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THE EXPANDING USE OF BINDING ARBITRATION AGREEMENTS IN NURSING FACILITIES (AND OTHER HEALTH CARE PROVIDERS).

By Greg Young and Brian White

I. INTRODUCTION.

The use of arbitration agreements has grown in recent years, and with the growing support of the courts, this trend is likely to continue. The use of arbitration as an alternative to trial is seen to have many advantages. In fact, the Supreme Court has pointed out several of its advantages, including it is cheaper and faster than litigation, it can have simpler procedural and evidentiary rules, it normally minimizes hostility, and it is often more flexible in regard to scheduling of times and places of hearings and discovery devices.[1] These advantages are equally applicable in the nursing facility industry, or other expensive and time consuming litigation businesses, where disputes arise between nursing home facilities and their residents. Given the increasing costs of nursing home litigation, the use of arbitration agreements has become more and more prevalent in nursing facility settings and other business enterprises.

Unfortunately, there are many pitfalls that can potentially render an arbitration agreement unenforceable. While the pitfalls are plentiful and largely relate to the law of construction of contracts, this article will focus on two potential pitfalls in the nursing home setting. First, as will be discussed below, the Kansas Uniform Arbitration Act prohibits the enforcement of arbitration agreements for tort claims. This obviously is a major road block to nursing facilities who wish to arbitrate all disputes with their residents, including torts. Fortunately, the Federal Arbitration Act (FAA) will preempt this Kansas prohibition, if the nursing facility residential agreement, which includes the arbitration provision, is "a contract evidencing a transaction involving commerce." As such, one area of focus in this article will be what is needed to meet the "involving commerce" requirement of the FAA so that the tort prohibition provision of the Kansas Act is preempted. A second area of focus in this article will be avoiding a finding that the arbitration agreement is unconscionable, and, therefore, unenforceable. Nursing facility arbitration agreements appear to be more susceptible to a finding of unconscionability as they usually involve elderly individuals who are often in need of immediate care or assistance (with few options) and the agreements are usually considered contracts of adhesion. Before we examine these two issues, however, a review of the Kansas Uniform Arbitration Act and FAA provisions will be instructive.

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II. STATE AND FEDERAL ARBITRATION STATUTES.

A. Kansas Uniform Arbitration Act.

Under K.S.A. 5-401(b), "a provision in a written contract to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable and irrevocable except upon such grounds as exist at law or in equity for the revocation of any contract." There are, however, several major exceptions to this general rule, including and most important to this article, an arbitration provision will not be valid in any contract providing for arbitration of a tort claim.[2]

The Kansas Uniform Arbitration Act provides some procedures and requirements for the actual arbitration process which should be examined when drafting and or using an arbitration agreement. These basic requirements, including a provision for the appointment of arbitrators and procedures for awarding and challenges damages, are to be followed unless otherwise agreed. While these specific procedures will not be discussed in this article, it should be kept in mind that the Act allows the parties to mold their arbitration process as they see fit through their arbitration agreement.

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Kansas Supreme Court Clarifies Class Certification Standards

By James P. Muehlberger and Andrew D. Carpenter

I. INTRODUCTION

As class counsel and courts are aware, an issue that frequently arises in the class certification calculus is the tension between a court's duty to conduct a "rigorous analysis"[1] as to whether the plaintiff has satisfied plaintiff's burden to demonstrate that the requirements of Federal Rule of Civil Procedure 23 (or its state law counterparts) are satisfied, and the so-called "*Eisen*"[2] rule, which plaintiffs argue mandates that the court must accept as true the allegations in plaintiff's Complaint for purposes of the class certification analysis. Over the last few years, several federal circuit courts have rejected the proposition that *Eisen* requires a court to analyze a proposed class based upon the bare allegations in the pleadings. Recently, in a well-reasoned decision, *Dragon v. Vanguard Industries, Inc.*, 277 Kan. 776, 89 P.3d 908, (Kan. 2004), the Kansas Supreme Court joined this growing trend and provided needed clarification as to class certification standards in Kansas.

This article will first describe the origin of the *Eisen* rule before addressing later Supreme Court decisions clarifying *Eisen*. Recent federal court decisions which recognize the limits of *Eisen* will then be analyzed. Finally, this article will discuss *Dragon v. Vanguard Industries, Inc.* and its teachings as to class certification standards in Kansas.

A. The *Eisen* Rule

Thirty years ago, the United States Supreme Court in *Eisen v. Carlyle & Jacqueline*, 417 U.S. 156 (1974), issued the following statement:

> "[N]othing in either the language or history of Rule 23 . . . gives a court any authority to conduct a preliminary inquiry into the merits of a suit in order to determine whether it may be maintained as a class action."

Id. at 177. From this single sentence of *dicta*, many plaintiffs' counsel, and even some courts, have accepted the proposition that courts must assume for purposes of class certification analysis that whatever allegations and averments plaintiffs make are true, without any analysis of whether there is actually any factual support for such allegations and averments.

But the context in which the Supreme Court made that statement demonstrates its limits. *Eisen* presented the question of whether, under Federal Rule of Civil Procedure 23, the district court should have required the defendant rather than the plaintiffs in that case to bear the full cost of providing class notice to approximately 2.25 million potential class members. The district court had held that the defendant should bear 90% of the cost because plaintiff was "more likely" to "prevail on his claims." *Id.* at 177. In other words, the district court had shifted the cost of notice to the defendant based on its assessment of the strength of the merits of the case.

Read in its proper context, the *Eisen dicta* merely states the obvious: it is improper to shift the entire burden of notice payment from one party to another based on the court's preliminary evaluation of which party will ultimately prevail on the merits of the claim. *Id.* at 178. Later Supreme Court cases clarified *Eisen*'s *dicta*.

B. Later Supreme Court Decisions Clarify *Eisen*

Subsequent Supreme Court decisions have made it clear that *Eisen* does not stand for the proposition plaintiffs' counsel often advance – *Eisen* does not construct a wall between merits analysis and class certification analysis. In *Coopers & Lybrand v. Livesay*, 437 U.S. 463 (1978), the United States Supreme Court held that:

> "Evaluation of many of the questions entering into determination of class action questions is intimately involved with the merits of the claims. The typicality of the representatives' claims or defenses, the adequacy of the representative, and the presence of common questions of law or fact are obvious examples. The more complex determinations required in Rule 23(b)(3) class actions entail even greater entanglement with the merits."

437 U.S. at 469.

Four years later in *General Tel. Co. of Southwest v. Falcon*, 457 U.S. 147 (1982), the United States Supreme Court further clarified the relation between plaintiff's proof and class certification analysis in the context of Fed. R. Civ. P. 23(a)'s adequacy requirement:

> "Sometimes the issues are plain enough from the pleadings to determine whether the interests of the absent parties are fairly encompassed within the named plaintiff's claim, and sometimes it may be necessary for the court to probe behind the pleadings before coming to rest on the certification question. . . . [A]ctual, not presumed conformance with Rule 23(a) remains . . . indispensable . . . [A] Title VII class action, like any

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Many plaintiffs' counsel, and even some courts, have wrongly accepted the proposition that courts must assume for purposes of class certification analysis that whatever allegations and averments plaintiffs make are true, without any analysis of whether there is actually any factual support for such allegations and averments.

In contrast to a 12(b)(6) motion, which strictly tests the legal sufficiency of a pleading, a motion for class certification tests both the legal and factual sufficiency of a claim. Thus, the court should consider whatever facts are relevant to the issue of class certification.

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> other class action, may only be certified if the trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied."

457 U.S. at 160. Subsequent cases have confirmed that the Supreme Court's reasoning applies with equal force to class certification questions concerning other aspects of Rule 23 as well.

C. The Seventh Circuit Rejects the *Eisen* Rule

In *Szabo v. Bridgeport Machines, Inc.*, 249 F.3d 672 (7th Cir. 2001), the Seventh Circuit rejected the proposition that *Eisen* requires a court to certify a class based solely on the bare allegations in the pleadings. *Id.* at 675-76. In this fraud and breach-of-warranty action, the district court refused to consider the defendant's uncontroverted evidence that the elements for class certification were not met. *Id.* at 674.

The Seventh Circuit vacated the order certifying the class, based on its consideration of evidence that illustrated "[n]agging issues of choice of law, commonality, and manageability." *Id.* at 677. The Seventh Circuit reasoned that, unlike Rule 12(b)(6) motions, a court ruling upon a motion for class certification need not accept the allegations in the complaint as true. *Id.* at 675-76. The court said that in contrast to a 12(b)(6) motion, which strictly tests the legal sufficiency of a pleading, a motion for class certification tests both the legal and factual sufficiency of a claim. *Id.* The order certifying a class or denying certification becomes the court's "last word" on the issue. *Id.* Thus, the court should consider whatever facts are relevant to the issue of class certification. *Id.*

The court then analogized class certification with determinations of venue, *forum non conveniens*, and amount in controversy for diversity jurisdiction. *Id.* at 676. Courts routinely look to the merits of a case to resolve disputed issues of jurisdiction and venue before allowing a case to proceed. *Id.* at 676-77. The court said because these other 12(b) motions are not governed by the 12(b)(6) requirement that the court accept the plaintiff' pleadings at face value, there is no reason to extend such a requirement to class certification. *Id.* at 677. Additionally, the court reasoned that *Eisen*, *Falcon*, and the 1966 amendments to Rule 23 dictate that a district court must "probe beyond the pleadings" in order to determine whether the plaintiffs are able to satisfy the Rule 23 certification requirements. *Szabo*, 249 F.3d at 677.

The Seventh Circuit in *Szabo* interpreted *General Telephone* to hold that similarity of claims must be demonstrated rather than assumed. *Szabo*, 249 F.3d at 677. Further, the Seventh Circuit reasoned that accepting the allegations in the pleadings as true places unfair power in the hands of plaintiffs' attorneys. *Id.* If courts were to blindly accept such allegations, plaintiffs' attorneys could use the pleadings in ways injurious to some members of the class or the defendants. *Id.* Therefore, the court held, defendants as well as absent class members are entitled to an independent judicial review of plaintiffs' allegations. *Id.*

D. The Majority of Circuits Now Recognize the Limits of *Eisen*

Szabo's rejection of the *Eisen* rule has been followed in over 30 decisions within the Seventh Circuit. *See* Linda Mullenix, *Inroads on 'Eisen'*, Nat'l Law J., Sept. 22, 2003 at 13. Moreover, the First, Third and Fourth Circuit Court of Appeals and the United States Court of Federal Claims have adopted *Szabo*'s approach to class certification. *Id.*

The Third Circuit adopted *Szabo* outright, reasoning that in light of the Supreme Court's apparent rejection of *Eisen*, and the Seventh Circuit's arguments in *Szabo*, it had the discretion to conduct preliminary inquiry into the merits to determine whether the alleged claims would be properly resolved in a class action. *Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 259 F.3d 154, 168 (3d Cir. 2001). The United States Court of Federal Claims shortly thereafter issued *Christopher Village, LP v. U.S.*, 50 Fed. Cl. 635, 643 (Fed. Fl. 2001) (denying class certification on grounds that the plaintiffs did not present evidence beyond the pleadings sufficient to refute the government's evidence).

In *Tardiff v. Knox County*, 365 F.3d 1 (1st Cir. 2004), the First Circuit concluded that when faced with the issue of accepting the complaint's factual allegations as true or attempting to resolve disputed contentions during the class certification process, the court should opt for the latter. The court noted that "it is sometimes taken for granted that the complaint's allegations are necessarily controlling; but class action machinery is expensive and in our view the court has the power to test disputed premises early on if and when the class action would be proper on one premise but not another." *Id.* at *4 (noting the split between the Second and Tenth Circuits (discouraging any preliminary inquiry) and the Third and Seventh Circuits (allowing such an inquiry)).

Most recently, in *Gariety v. Grant Thornton LLP*, 368 F.3d 356 (4th Cir. 2004), the Fourth Circuit held that the district court erred when it refused to look beyond the plaintiff's complaint before deciding that common questions of law or fact predominated over individual issues in a securities fraud case. The court explained that "the district court's reliance on mere assertions did not fulfill the requirement that the district court take a 'close look' at relevant matters, conduct a 'rigorous analysis,'

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and make findings in determining whether the plaintiffs had demonstrated that the requirements of Rule 23(b)(3) have been satisfied." *Id.* at 359.

In addition to courts that have explicitly adopted *Szabo*, the Fifth and Eleventh Circuits seem to have indicated that it is appropriate to consider evidence outside the plaintiffs' pleadings to determine whether Rule 23's requirements are met. *See Castano v. American Tobacco Co.*, 84 F.3d 734, 744 (5th Cir. 1996) ("going beyond the pleadings is necessary, as the court must understand the claims, defenses, relevant facts and applicable substantive law in order to make a meaningful determination of the certification issues"); *Rutstein v. Avis Rent-A-Car Sys., Inc.*, 211 F.3d 1228, 1234 (11th Cir. 2000) (same).

The Ninth Circuit has issued seemingly conflicting decisions on the subject. *Compare In re Coordinated Pretrial Proceedings in Petroleum Prods. Antitrust Litig.*, 691 F.2d 1335, 1342 (9th Cir. 1982) (district court is bound to take the substantive allegations of the complaint as true), with *Hanon v. Dataproducts Corp.*, 976 F.2d 497, 509 (9th Cir. 1992) ("we are at liberty to consider evidence which goes to the requirements of Rule 23 even though the evidence may also relate to the underlying merits of the case" (quotations and citations omitted)).

Although the Eighth Circuit has not specifically addressed this issue, two district courts in the Eighth Circuit have adopted *Szabo*. *See Sample v. Monsanto Co.*, 218 F.R.D. 644, 647-48 (E.D. Mo. 2003); *Sanft v. Winnebago Indust., Inc.*, 214 F.R.D. 514 (N.D. Iowa 2003). In *Sample*, the district court denied class certification for a group of corn and soybean farmers who alleged seed companies had engaged in a price-fixing conspiracy in violation of the Sherman Anti-trust Act. *Id.* at 646. The court whole-heartedly adopted *Szabo's* approach to class certification *Id.* at 647-48. The court relied on *Falcon* for the proposition that a court must conduct a "rigorous analysis" to ensure Rule 23 requirements are met. *Id.* at 647. *Sample* also relied on *Winnebago* in its decision to adopt *Szabo*. *Sample* 218 F.R.D. at 647. In *Winnebago*, the court summarily dismissed the line of cases that maintain a court must accept the allegations in the pleadings as true. *Winnebago* at 519, n.3 (collecting cases).

It appears that only the Second, Sixth, and Tenth Circuits explicitly hold that the allegations in plaintiffs' complaint are controlling at the class certification stage. *See Caridad v. Metro-North Commuter R.R.*, 191 F.3d 283, 291-93 (2d Cir. 1999); *Reeb v. Ohio Dep't. of Rehab and Corr.*, 2003 WL 22734623 (6th Cir. 2003); *J.B. ex rel. Hart v. Valdez*, 186 F.3d 1280, 1290 n.7 (10th Cir. 1999).

E. *Dragon v. Vanguard Industries, Inc.*

In *Dragon v. Vanguard Industries, Inc.*, 277 Kan. 776, 89 P.3d 908 (Kan. 2004), the Kansas Supreme Court reversed a trial court certification of a nationwide class of property owners whose properties contained certain polybutylene pipe. Defendants contended that the trial court failed to conduct a rigorous analysis and resolve certain fact issues before certifying the class. Plaintiffs advocated, among other things, that trial courts must accept the allegations in the complaint as true for class certification and may not inquire into the merits.

The Kansas Supreme Court sided with the defendants and held that the trial court must give careful consideration to, and conduct "a rigorous analysis" of, the prerequisites imposed by the Kansas class action rule, K.S.A. 2003 Supp. 60-223. The court first noted that it has traditionally followed the federal courts' interpretation of the federal class certification rule in interpreting K.S.A. 60-223. 277 Kan. at 778. Relying upon *General Telephone* and *Szabo*, the court then rejected plaintiffs' contention that the court should make the class certification decision based solely upon the basis of the allegations contained in the pleadings. 277 Kan. at 781-83.

The court found that plaintiffs had the obligation to present proper evidence in support of certification pursuant to K.S.A. 2003 Supp. 60-243(d). 277 Kan. at 783. The court explained that the trial court should consider evidence when submitted by the parties and "make those factual determinations necessary to a determination of whether the prerequisites for class action are met." *Id.*

The defendants had submitted affidavits and deposition testimony to the trial court relating to the number of states where the product was sold, among other things. The defendants contended that Kansas' choice-of-law rules would implicate the laws of numerous states, making class certification inappropriate. *Id.* at 784. The trial court did not resolve the factual issue of the number and identity of possible states at issue, however, finding it premature to determine whether Kansas law would govern the entire class or whether other states' laws may be applicable. 277 Kan. at 786.

Plaintiffs presented several arguments to the Kansas Supreme Court as to why the trial court could certify a class without analyzing the impact of the choice-of-law issue. First, plaintiffs noted that class certification was subject to modification. The court noted that while this was true, the provisional nature of class certification "does not lessen the movant's burden of establishing that the prerequisites for certification are met." 277 Kan. at 787. Additionally, plaintiffs cited to the

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In Dragon v. Vanguard Industries, Inc., 277 Kan. 776, 89 P.3d 908 (Kan. 2004), the Kansas Supreme Court held that the trial court should consider evidence when submitted by the parties and "make those factual determinations necessary to a determination of whether the prerequisites for class action are met."

The Kansas Supreme Court joined the growing trend of courts recognizing the impossibility of making sensible class certification decisions without looking to those underlying facts that relate to the class certification analysis.

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trial court's reliance on Kansas' long history of certified class actions. The Supreme Court noted, however, that nothing in these decisions deviates from the statement in *Shutts' Executor v. Phillips Petroleum Co.*, 222 Kan. 527, 557, 567 P.2d 1292 (1977), *cert. denied* 434 U.S. 1068 (1978), cautioning a trial court to consider "any possible conflict of law problems" because class prerequisites could be defeated when liability is to be determined according to varying and inconsistent state laws. *Dragon*, 277 Kan. at 788.

The court found that because these issues were not developed in the record "before us and were not analyzed by the trial court, we can not determine the validity of plaintiffs' argument or determine which state's or states' laws apply in this case." 277 Kan. at 791. The court concluded, however, that the trial court erred in not considering the choice of law issues, and held that the plaintiffs had the burden to show that "there are no significant differences in the various states' law or, if there are variations, that they can be managed by the trial court." 277 Kan. at 792. The court therefore remanded the case for consideration of the choice-of-law issue and the impact upon the prerequisites imposed by K.S.A. 2003 Supp. 60-223.

F. Conclusion:

Dragon v. Vanguard Industries, Inc., put a well-deserved end to the so-called *Eisen* rule in Kansas. In doing so, the Kansas Supreme Court joined the growing trend of courts recognizing the impossibility of making sensible class certification decisions without looking to those underlying facts that relate to the class certification analysis. The court also clarified class certification standards in Kansas, particularly with respect to proposed nationwide or multistate classes.

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1. See *General Telephone Co. of Southwest v. Falcon*, 457 U.S. 147, 161 (1982).

2. See *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 177-78 (1974).