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Federal Statute Precluding Enforcement of Arbitration Clauses in Motor Vehicle Franchise Contracts Inapplicable to Snowmobile, ATV Dealer Agreements

Champion Auto Sales, LLC v. Polaris Sales Inc., 2013 U.S. Dist. Lexis 65219 (E.D.N.Y. Mar. 27, 2013)

Mandatory arbitration clauses are common in franchise agreements, including motor vehicle franchise agreements. Whether a manufacturer can enforce such a provision requires an analysis of competing state and federal statutes and a determination of whether the vehicles sold fall within the statutory definition of a "motor vehicle." In an opinion addressing the various statutory regimes, a federal district court in New York held the Motor Vehicle Franchise Contract Arbitration Fairness Act, 15 U.S.C. 1226 (the Fairness Act), did not limit a franchisor's effort to arbitrate a dispute concerning dealer agreements for snowmobiles and all-terrain vehicles (ATVs). At the same time, the court held that the Fairness Act did serve to block arbitration of claims regarding the same dealer's motorcycle franchise. Champion Auto Sales, LLC v. Polaris Sales Inc., 2013 U.S. Dist. Lexis 65219 (E.D.N.Y. Mar. 27, 2013).

Factual and Procedural Background

Polaris entered into a Dealer Agreement with Champion on July 21, 2011, pursuant to which Champion was authorized to sell Polaris snowmobiles, various types of ATVs and Victory brand motorcycles. The Dealer Agreement provided that any claims arising between the parties were subject to mandatory arbitration proceedings in Minnesota. Although only one agreement was executed, the parties agreed that each product line was considered to be a separate franchise. *Champion* 2013 U.S. Dist. Lexis 65219 at *2-4.

In January 2012, Polaris sent a termination notice to Champion, accusing it of breaching the Dealer Agreement. Champion and its principal filed suit in New York State Supreme Court, seeking preliminary and permanent injunctive relief and asserting a number of claims, including violation of the New York Franchised Motor Vehicle Act (NYFMVA), N.Y. Veh. 7 Traf. Law ? 463. Polaris removed the action to the United States District Court for the Eastern District of New York and filed a motion to compel arbitration and/or stay the action.

Enforceability of the Arbitration Clause

In its opinion, the court analyzed whether the claims were subject to the arbitration clause in the agreement and then whether that clause was enforceable. As the court noted, there is generally a four-part inquiry when determining whether a cause of action is subject to arbitration: (1) whether the parties agreed to arbitrate; (2) the scope of the agreement; (3) if federal statutory claims are asserted, whether Congress intended that certain claims be nonarbitrable; and (4) if some, but not all, of the claims are arbitrable, whether to stay the balance of the proceedings pending arbitration. *Champion* 2013 U.S. Dist. Lexis 65219, at *7 (quoting *JLM Indus., Inc v. Stolt-Nielsen SA*, 387 F.3d 163, 169 (2d Cir. 2004)).

Although the court determined that the franchise agreement contained an agreement to arbitrate that covered the asserted claims, it needed to address Champion's contention that the clause was not enforceable for two reasons. First, the court quickly disposed of Champion's argument that the clause was unconscionable simply because it was drafted by Polaris, a

party claimed to be in a superior bargaining position. Second, the court examined whether Section 469(2) of the NYFMVA nullified the arbitration clause in the Dealer Agreement. That section of the act provides, in part, as follows:

> Whenever a franchise provides for the use of arbitration to resolve a controversy arising out of or relating to such contract, arbitration may be used to settle such controversy only if after such controversy arises all parties to such controversy consent in writing to use arbitration to settle such controversy.

Id. Thus, under the NYFMVA, a mandatory arbitration clause in a motor vehicle franchise agreement is converted into a consensual arbitration clause. The court, however, held that this portion of the NYFMVA was itself not enforceable because it was preempted by the Federal Arbitration Act, 9 U.S.C. 1 (the FAA). *Champion* 2013 U.S. Dist. Lexis 65219 at *12. "Once it is determined that the FAA applies to a particular arbitration agreement, incongruent state statutory schemes are preempted." Id. (quoting *Shamah v. Schweiger*, 21 F.Supp.2d 208, 212 (E.D.N.Y. 1998).

Finding there was an agreement to arbitrate and the scope of the agreement encompassed all of Champion's claims, the court next looked at whether Congress intended to make any of the asserted claims nonarbitrable. Champion argued that Congress explicitly carved out an exception to the FAA in passing the Fairness Act, which (much like the NYFMVA) precludes the enforcement of pre-dispute arbitration clauses in motor vehicle franchise contracts. The Fairness Act states,?

> [W]henever a motor vehicle franchise contract provides for the use of arbitration to resolve a controversy arising out of or relating to such contract, arbitration may be used to settle such controversy only if after such controversy arises all parties to such controversy consent in writing to use arbitration to settle such controversy.

15 U.S.C. 1226.

On this point, the court agreed with Champion but only with respect to the motorcycle franchise. Under the definition incorporated into the Fairness Act, a "motor vehicle" is defined as "a vehicle driven or drawn by mechanical power and manufactured primarily for use on public streets, roads and highways, but does not include a vehicle operated only on a rail line." See 49 U.S.C. 30102(a)(6). The court concluded that this definition excluded Champion's claims related to its snowmobile and ATV franchise agreements from the Fairness Act.

The final step in the court's analysis was whether to stay the claims that were not subject to arbitration. It held, because the non-motor vehicle claims were identical to the claims related to Champion's motorcycle franchise, a stay would promote judicial economy and avoid confusion and the possibility of inconsistent results. *Champion*, 2013 U.S. Dist. Lexis 65219 at *18.

Separately, the court concluded that it lacked authority under the FAA to compel the arbitration proceeding in Minnesota as provided for in the Dealer Agreement. Because the FAA grants a district court the power to compel arbitration only within its own district, 9 U.S.C. 4, the court stayed the litigation and left it to the parties to initiate an arbitration proceeding relating to the non-motor vehicle claims in the appropriate venue. *Champion*, 2013 U.S. Dist. Lexis 65219 at * 20 (citing *Provident Bank v. Kabas*, 141 F.Supp.2d 310, 315 (E.D.N.Y. 2001).

The decision highlights limitations in the Fairness Act where the franchisor-franchisee relationship extends beyond motor vehicles. In such cases, a court will likely stay the motor vehicle-related claims while the controversy is arbitrated. In many cases, resolution of the arbitration will likely dictate how the motor vehicle-related claims will be determined.