 (quoting *Peacock*, 110 F.3d at 230).

Furthermore, the arbitration provisions in the Amway Rules of Conduct further support that Respondents' alleged defenses to arbitrability are appropriately directed to the arbitrator. The Amway Rules of Conduct state that "[j]urisdictional and arbitrability disputes, including disputes over the existence, validity, interpretation or scope of the agreement under which Arbitration is sought, may be submitted to and ruled on by the Arbitrator." (A1269-70; *see also* A1340.) Additionally, the Amway Rules of Conduct provide for JAMS/Endispute arbitration (A1270; A1340), and JAMS/Endispute also has Comprehensive Arbitration Rules and Procedures. Rule 11(c) of the JAMS rules provides that "[j]urisdictional and arbitrability disputes, including disputes over the existence, validity, interpretation or scope of the agreement under which Arbitration is sought, and who are proper Parties to the Arbitration, shall be submitted to and ruled on by the Arbitrator. The Arbitrator has the authority to determine jurisdiction and arbitrability issues as a preliminary matter." JAMS Comprehensive Arbitration Rules, Rule 11(c), *available at* http://www.jamsadv.com/rules/comprehensive.asp.

In sum, although Respondents seek to evade arbitration by any means, including making multiple attacks on the procedures under which the arbitration would proceed and challenges to the validity of the Amway Rules rather than the arbitration clause itself,

none of these arguments address the limited inquiry to be made by this Court.[18] Because the Respondents are bound by the arbitration agreement in the Amway Rules of Conduct, and this arbitration agreement encompasses the business disputes between the parties, this Court should reverse the decision of the trial court, and order the parties to arbitration.

III. The Trial Court erred in denying Appellants' Motion to Compel Arbitration and to Stay Litigation Pending Arbitration because the Trial Court failed to address the separate arbitration agreement in the Pro Net Terms and Conditions, which independently bound all of the parties to arbitrate all issues in this case under the unimpeachable Rules of the American Arbitration Association ("AAA").

A. Standard of Review

The trial court's denial of the motion to compel arbitration is reviewed *de novo*. *Dunn Indus. Group*, 112 S.W.3d at 428.

B. The Pro Net Arbitration Agreement also requires arbitration of Respondents' dispute with Appellants

All members of Pro Net agreed to "abide by all Terms and Conditions of Association Membership." (A2136.) Those Terms and Conditions included a broad dispute resolution clause that requires arbitration of any disputes or controversies relating

[18] Indeed, to the extent Respondents have proved anything through this protracted litigation, it is precisely why businesses seek to limit the difficulty and expense of resolving business disputes by contracting for arbitration.

in any way to Pro Net, including all disputes between members of Pro Net and between Pro Net and any of its members. (A2139.) The Court should conclude that the parties have an agreement to arbitrate, and that the subject matter of this dispute is encompassed by the arbitration agreement in the Pro Net Terms and Conditions. Accordingly, the Court should hold that the Pro Net arbitration agreement requires arbitration of Respondents' dispute with Appellants.

1. The parties are bound by the Arbitration Clause in the Pro Net Terms and Conditions

a. Netco is bound by the Pro Net Arbitration Clause

The Court should conclude that Respondent Netco is bound by the AAA arbitration clause in the Pro Net Terms and Conditions. The Pro Net membership application form expressly states that Pro Net has "put into place procedures to avoid litigation" and that one condition of membership is "use of American Arbitration Association arbitration procedures" if disputes cannot be resolved internally. (*Id*.)

These terms were clearly disclosed to Pro Net applicants, including Netco and the Schmitzes. (A2090.) In addition, on the very first page of the membership application, directly under the title, is the provision that "The undersigned applicant agrees to abide by all Terms and Conditions of Association Membership." (A2136.) Those Terms and Conditions include a broad arbitration clause applicable to all disputes concerning Pro Net, including any disputes among its members or with Pro Net. (A2141.)

On December 9, 1998, Netco submitted its application for membership in Pro Net. (A2136.) The application expressly stated that it was submitted on behalf of "Netco, Inc.

(Charlie & Kim Schmitz)," and was signed by "Charlie E. Schmitz," who signed the application in his capacity as Netco's "President." (*Id*.) Netco submitted a check for membership in Pro Net, which was cashed by Pro Net. (A2091; A2137.) The Terms and Conditions of Pro Net membership – including the arbitration clause – became part of the membership "Obligations and Benefits" that were binding on Netco. This application was accepted by Pro Net and Netco, Schmitz Associates and the Schmitzes became members of Pro Net. (A2091; A2136.)

By agreeing to be bound by Pro Net's member obligations, Netco received the member benefits provided by Pro Net, which included, most notably, the benefits derived from "[m]aking business support materials, services, marketing materials and other print or electronic literature available for purchase by members." (A0114.) As part of its membership in Pro Net, Netco purchased more than 100,000 tapes and other BSMs from Global Support in 1998 and 1999. (A2516-17; A2520.) Many of these tapes were produced by Pro Net members that were not in the Schmitzes' upline or downline, and Netco and the Schmitzes purchased tapes made by at least thirteen Pro Net members with which Respondents have no connection in their lines of sponsorship. (A2518.) Thus, Respondents were able, through Pro Net, to distribute tapes and other BSMs that they would not otherwise have had the right to distribute or sell. (*Id*.)

The Pro Net membership of Netco and the Schmitzes in Pro Net also enabled them to sell their BSMs to other Pro Net members; Pro Net facilitated for sale of tapes and speeches by the Schmitzes through Global Support. (A2517-18.) In addition to these sales, the Schmitzes attended Pro Net functions in 1998 and 1999. (A0108.)

Additionally, Netco and the Schmitzes received other membership benefits by being highlighted in Pro Net publications. For example, in 1998, Pro Net published the profiles of Pro Net's Diamond members in a book entitled *Profiles: Portraits of Success*. (A2518; A2142-297.) In it, the Schmitzes were prominently featured as successful Amway Diamond distributors who had joined Pro Net. (A2275-76.) In their profile, the Schmitzes promoted not only their "great lifestyle" and "close relationships and enduring friendships we have in our business." (A2276.) The Schmitzes also wax eloquent in discussing the benefits of their Pro Net network: "The great thing about networking is that we all work as a team. As we assist others in the group to develop solid businesses, we all win." *Id.* The Schmitzes' enthusiastic involvement with this Pro Net publication confirms that they were Pro Net members who received membership benefits from Pro Net. Indeed, the Schmitzes committed to purchasing 200 copies of this hardbound book. (A2662.)

Having received these significant member benefits provided under their agreement with Pro Net, Netco and the Schmitzes cannot now avoid the binding member obligation of resolving this dispute through AAA arbitration.

b. Respondent Schmitz Associates is also bound by the Pro Net Arbitration Clause

Respondent Schmitz Associates also is bound by the arbitration clause of the Netco agreement with Pro Net because it was an integral part of the "Schmitz Organization" which was a member of Pro Net. (A2516; A2664; A2313; A2315.) Although the Pro Net application was signed by Schmitz Associates President and

Principal Charlie Schmitz for "Netco, Inc. (Charlie and Kim Schmitz)" (A2136), in the Amway business "individual principals, their Amway distributorship corporation, and their Amway-related BSMs/functions corporation are generally considered together to comprise the principals' 'organization.'" (A2313; *see also* A2090.) Accordingly, the Pro Net Steering Committee "intended that membership in Pro Net would include [a] distributor's entire Amway and Amway-related BSMs/functions organization." (A2313; A2089.) Indeed, the Pro Net Bylaws state that "*Organizations* seeking membership in the Corporation as Regular Members must submit a completed application." (A2103; emphasis added.) Given the admissions by Schmitz Associates that it "facilitated the Amway-related rally, convention and function business for Charlie and Kim Schmitz (Netco)" (A0004) that Schmitz Associates operated without any employees by paying a management fee to Netco, and that Netco, the Schmitzes and Schmitz Associates collectively refer to themselves as the "Schmitz Organization" (A0550-51), the signing of the Pro Net application by President Charlie Schmitz also bound Schmitz Associates.

Even if Schmitz Associates were not a full member of Pro Net, it still is bound by the Pro Net Terms and Conditions as a third-party beneficiary or, alternatively, under the doctrine of equitable estoppel. Schmitz Associates' claims are based upon its allegedly adverse treatment within the Pro Net organization. For example, Schmitz Associates alleges "conspiratorial efforts" of the Appellants "to monopolize and control" the distribution of BSMs and eliminate competition within the Gooch Network through "mandatory provisions in the Pro Net 'Membership Application Terms and Conditions' for 'regular members.'" (A0608.) Schmitz Associates further alleges that "coercive

terms" in the Pro Net Terms and Conditions for non-voting members "served as a means to control the distributors of BSMs." (A0609.) As such, Schmitz Associates has directly placed the Pro Net Terms and Conditions at issue in its claims. Thus, Respondents' allegations demonstrate that Schmitz Associates' standing to sue the Appellants is based, at least in part, on claims arising from the Appellants' alleged breach of the Pro Net Membership Terms and Conditions and Pro Net's Bylaws. (A2140-41; A2103.)

Schmitz Associates' reliance on the Pro Net Terms and Conditions for its claims requires it to arbitrate under that agreement. First, that reliance is in essence a claim to be a third-party beneficiary of the membership agreement entered into by Netco. It is well established that a third-party beneficiary of an agreement is bound to arbitrate under that agreement. Schmitz Associates "cannot claim a right to maintain an action based on [its] status" under the Pro Net Terms and Conditions "and, at the same time, disavow this relationship for the purposes of arbitration." *Tractor-Trailer Supply*, 873 S.W.2d at 631.

Second, Schmitz Associates is equitably estopped from arguing that it is not bound by the agreement. It cannot assert rights under an agreement but disavow the obligations that the agreement imposes. *See, e.g.*, *Sunkist Soft Drinks*, 10 F.3d at 757-58. Accordingly, the Court should hold that Schmitz Associates is bound by the Arbitration Agreement in the Pro Net Terms and Conditions.

c. Appellants are entitled to compel arbitration under the Pro Net Arbitration Clause

The Court also should conclude that Appellants are entitled to compel arbitration under the Pro Net arbitration clause. Seven of the eleven Appellants joined Pro Net as

members[19] and therefore are subject to the arbitration clause set forth in the Pro Net Terms and Conditions. In addition, Pro Net itself is a defendant and under the arbitration clause is entitled to compel arbitration of disputes "between the Association and any of its members." (A2141.)

The remaining three Appellants are entitled to compel arbitration because of their alleged relationship to Pro Net. Appellant Global Support was named as a defendant because it provided services to Pro Net members under a contract and licensing agreement with Pro Net and is alleged to be a "co-conspirator" with Pro Net "buying, manufacturing and supplying and/or selling business support materials or 'tools' to Defendant Pro Net members." (A0554.) *See McMahan Secs. Co. L.P. v. Forum Capital Mkts. L.P.*, 35 F.3d 82, 88 (2d Cir. 1994); *Pritzker v. Merrill Lynch, Piere, Fenner & Smith*, 7 F.3d 1110, 1122 (3d Cir. 1993). Appellant Jim Evans and J. L. Evans & Associates, although not Pro Net members, are alleged to be "co-conspirators" with Pro Net and with the Pro Net member Appellants. (A0553-54.)

It is well established that entities that are not signatories to arbitration agreements, such as these three Appellants, are still entitled to compel arbitration. *See Pritzker*, 7 F.3d at 1122 (non-signatory may demand arbitration under an agreement if non-

[19] Those Appellants are Jimmy V. Dunn, Jimmy V. Dunn & Associates, Harold Gooch, Gooch Enterprises, Inc., Gooch Support Systems, Inc., Billy S. Childers and TNT, Inc. (A0109.)

signatory's interests are "directly related to, if not predicated upon, [the signatory's] conduct").

2. The Arbitration Clause in the Pro Net Terms and Conditions covers Respondents' dispute with Appellants

This dispute is governed by the substantive provision of the Federal Arbitration Act, and that body of law that requires courts to "construe arbitration clauses as broadly as possible" and ensure that "[a]mbiguities as to the scope of the arbitration are resolved in favor of arbitration." *Fru-Con Constr. Co.*, 908 S.W.2d at 744; *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24-25. Under this rule of construction and the federal policy favoring arbitration the Court should conclude that the arbitration clause in the Pro Net Terms and Conditions covers Respondents' dispute.

The Pro Net arbitration clause applies to two distinct categories of claims, and all of the claims in this case fit within one or both of these categories. First, the clause governs "any dispute, controversy, or claim between one or more members of the Association or between the Association and any of its members." (A2141.) All of Respondents' claims against eight of the eleven Appellants obviously fit within this category, because Respondents and these Appellants are all members of Pro Net, or principals of Pro Net members. In addition, Respondents' claims against Pro Net plainly fit within the category of claims "between the Association and any of its members." (*Id.*)

Second, the arbitration clause governs "[a]ny dispute, controversy, or claim arising out of, relating to, or concerning the interpretation or performance of the [Pro Net] contract . . . or the breach thereof." (*Id.*) This portion of the clause is extraordinarily

broad, because it covers not only disputes "arising out of" the agreement, but also disputes "relating to" the agreement. The clear intent of the language of this part of the arbitration clause demonstrates an intent to make it as broad as possible in embracing disputes concerning Pro Net. *Fleet Tire Serv. of N. Little Rock v. Oliver Rubber Co.*, 118 F.3d 619, 621 (8th Cir. 1997) ("arising from" and "relating to" provision "constitutes the broadest language the parties would reasonably use to subject their disputes to that form of settlement, including collateral disputes that related to the agreement containing the clause"); *see also Lebanon Chem. Corp. v. United Farmers Plant Food, Inc.*, 179 F.3d 1095, 1101 (8th Cir. 1999).

This broad arbitration clause covers all of Netco's and Schmitz Associates' claims. Respondents make it clear that all of their claims in this matter relate to Pro Net, and in particular to an alleged conspiracy by Appellants to utilize Pro Net as a vehicle for depriving Respondents of the financial benefits of their "tool" and "function" businesses and disrupt Respondents' relationship with their Amway and BSM "downline." Respondents premise their claims on the specific assertion that Appellants used the Pro Net Terms and Conditions to further their alleged conspiracy:

> Defendants' conspiratorial efforts to monopolize and control the distribution of BSMs and to eliminate competition within the Gooch network were facilitated by. . . mandatory provisions in the Pro Net 'Membership Application Terms and Condition' for 'regular' members[.]

(A0608.) Thus, applying the rules of construction under the FAA requiring an interpretation in favor of arbitration, this Court should conclude that the AAA arbitration clause in the Pro Net Terms and Conditions covers Respondents' claims against all Appellants, because they are claims "relating to, or concerning the interpretation or performance of the [Pro Net] contract." (A2141.)

In so doing, the Court should follow the reasoning of the Circuit Court of Duval County, Florida, which held that the arbitration agreement in the Pro Net Terms and Conditions requires arbitration of exactly the same types of claims asserted in this case. *See U-Can-II* (A3837-42). In *U-Can-II*, a Pro Net member sued most of the same Appellants involved in the present case, making virtually identical allegations that they conspired to utilize Pro Net as a vehicle for depriving the plaintiff of the financial benefits of its "tool" business. The Florida court properly held that "the gist of [the Plaintiff's] claims is that the Defendants used Pro Net to take its BSM business, a subject matter that *clearly is within the scope of the Pro Net arbitration clause*." (A3839; emphasis added.)

3. The Circuit Court's grounds for decision do not apply to the Pro Net Arbitration Clause

In adjudicating the issues in this appeal, this Court should note that the Circuit Court's grounds for decision do not even apply to the Pro Net Terms and Conditions. The Circuit Court based its ruling solely on the ground that the Amway arbitration procedures were unconscionable. (A3901.) The Circuit Court's analysis of the Amway procedures was fundamentally flawed, but in any case has no bearing on the Pro Net

arbitration clause. The Pro Net arbitration clause does not utilize the Amway arbitration procedures, but instead requires that the arbitration be "administered by the American Arbitration Association under its Commercial Arbitration Rules." (A2141.) The AAA rules, of course, establish the procedures routinely used throughout the country in commercial arbitrations, and present none of the questions of unconscionability raised in the Circuit Court's letter opinion.

4. The defenses to arbitrability raised by Respondents should be addressed by an arbitrator

As with the arbitration agreement in the Amway Rules of Conduct, Respondents raise an extraordinary laundry list of complaints regarding arbitration under the Pro Net Terms and Conditions. Significantly, however, the Circuit Court below did not raise any unconscionability challenges – the sole basis on which the trial court had denied the motion to compel arbitration. – as to the Pro Net agreement. Nor could any such argument have been substantiated, since the Pro Net arbitration was to be administered by the American Arbitration Association under its Commercial Arbitration Rules. As the existence of the Pro Net binding arbitration agreement has been established, other issues which Respondents wish to raise concerning the scope of the agreement, and any other challenges to the Pro Net contract containing the arbitration clause, must be addressed to the arbitrator. *See Bob Schultz Motors*, 334 F.3d at 726 ("[I]f the parties have agreed to arbitration, the [Federal Arbitration] Act requires that a district court order them to proceed to that forum, where they must address all other claims to the arbitrator.").

For example, Respondents below raised a variety of defenses to the Pro Net contract containing the arbitration clause, including alleged waiver, economic duress, and membership ineligibility. Under *Prima Paint* and its progeny, as discussed earlier in this brief, these alleged challenges to the contract as a whole are to be submitted to the arbitrator. *See, e.g.*, *Howsam*, 537 U.S. at 84 ("waiver, delay, or a like defense to arbitrability" to be presented to the arbitrator, as well as "prerequisites such as time limits, notice, laches, estoppel, and other conditions precedent to an obligation to arbitrate").

The Pro Net Arbitration Agreement provides that disputes "shall be submitted to and settled by binding arbitration administered by the American Arbitration Association under its Commercial Arbitration Rules in effect at that time." (A2141.) Rule 7(a) of the same Rules – incorporated into the Pro Net arbitration clause through Rule 1(a) – provides that the arbitrator will decide issues concerning the existence, scope or validity of the arbitration agreement:

> [t]he arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope or validity of the arbitration agreement.

AAA Commercial Arbitration Rule 7(a), *available at* http://www.adr.org.

Given that issues concerning the scope of the arbitration shall be addressed to the arbitrator under the AAA Rules, this Court should follow the guidance of numerous other courts that have determined that an arbitrator must resolve any questions as to the scope of an arbitration agreement. *See, e.g.*, *Sleeper Farms v. Agway, Inc.*, 211 F. Supp. 2d

197, 200 (D. Me. 2002) (Former AAA Rule 8, now AAA Rule 7(a), is "a 'clear and unmistakable' delegation of scope-determining authority to an arbitrator") (citation omitted); *Lucile Packard Children's Hosp. v. U.S. Nursing Corp.*, No. 02-0192 MMC, 2002 WL 1162390, at *3 (N.D. Cal. May 29, 2002) (under arbitration agreement governed by AAA rules, questions of arbitrability are to be determined by the arbitrator).

CONCLUSION

This Court should reverse the Circuit Court's judgment, and remand this case to the Circuit Court, with directions that the parties be ordered to arbitration under both the Amway Rules of Conduct and the Pro Net Terms and Conditions and that the proceedings be stayed pending arbitration.

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The undersigned hereby certifies that two copies of Appellants' Substitute Opening Brief and its appendix and a disk containing the brief were delivered via overnight mail on the 11th day of July, 2005, to each of the following:

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CERTIFICATE OF COMPLIANCE

The undersigned certifies that the forgoing brief includes the information required by Rule 55.03 and complies with the limitations contained in Rule 84.06(c). Relying on the word count of the Microsoft Word program, the undersigned certifies that the total number of words contained in this brief is 22,830, excluding the cover page, signature block, and certificates of service and compliance.

The undersigned further certifies that the diskette filed herewith containing Appellants' Substitute Opening Brief in electronic form complies with Rule 84.06(g) because it has been scanned for viruses and is virus-free.

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