§ 90.300", and that the security deposit would be used "to remedy lessor's defaults in the performance of this agreement and to repair damage to the premises."

By the terms of his lease and of Or. Rev. Stat. § 90.300, Casserino thus had two rights: the right to live in his apartment for one month without paying additional rent, and the right, upon vacating the premises, to have repairs costing $400 or less satisfied from his already-committed funds. Although these benefits were to be enjoyed in the future, Casserino became entitled to them upon paying the deposit, both by the terms of the lease and by operation of Oregon lease law. Because the interest protected by the homestead exemption derives from the residential leasehold, the benefits and burdens of the leasehold—including both the obligation to pay a deposit and the right to have it applied to particular purposes—are an integral part of the leasehold. Therefore, they cannot be detached from the rest of the exemptible leasehold interest.

The court stated that interpreting Oregon's homestead statute as not exempting rent and security deposits would produce a counter productive result. If landlords were required to turn over the leaseholder's deposits to the bankruptcy trustee, they would presumably demand from the debtor a replacement deposit that, in many cases, he or she could not pay and could not arrange for others to pay. A debtor who could not replace the security deposit would often face eviction. This outcome would completely subvert the homestead exemption's purpose of allowing the debtor to keep "a roof over [his] head.", and would be at odds with Oregon's policy to give the homestead statute a "liberal and humane interpretation."

## ARBITRATION

### NONPARTY NOT BOUND BY ARBITRATION AGREEMENT

R.J. Griffin & Co. v. Beach Club II Homeowners Ass'n., 384 F.3d 157 (4th Cir. 2004).

**FACTS:** Drake Dev. Corp. IV ("Drake") engaged R.J. Griffin & Co. ("Griffin") as a contractor to construct the Beach Club II, a forty-five unit condominium. The contract called for "all claims, disputes, and other matters in question between the Contractor and the Owner arising out of, or relating to, the Contract Documents or the breach thereof" to be decided by arbitration. After construction completed in 1996, Drake filed a master deed on the property. The deed imposed restrictions on Drake, the condominium owners, and the Beach Club II Homeowners Association ("BCHA"), including arbitration of "any dispute arising out of use, ownership, or occupancy of…the common elements…and any complaint against the Grantor."

BCHA filed suit against Drake, Griffin and two others after an inspection revealed numerous defects in the condominium units. The claims asserted against Griffin included negligence and breach of implied warranty of good workmanship. Griffin then sought an order in federal court to compel the BCHA to arbitrate the claims pursuant to the general contract and the Beach Club master deed. The district court dismissed the claim on abstention principles, but the 4th Circuit reversed, remanded, and instructed the district court to rule on the merits. The district court denied Griffin's motion to compel arbitration. Griffin again appealed.

**HOLDING:** Affirmed.

**REASONING:** Griffin argued that BCHA was compelled to arbitrate under the arbitration clauses found in the general contract and the master deed. Griffin asserted that the general contract bound BCHA, even though not a signatory to the contract, to arbitrate any claims against him because of equitable estoppel.

Arbitration clauses are a matter of contract and cannot bind parties who did not sign the contract. While it is possible that parties can agree to arbitrate by means other than signing the contract, equitable estoppel will only apply when one party attempts to hold another party to terms of an agreement, while simultaneously trying to avoid the agreement's arbitration clause. Relying on *International Paper v. Schwabedissen,* 659 F.2d 836 (7th Cir. 1981) the court concluded arbitration would not be compelled because the association was seeking a direct benefit from the general construction contract. The association's claims were derived from common law, not the contract, and thus the association was in no way relying on the contract for any benefit. Here, Griffin's duties arose out of its role as a builder, not out of its construction contract with Drake.

Griffin further argued that that the association was compelled to arbitrate based on the master deed because the association benefited from the deed as a third party. The court, however, found that Griffin and Drake did not intend for the association to be a third-party beneficiary at the time of signing. The court concluded, therefore, that the association was not compelled to arbitrate.

### ARBITRATORS AWARD OF 6 MILLION IN PUNITIVE DAMAGES FOR CLAIM ARISING OUT OF WRONGFUL DEBT COLLECTION UPHELD

Stark v. Sandberg, Phoenix and Von Gontard, P.C., 381 F.3d 793 (8th Cir. 2004).

**FACTS:** In 1999, in hopes of shoring up a failing business, Stanley and Patricia Stark ("Starks") borrowed $56,900 against their home and secured the loan with a mortgage. Despite the infusion of funds, the business failed and in early 2000 the Starks petitioned for bankruptcy protection. During this same time, the Starks' lender sold the note, which was in default, to EMC Mortgage Corporation ("EMC") making EMC a debt collector under the provisions of the Fair Debt Collection Practices Act ("FDCPA"). During late 2000 and early 2001, despite letters from the Starks advising EMC that they were represented by counsel and not to contact them directly, EMC

tried several times to deal directly with the Starks.

The Starks subsequently filed suit against EMC and its attorneys alleging violations of the FDCPA. EMC moved to compel arbitration pursuant to the loan agreement and the motion was granted. During the arbitration, EMC's agent, without the Starks' consent, forcibly entered the home and posted a sign in the front window which indicated that the "[p]roperty ha[d] been secured and winterized." Further, in late 2001 and early 2002, EMC wrote to the Starks directly regarding insurance coverage on the home. In total, the Starks testified EMC contacted them by mail, telephone or in person at least ten times after being advised they were represented by counsel. After these incidents, the Starks moved to amend their complaint to include claims alleging intentional torts against EMC and seeking punitive damages. The arbitrator found that EMC violated the FDCPA and awarded the Starks damages, including 6 million dollars in punitive damages. The district court vacated the award of punitive damages, holding the arbitration agreement was unambiguous and not susceptible to the arbitrator's interpretation. The Starks appealed the judgment of the district court.

**HOLDING:** Reversed.

**REASONING:** In the case of an arbitration award the courts accord an extraordinary level of deference to the underlying award itself, because federal courts are not authorized to consider the merits of an arbitral award. The court held that the situation where the arbitration award was completely irrational, or a manifest disregard for the law, would be a situation conducive to vacating the award. An award is irrational where it fails to draw its essence from the agreement. An agreement is a manifest disregard for the law where the arbitrator clearly identifies the applicable, governing law and then proceeds to ignore it.

The court held that because the arbitration agreement waived the right to sue for punitive damages to the fullest extent of the law, and the applicable law in this case was Missouri law, which precludes waivers of punitive damages, the arbitration provision was ambiguous. In this situation, the court stated it would construe the provision against the party who drafted it, in this case EMC. Because the waiver provision was construed against EMC, the court held the award of punitive damages drew its essence from the agreement. The court stated, "[a] party seeking vacatur [based on manifest disregard of the law] bears the burden of proving that the arbitrators were fully aware of the existence of a clearly defined governing legal principle, but refused to apply it, in effect, ignoring it." To the extent the arbitrator's decision set forth the basis for the punitive damages award, it was apparent the arbitrator did not disregard governing law. The arbitrator's award was intended to punish EMC and to deter others from similar conduct.

## UNIFORM COMMERCIAL CODE

### BAD FAITH UNNECESSARY FOR BREACH OF GOOD FAITH

### NEW BUSINESS RULE DOES NOT PRECLUDE DAMAGES TO AN ENTERPRISE THAT HAS NEVER TURNED A PROFIT

O'Tool v. Genmar Holdings, Inc., ____ F.3d ____ (10th Cir. 2004).

**FACTS:** Cassandra and John O'Tool and Geoffrey Pepper ("Plaintiffs") sold their business, Horizon Marine, ("Horizon") to Genmar Holdings, Inc. ("Genmar"). Under the terms of the parties' written purchase agreement, Genmar created a new subsidiary ("GMK") that assumed all of the assets and liabilities of Horizon. GMK also offered written employment agreements to Pepper, who became President of GMK, and to Pepper's daughter and son-in-law ("O'Tools"). The purchase price paid by Genmar for Horizon was comprised of two components: (1) cash consideration of $ 2.3 million dollars; and (2) "earn-out consideration" that could total up to $5.2 million dollars if certain performance targets were met over the next 5 years.

Shortly after the sale, Genmar moved production for two of Genmar's other brands to the GMK facility, made these new brands a priority over the existing boat line, shifted additional costs to the facility for design of new boats, and made other accounting changes that prevented the GMK facility from meeting the targets needed for the "earn-out." After Pepper expressed his concerns to the CEO of Genmar, he and the O'Tools were terminated. After plaintiffs' termination, Genmar converted all the old Horizon dealers to other Genmar brands and in July 2001 stopped producing all of the old line of boats.

Plaintiffs filed suit asserting claims for fraud, breach of the purchase agreement, tortious interference with a contract, breaches of their individual employment agreements, etc. The District Court granted summary judgment in favor of defendants on Pepper's breach of employment agreement claim and the tortious interference claims. The jury found in favor of Plaintiffs on the breach of the purchase agreement and awarded $2.5 million in damages and found in favor of the O'Tools' on their breach of employment contract claims. The jury found against Plaintiffs on all remaining claims. Genmar filed a motion for judgment as a matter of law, or for remittitur or a new trial, all of which were denied. Genmar appealed.

**HOLDING:** Affirmed

**REASONING:** Every contract imposes a duty of good faith and fair dealing on each party. In the instant case, breach of good faith occurred when Genmar changed known brand names; shifted production priority to benefit its original line of boats; required the new subsidiary GMK to bear the costs of design and production of the new line of Ranger boats; failed to give Pepper the necessary operational control; discontinued the Plaintiff's prior brand of boats; flipped Plaintiff's customers to Defendants' prior brands

**Every contract imposes a duty of good faith and fair dealing ON each party.**