IN THE COURT OF APPEALS OF THE STATE OF NEW MEXICO

HARLEY JOHN, and
CHRISTINA PARKETT,

Plaintiffs/Appellees,

vs. N.M. Ct. App. No. 34,561

THE REHABILITATION CENTER
OF ALBUQUERQUE, LLC, CATHY CORREA,
and SKILLED HEALTHCARE, LLC,

Defendants/Appellants,

and

THE STATE OF NEW MEXICO,
NEW MEXICO DEPARTMENT OF
TRANSPORTATION,

Defendant.

Appeal from the First Judicial District
Santa Fe County, New Mexico
The Honorable Sarah M. Singleton

BRIEF IN CHIEF

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Overview

In recent years there has been no shortage of cases involving efforts to enforce arbitration agreements between nursing homes and their residents. This case seems to be the one in which the district court reached its limit of them. Statements the court made in a memorandum decision which underlies the order that gave rise to this appeal convey that understanding. (E.g., RP 211 ("This . . . concerns yet another nursing home contract which provides that the nursing home and the resident agree to arbitrate all disputed claims. This [a]greement contains an escape clause similar or identical to those found in other such [a]greements[.]"); id. at 212 ("Given [the] overwhelming authority against it[s] position, the [c]ourt is hard-pressed to understand Defendant's insistence that the clause should be enforced."); id. ("Despite the [c]ourt's belief that Defendant's position appears to be without precedential support, the [c]ourt will nevertheless review Defendant's argument[s]."). Whether it was because of the court's dim outlook on Appellants' arguments or its actual misapprehension of the law supporting them, it is fair to say that the court did not give the arguments the consideration they deserved.

This case is not one and the same as others that have come before it. There is a threshold question of whether Appellees waived the substantive unconscionability defense upon which they ultimately prevailed. If that question is not dispositive, this case presents an opportunity to decide whether the federal

preemption principles addressed in THI of New Mexico at Hobbs Center, LLC v. Patton, 741 F.3d 1162 (10th Cir. 2014), nevertheless foreclosed the defense. Finally, if reached, there is the question of whether the district court erred by failing to apply the substantive conscionability principles this Court enunciated in Bargman v. Skilled Healthcare Group, Inc., 2013-NMCA-006, 292 P.3d 42, cert. quashed, 2015-NMCERT-010, ___ P.3d ___. The de novo standard of review that applies to the issues, supra, calls for Defendants' arguments to be considered anew.

The proceedings from which the questions arose began with Appellants' motion to compel arbitration. The district court planned to hold an evidentiary hearing on Appellees' procedural unconscionability defense. Appellees later filed a summary judgment motion in which they argued that arbitration exceptions made the agreement substantively unconscionable as a matter of law. The court agreed. After it filed the memorandum decision in which it ruled against Defendants on the issues, supra, the court filed an order granting Appellees' summary judgment motion and denying Appellants' motion to compel arbitration. The order should be reversed.

Summary of Facts and Proceedings

Harley John was traveling with his wife, Christina Parkett, in a vehicle on a state road when they lost control of the vehicle and it flipped off the road. (RP 3; RP 95.) John suffered a spinal injury which left him a paraplegic. (RP 3.)

Following treatment at a hospital and two rehabilitation centers, John was transferred to a skilled nursing facility, namely, The Rehabilitation Center of Albuquerque, LLC ("RCA"/"Facility"). (RP 94-95.)

Three weeks after he arrived at RCA, John was asked to sign Admission Agreement paperwork. (RP 2, 70-71, 120, 123.) The paperwork included a non-mandatory Arbitration Agreement. (RP 72, 74, 75.) John initialed and signed the Arbitration Agreement. (RP 72-75.)

John remained a resident at RCA for months. (RP 2.) After he left, joined by his wife, John sued RCA, Cathy Correa (RCA's Administrator), and Skilled Healthcare, LLC (collectively, "Defendants" unless otherwise stated).[1] (RP 1-2.) John alleged negligence and negligence per se claims arising out of his care at RCA and his wife alleged a derivative loss of consortium claim. (RP 3-9.)

Waiver of Substantive Unconscionability Issue

Defendants responded to the complaint by moving to compel arbitration of the claims based on the Arbitration Agreement. (RP 63; RP 76.) In the exhibits to their motion, Defendants included a copy of the agreement. (RP 72-75.) The agreement explained that by signing it, the Facility and the Resident agreed to

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[1] John also sued the State of New Mexico and the New Mexico Department of Transportation, alleging that the poor condition of the state road that he and his wife had been traveling on caused the previously-mentioned accident. (RP 1.) Those allegations are not relevant to the issues raised in this appeal. (RP 218, 221-22.) The allegations therefore are not further addressed in this brief.

arbitrate all "Disputes." (RP 72.) That term was defined to include "all disputed claims that the Facility and the Resident may have against each other associated with this Arbitration Agreement, the relationship created by the Admission Agreement and/or the provision of services under the Admission Agreement, including all disputed claims arising out of or related to treatment or services provided by the Facility to Resident, including disputed claims as to whether any services . . . were improperly, negligently or incompetently rendered." (RP 72.)

"Disputes" did not include "claims for monetary damages that fall within the jurisdictional limit of the New Mexico metropolitan, magistrate or other small claims court." (RP 72.) "Disputes" also did not include "claims related to the eviction, transfer or discharge of Resident that are subject to a federal or state administrative hearing process." (RP 72.)

Plaintiffs filed a response brief. (RP 94.) Where they raised unconscionability as a defense against enforcement of the Arbitration Agreement, Plaintiffs laid out the following principles. "A New Mexico court may find that a contract or contractual term is unenforceable because the contract or term is procedurally unconscionable, substantively unconscionable or a combination of both." (RP 96.) "While substantive unconscionability concerns the legality and fairness of the contract terms themselves, procedural unconscionability examines the particular factual circumstances surrounding the formation of the contract[.]"

(RP 96.) "[T]here is no requirement that both [procedural and substantive unconscionability] be present to prove a contract is unconscionable." (RP 96.) In support, Plaintiffs cited Strausberg v. Laurel Healthcare Providers, LLC, 2013-NMSC-032, 304 P.3d 409. (RP 96.)

Afterward, as they had foretold earlier in their response (see RP 95 n.1), Plaintiffs made only procedural unconscionability arguments. (RP 96-98.) In doing so, Plaintiffs relied on a decision by the district court in another case in which the court had ruled that an arbitration agreement was unenforceable based solely on procedural unconscionability. (RP 96-97, 103-08.) Treating the decision as a template and modeling an affidavit from John on it (RP 100-01), Plaintiffs argued that this case was analogous (RP 97-98). Plaintiffs ended their response by reiterating that the court should find the agreement unenforceable "on the basis of procedural unconscionability." (RP 98.)

Defendants replied. (RP 110.) After pointing out that Plaintiffs had not argued that the Arbitration Agreement was substantively unconscionable (RP 113 n.2), Defendants focused solely on addressing Plaintiff's procedural unconscionability arguments (RP 113-24).

Following the completion of briefing (RP 125-26), the district court and the parties agreed on a discovery plan with an eye toward holding an evidentiary hearing on any issues regarding the enforceability of the Arbitration Agreement

before the court ruled on the motion. (See RP 138-41; RP 142-44.) In the order that it entered addressing those matters, the court set a status conference to clarify how much time the parties would need to present evidence "on the issue of procedural unconscionability." (RP 143.)

A little over two months later, when the first status hearing took place to talk about the discovery and scheduling the evidentiary hearing (RP 143, ¶ 4), Defendants sought to confirm that Plaintiffs did not intend to rely on a substantive unconscionability defense in challenging the enforceability of the Arbitration Agreement. To that end, the following exchanges took place:

> [Defense counsel]: I believe the issue that we're going to be dealing with at an evidentiary hearing is going to be procedural unconscionability as opposed to substantive unconscionability . . . . I just wanted to . . . confirm that it is just procedural unconscionability.
>
> [Plaintiffs' counsel]: Sure.
>
> Court: You can confirm --
>
> [Plaintiffs' counsel]: I can agree with that.
>
> Court: You can confirm that?
>
> [Plaintiffs' counsel]: I can.
>
> Court: Okay.

(Tr. 7/1/14 at 12:13:34-12:14:03.)

Consequently, it came as a surprise when, nearly a year into their efforts to enforce the Arbitration Agreement (RP 63), Defendants found themselves facing a motion for summary judgment in which Plaintiffs argued that the Arbitration Agreement was unenforceable on the basis of substantive unconscionability (RP 157). Plaintiffs based their substantive unconscionability argument upon the arbitration exceptions. (See RP 158, RP 161-64.) In arguing that the exceptions made the agreement unreasonably and unfairly one-sided and, as such, substantively unconscionable as a matter of law, Plaintiffs primarily relied on a nearly unbroken line of opinions involving similar nursing home arbitration agreements, beginning with Figueroa v. THI of New Mexico at Casa Arena Blanca, LLC, 2013-NMCA-077, 306 P.3d 480, and continuing through Cecil v. Skilled Healthcare Group, Inc., No. 32,433, mem. op. (N.M. Ct. App. May 29, 2014) (non-precedential). (RP 160-64.)

In doing so, Plaintiffs cast Bargman v. Skilled Healthcare Group, Inc., 2013-NMCA-006, as an outlier, implying that the Supreme Court had granted review of the opinion for that reason. (RP 162.) In Bargman, this Court agreed with both sides that, as a matter of law, an arbitration exception for discharge proceedings did not provide a basis for finding substantive unconscionability, see id. ¶ 18, and with Defendants that they should be afforded an opportunity to present evidence tending to show that the collections exception at issue did not make the agreement

substantively unconscionable – i.e., unreasonably and unfairly one-sided. See id. ¶¶ 17, 21-24.

At the second status hearing, which took place shortly after Plaintiffs filed their summary judgment motion (RP 155; RP 157), Defendants argued that the district court should disregard the motion because Plaintiffs had waived the issue of substantive unconscionability based both on their response to Defendants' motion to compel arbitration and Plaintiffs' counsel's statements at the first status hearing. (Tr. 9/15/14 at 10:56:37-10:57:29.)

Defense counsel further argued that if the court disagreed, then the evidentiary hearing should held on both the procedural and substantive unconscionability issues. (Tr. 9/15/14 at 10:57:29-10:57:49.) Plaintiffs' counsel, after agreeing that the summary judgment motion had been filed "late," argued that the Figueroa line of cases was dispositive of the motion to compel arbitration analysis as a matter of law. (Tr. 9/15/14 at 10:58:42-10:59:07.) After defense counsel raised the evidentiary holding in Bargman, Plaintiffs' counsel argued that the holding had not been followed in subsequent cases. (Tr. 9/15/14 at 10:59:16-11:00:16.)

In addressing defense counsel, the district court stated that Defendants could pursue their waiver argument. (Tr. 9/15/14 at 11:01:26-11:01:28.) It also indicated that if it decided against them on the waiver issue, it would give them an

evidentiary hearing on Plaintiffs' unconscionability challenge(s) to the agreement. (Tr. 9/15/14 at 11:01:56-11:02:46; 11:02:55-11:02:58.) In doing so, the court indicated that it would rely on the hearing in deciding whether the case should be arbitrated. (Tr. 9/15/14 at 11:02:40-11:02:45.)

In their summary judgment response, Defendants briefed the waiver issue, reiterating both bases that defense counsel had raised during the second status hearing. (RP 179-81.) Plaintiffs, in pertinent part, replied that they had always maintained that the Arbitration Agreement was unconscionable and that their counsel's statements at the first status hearing did not foreclose them from arguing substantive unconscionability because no evidentiary hearing on the issue was necessary given the authority they had cited which showed that the agreement was substantively unconscionable as a matter of law. (RP 193-94.)

In ruling on the issue in its memorandum decision, in pertinent part, the district court stated:

> Defendant argues that Plaintiffs have waived the substantive unconscionability argument. This argument rests on the Plaintiffs' counsel's statement at early hearings that it was relying on procedural unconscionability and not substantive unconscionability. The statement was made in response to a question from the [c]ourt which was asked to elicit information that would allow the [c]ourt to schedule a hearing on the motion. Because the [c]ourt routinely holds hearings on procedural unconscionability but does not routinely hold hearings on substantive unconscionability, the question was intended to enable scheduling not to force Plaintiffs to elect. The response that was given has to be taken within the context of whether a hearing was needed. Plaintiff, like the [c]ourt, believed that no hearing was

> needed on a substantive unconscionability claim of the sort being raised. The Plaintiffs has always contended that the arbitration agreement was unconscionable.

(RP 211, 212-13.) "In addition, no prejudice has been shown from the fact that Plaintiffs have urged both forms of unconscionability." (RP 213.)

Federal Preemption Issue

In the event that the district court ruled against them on the waiver issue, supra, relying on THI of New Mexico at Hobbs Center, LLC v. Patton, 741 F.3d 1162 (10th Cir. 2014), Defendants argued that the Federal Arbitration Act ("FAA") preempted the New Mexico substantive unconscionability law upon which Plaintiffs had predicated their substantive unconscionability defense. (RP 181-85; see also RP 184 n.3, RP 188-89 (Defendants laid legal and factual foundation regarding applicability of FAA to the Arbitration Agreement).) Plaintiffs replied that Defendants' reliance on Patton was misplaced because the Tenth Circuit's analysis was not binding on a New Mexico state court and New Mexico substantive unconscionability law was controlling instead. (RP 197-98; see also RP 197-98 (Plaintiffs did not challenge applicability of FAA to the Arbitration Agreement).)

In ruling on the issue in its memorandum decision, the district court stated:

> Defendant's next argument against application of controlling New Mexico precedent is that the Tenth Circuit has rejected the idea that such clauses are unconscionable. THI of New Mexico at Hobbs Center, LLC v. Patton, 741 F.3d 1162 (10th Cir. 2014). This Court is

> not bound by Patton. See Sundial Press v. City of Albuquerque, 1992-NMCA-068, ¶ 8, 114 N.M. 236[.] On the other hand, this [c]ourt is bound by the decisions of the New Mexico appellate courts. See State ex rel. Martinez v. City of Las Vegas, 2004-NMSC-009, ¶ 21, 135 N.M. 375[.]

(RP 213-14) (case parentheticals omitted).

Substantive Conscionability Issue

Plaintiffs' summary judgment motion was predicated on the idea that the arbitration exceptions made the Arbitration Agreement substantively unconscionable as a matter of law pursuant to New Mexico precedent. (RP 157-64.) Included among the cases cited in support of that proposition was Cecil which Plaintiffs pointed out involved the same arbitration exceptions as in this case. (RP 163.) In their response, Defendants invoked Bargman for the proposition that they should be afforded an opportunity at an evidentiary hearing to make a showing that the small claims exception did not make the Arbitration Agreement unreasonably and unfairly one-sided. (RP 185.) To that end, Defendants relied on an affidavit which explained that the facility had never filed a lawsuit against a resident and that if in the future the facility considered pursuing a claim against a resident for $10,000 or less, unless it could litigate the claim in court, it likely would forgo trying to recover the amount owed because under the terms of the Arbitration Agreement it would be cost-prohibitive to arbitrate such a claim. (RP 186, 188-91.)

In replying, Plaintiffs clustered Bargman with other cases in which arbitration agreements had been found substantively unconscionable as a matter of law (RP 194) and argued that the evidentiary holding in Bargman had been overruled by the Strausberg trilogy (RP 198-200).[2] That is to say, Plaintiffs read the Supreme Court's holding that a plaintiff bears the burden of proof on unconscionability to mean that once the plaintiff meets that burden, the arbitration agreement becomes unenforceable as a matter of law. (RP 198-200.)

In ruling on the issue in its memorandum decision, the district court stated:

> Defendant's third reason for arguing against the grant of summary judgment is that it wishes to have a hearing to present evidence that is set forth in its brief. This evidence is strikingly similar to the argument that was put forth in Cecil. While it is true that the court noted that no evidence had been presented, it is also true that the clause as written gives Defendant the right to choose litigation if it wishes in its most likely type of claims while requiring Plaintiffs to arbitrate their most likely types of claims. Whether or not Defendant decides to bring suit does not do away with this inequality.

(RP 214.)

Outcome of Proceedings

Based on its rulings in its memorandum decision, the district court entered an order granting Plaintiffs' summary judgment motion and denying Defendants'

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[2] "Strausberg trilogy" denotes: Strausberg v. Laurel Healthcare Providers, LLC, 2012-NMCA-006, 269 P.3d 914 ("Strausberg I"); 2013-NMSC-032, 304 P.3d 409 ("Strausberg II"); and No. 29,238, mem. op. (N.M. Ct. App. Sept. 11, 2013) ("Strausberg III").

motion to compel arbitration. (RP 215-16.) Defendants timely appealed from the order. (RP 218.)

Argument

1. The District Court Erred in Ruling that Plaintiffs Had Not Waived Their Substantive Unconscionability Defense and that Defendants Were Not Prejudiced As a Result.

Standard of Review: Where the facts underlying a waiver issue are not in dispute or are clearly established, "waiver is a question of law subject to de novo review." Palenick v. City of Rio Rancho, 2013-NMSC-029, ¶¶ 8-9, 306 P.3d 447; see also id. ¶ 9 ("When a party is challenging a legal conclusion, the standard for review is whether the law correctly was applied to the facts[.]" (internal quotation marks, alteration & case citation omitted)).

Preservation: The following arguments were preserved by the motion to compel arbitration briefing, the status hearings, the summary judgment briefing, and the district court's memorandum decision on the issue. Supra pp. 3-10.

Bringing the procedural record to bear upon the district court's analysis of the substantive unconscionability waiver issue shows that the court did not accurately depict or correctly apprehend Defendants' arguments and the parts of the record supporting them. The record also shows that the court further erred in deciding that Defendants were not prejudiced by Plaintiffs' substantive unconscionability defense.

In analyzing the waiver issue, the district court disregarded Defendants' argument, despite their having made it twice, that Plaintiffs had waived the defense of substantive unconscionability by not arguing it in their response to Defendants' motion to compel arbitration. (9/15/14 Tr. at 10:56:37-10:57:29; RP 179-81; cf. RP 212-13.) Plaintiffs' response was integral to understanding why Defendants' waiver argument had merit. The response alone provided a basis for finding waiver. See Talley v. Sec. Serv. Corp., 1983-NMSC-046, ¶ 18, 99 N.M. 702 (The elements constituting waiver are "an existing right; knowledge of such right; and an intention to relinquish or surrender it." (internal quotation marks & citation omitted)); Cooper v. Albuquerque City Comm'n, 1974-NMSC-006, ¶ 28, 85 N.M. 786 ("[T]he act of waiver may be evidenced by conduct as well as by express words.").

To begin with, Plaintiffs' response shows that they had the right to argue that the Arbitration Agreement was unenforceable based on substantive unconscionability, Plaintiffs knew it, and Plaintiffs chose not to argue the defense. Supra pp. 4-5. Having relied on the Supreme Court's opinion in Strausberg, see id., and operating within a Rule 1-007.1 NMRA procedural framework, Plaintiffs must have known that if they intended to argue substantive unconscionability it was their burden to do so, see 2013-NMSC-032, ¶¶ 36-39, in their response. See id. ¶ 43 ("[O]nce the party who seeks to compel arbitration has satisfied the initial

burden of proving the formation of a valid contract, . . . the burden shifts to the party opposing arbitration to demonstrate that an affirmative defense, such as unconscionability, renders the contract unenforceable."); see also Rule 1-007.1 (under the rule, the response provides the non-movant's only opportunity to brief counterarguments or defenses); State v. Flores, 2015-NMCA-002, ¶ 17, 340 P.3d 622 (It is a party's responsibility to set forth a developed argument; a court has no duty to review an argument that is not adequately developed or to guess at what the argument might be or what the party intended.), cert. quashed, 2015-NMCERT-090, ___ P.3d ___.

Plaintiffs unquestionably had the means to argue substantive unconscionability. The Arbitration Agreement containing the arbitration exceptions was attached to Defendants' underlying motion, supra p. 3, and there was favorable case law in which this Court had held that analogous arbitration exceptions made arbitration agreements substantively unconscionable and, as such, unenforceable. E.g., Figueroa v. THI of N.M. at Casa Arena Blanca, LLC, 2013-NMCA-077, 306 P.3d 480; Ruppelt v. Laurel Healthcare Providers, LLC, 2013-NMCA-014, 293 P.3d 902.

The logical inference to draw is that Plaintiffs intentionally chose to forgo arguing the defense of substantive unconscionability. From the procedural unconscionability arguments that they chose to develop, it appears that Plaintiffs

were confident that the district court would simply replicate its procedural unconscionability decision in another case in this case. Supra pp. 4-5. Had they been considered, the preceding considerations were enough to find that in filing the response that they did, Plaintiffs intentionally waived the defense of substantive unconscionability. Supra Talley, Cooper.

The district court did consider Defendants' argument that Plaintiffs had waived the defense based on Plaintiff's counsel's statements. Supra pp. 9-10. But in rejecting the argument the court conflated the two status hearings and mischaracterized what was said during them.

Defendants' waiver argument related to Plaintiffs' counsel's statements during the first of the two status hearings. Supra pp. 8, 9. In an abundance of caution, Defendants sought to confirm their understanding, based on Plaintiffs' response brief, supra pp. 4-5, that Plaintiffs did not intend to argue that the Arbitration Agreement was unenforceable based on substantive unconscionability, supra pp. 5, 6. When Plaintiffs' counsel affirmatively represented that Plaintiffs were not going to address substantive unconscionability at the evidentiary hearing, supra p. 6, Defendants were completely justified in concluding that Plaintiffs had decided to waive the defense. At the time, the parties had agreed to undertake discovery in working toward an evidentiary hearing which the district court would use in deciding whether to grant Defendants' motion to compel arbitration. Supra

pp. 5-6. If, after the hearing, the court decided to grant the motion, that decision would spell the end of the litigation against Defendants. (Cf. RP 1-9 with RP 72.) Consequently, if Plaintiffs were going to rely on substantive unconscionability, that was the time to say so.

In reasoning differently in its memorandum decision, the district court created the impression that the exchange between itself and Plaintiffs' counsel depicted in its analysis took place at a time when Plaintiffs had made a substantive unconscionability argument. Supra pp. 9-10. But that was not so.

What the audio recordings of the two status hearings, supra, reveal is that the only time Plaintiffs' counsel stated that Plaintiffs would not be relying on the defense of substantive unconscionability was during the first status hearing on July 1, 2014. Supra p. 6. At that point, Plaintiffs had argued only that the Arbitration Agreement was procedurally unconscionable and Plaintiffs' counsel had affirmatively represented that Plaintiffs would not address substantive unconscionability at the evidentiary hearing. Supra pp. 4-5, 6.

When the exchange between Plaintiffs' counsel and the district court regarding substantive unconscionability took place during the second status hearing, the exchange was not as the court recounted it. Plaintiffs' counsel did argue that no evidentiary hearing was needed to decide whether the Arbitration Agreement was substantively unconscionable. (Tr. 9/15/14 at 11:00:19-11:00:35.)

However, in response, the court did not express the view that, if the court concluded that Plaintiffs had not waived the defense, no evidentiary hearing on substantive unconscionability would be needed to decide the issue. Supra pp. 8-9. To the contrary, after the hearing, the court entered an order indicating that if it rejected Defendants' waiver argument, an evidentiary hearing on the substantive unconscionability issue would occur. (RP 169-70.)

As for the court's remark that Plaintiffs always had contended that the Arbitration Agreement was unconscionable, supra p. 10, the court was literally correct. But that does not mean that Plaintiffs did not waive the defense of substantive unconscionability, at the very latest, by the end of the first status hearing. After all, an argument has to be developed for a court to consider it. Supra p. 15 (Flores); see also Flores, 2015-NMCA-002, ¶ 17 ("This Court will not rule on an inadequately-briefed issue where doing so would require this Court to develop the arguments itself, effectively performing the parties' work for them." (internal quotation marks & citation omitted)). Moreover, it would be inimical to "the just, speedy and inexpensive determination" of proceedings, Rule 1-001 NMRA, especially when arbitration is at issue, to let a party unveil defenses sequentially and several months apart from each another when the party later rethinks its original strategy and decides it wants to front a different defense that it always knew was available to it but that it had chosen not to develop earlier. If

that was an option, it becomes difficult to conceive of a scenario in which a party could be said to have waived an argument during the course of district court proceedings.

Moreover, the district court's rationale that Defendants were not prejudiced by Plaintiffs' substantive unconscionability argument, see supra p. 10, is wrong. During the second status hearing, in the event that the court rejected their waiver argument, Defendants invoked Bargman in asking the court to hold an evidentiary hearing on substantive unconscionability to ensure that they would have a fuller opportunity to make a substantive conscionability showing regarding the small claims arbitration exception, supra p. 8. At the time, the court seemed committed to holding such a hearing. Supra pp. 8-9. Subsequently, however, it appears that based on their substantive unconscionability briefing (RP 157-65; RP 193-201), Plaintiffs succeeded in persuading the court that no such hearing was needed because the arbitration exception made the agreement substantively unconscionable as a matter of law, supra pp. 9-10. Plaintiffs' view of the law, upon which the court's analysis turned, was incorrect. Infra Issue 3.

Defendants therefore did suffer prejudice. Not only were they not afforded the evidentiary hearing that might have changed the outcome, but also the district court ruled against them on based upon its misapprehension of the law applicable

under the circumstances. The court erred in concluding differently and should be reversed.

2. The District Court Erred in Ruling that Plaintiffs' Substantive Unconscionability Defense Was Not Preempted Under Federal Law.

Standard of Review: "[F]ederal preemption is a legal question, which is reviewed de novo." Hadrych v. Hadrych, 2007-NMCA-001, ¶ 5, 140 N.M. 829.

Preservation: The following arguments were preserved by the parties' briefing regarding Patton and the district court's memorandum decision on the issue. Supra pp. 10-11.

The district court's analysis of Defendants' argument regarding THI of New Mexico at Hobbs Center, LLC v. Patton, 741 F.3d 1162 (10th Cir. 2014), does not accurately depict the argument nor correctly apprehend the "controlling" law. Supra pp. 10-11. Defendants' argument did not pose the question of whether the Tenth Circuit's views on a matter of New Mexico law were binding. (Cf. RP 213 (citing Sundial Press).) Instead, the question posed was whether under federal law the FAA preempts what the Tenth Circuit dubbed "the Figueroa rule," 741 F.3d at 1168, based on a line of reasoning not previously addressed by New Mexico's appellate courts. (Cf. RP 213-14 (citing State ex rel. Martinez).) The errors in the district court's analytical approach explain why it arrived at the wrong answer.

In referring to "controlling New Mexico precedent" the district court did not specify which cases it had in mind. (RP 213.) Defendants assume the court was referring to the appellate cases it cited in its memorandum decision. (RP 212.) Out of them, Figueroa was the only one in which this Court considered whether the FAA preempted New Mexico law regarding the substantive unconscionability of arbitration exceptions. Cf. Ramirez v. Dawson Prod. Partners, Inc., 2000-NMCA-011, ¶ 10, 128 N.M. 601 (This Court "adhere[s] to the rule that cases are not authority for propositions they do not consider."); City of Sunland Park v. Paseo del Norte Ltd. P'ship, 1999-NMCA-124, ¶ 7, 128 N.M. 163 ("[I]t [therefore] would be a mistake to use an opinion as authority for a proposition not [considered].").

Figueroa expresses the rationale upon which this State's appellate courts previously have relied in rejecting arguments that the FAA preempts New Mexico law regarding the substantive unconscionability of arbitration exceptions. The rationale is based on 9 U.S.C. § 2 of the FAA and case law construing it. Simply put, under Section 2, the doctrine, or more aptly the defense, of substantive unconscionability falls within the domain of state courts provided that the defense is a "generally applicable" one – i.e., not only applicable to arbitration agreements but also to any other contract. Figueroa, 2013-NMCA-077, ¶ 8 (internal quotation marks & citation omitted). Such a defense does not impermissibly "single out

arbitration agreements" or "derive[] [its] meaning from the fact that an agreement to arbitrate is at issue" so as to trigger FAA preemption. Id. (internal quotation marks & citation omitted); cf. id. ("[I]f a state law or judicial doctrine treats arbitration agreements disparately, it is inconsistent with, and preempted by the FAA and cannot be used to render the arbitration agreement unenforceable."). See also Cordova v. World Finance Corp., 2009-NMSC-021, ¶¶ 36-38, 146 N.M. 256; accord Rivera v. Am. Gen. Fin. Servs., Inc., 2011-NMSC-033, ¶¶ 17-18, 150 N.M. 398.

In Patton, the Tenth Circuit disagreed with Figueroa's rationale for avoiding FAA preemption. The Tenth Circuit had before it the same nursing home arbitration agreement as in Figueroa. 741 F.3d at 1164-65. The issue that the Tenth Circuit had to decide was whether the district court had erred in finding the agreement substantively unconscionable based on Figueroa. Id.

In approaching the issue, the Tenth Circuit brought the following principles to bear upon the analysis. "Congress enacted the FAA . . . to overcome judicial hostility to arbitration agreements[.]" 741 F.3d at 1165. "Section 2 is a Congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary[.]" Id. (internal quotation marks & citation omitted). "[T]he FAA rejects the view that arbitration is inferior to court proceedings as a method of deciding

important rights." Id. Therefore, "[a]lthough § 2 permits agreements to arbitrate to be invalidated by generally applicable contract defenses, such as . . . unconscionability, they cannot be invalidated by defenses . . . that derive their meaning from the fact that an agreement to arbitrate is at issue." Id. at 1168 (internal quotation marks, citation omitted & emphasis omitted). "In other words, . . . the FAA preempts . . . state common law – including the law regarding unconscionability" – "that is predicated on the view that arbitration is an inferior means of vindicating rights." Id. at 1167.

In examining Figueroa, the Tenth Circuit observed that this Court had held that the arbitration agreement was "unconscionably unfair to nursing home residents because it permitted THI to litigate its most likely claims against the resident – guardianship, collection, and eviction claims – while requiring arbitration of the resident's most likely claims against the nursing home – personal injury claims and the like." 741 F.3d at 1168. In particular, the Tenth Circuit focused upon the following statement by this Court:

> [W]e refuse to enforce an agreement where the drafter unreasonably reserved the vast majority of his claims for the courts, while subjecting the weaker party to arbitration on essentially all of the claims that party is likely to bring.

Id. (quoting Figueroa, 2013-NMCA-077, ¶ 30). As the Tenth Circuit recognized, by speaking of "subjecting the weaker party to arbitration," this Court "clearly evince[ed] the view that having to arbitrate a claim is disadvantageous." Id. at

1169. Or, more plainly stated, "the alleged unfairness boils down to the residents having to arbitrate, rather than litigate, the claims they are most likely to make." Id. (emphasis omitted).

"The rationale for the state unconscionability rule [thus] runs counter to [United States] Supreme Court precedent." 741 F.3d at 1169. "Common law defenses to an arbitration demand are preempted by the FAA if they derive their meaning from the fact that an agreement to arbitrate is at issue. Id. (internal quotation marks & citation omitted). "The rule of Figueroa derives its meaning from the fact that the agreement is an arbitration agreement because the heart of the asserted unfairness is the disparity in what claims must be arbitrated." Id. (emphasis omitted).

As a result, federal law becomes the "controlling" authority. That result follows because, "[a]lthough § 2's saving clause preserves generally applicable contract defenses, nothing in it suggests an intent to preserve state-law rules that stand as an obstacle to the accomplishment of the FAA's objectives." AT&T Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1748 (2011). Where there is a conflict between state and federal law on a matter of federal law, the latter must prevail. That is a correct statement even though the Tenth Circuit's analysis technically may not be binding on this Court. To rely on such a technicality as the reason not to apply Patton would be to elevate form above substance. United

States Supreme Court precedent undergirds the Tenth Circuit's preemption analysis. See Patton.

This Court itself has acknowledged that it is bound by United States Supreme Court precedent, not to mention federal statutory law, under the Supremacy Clause of the United States Constitution. In Walker v. Maruffi, the Court was faced with resolving an inconsistency between federal and state court decisions over which statute of limitations should apply in a federal civil rights action filed in state court. See 1987-NMCA-048, ¶¶ 3-8, 105 N.M. 763. In rejecting an argument that it was bound to follow an existing New Mexico Supreme Court opinion addressing the issue, this Court recognized that the choice of the appropriate statute of limitations was a matter of federal, not state, law and that under the Supremacy Clause this Court therefore was bound to follow United States Supreme Court precedent affecting federal law. See id. ¶¶ 13-14; see also id. ¶¶ 15-21 (in determining appropriate limitations period Supreme Court was guided by public policy objective of the underlying federal statute). Additionally, this Court recognized that the New Mexico Supreme Court had yet to address which statute of limitations was applicable as a matter of federal law, meaning that an earlier decision that the Supreme Court had authored was not controlling precedent on the issue. Id. ¶¶ 24-25.

So it can be said in this case. To date, the only opinion in New Mexico in which Patton is mentioned is one from this Court. In Dalton v. Santander Consumer USA, Inc. this Court declined to address the impact of Patton on New Mexico's substantive unconscionability law regarding arbitration exceptions. See 2015-NMCA-030, ¶ 30, 345 P.3d 1086, cert. granted, 2015-NMCERT-003, 346 P.3d 1163. In doing so, the Court stated that it was bound by Rivera in which the New Mexico Supreme Court had expressly rejected the defendant's FAA preemption argument regarding a UCC arbitration exception which the Supreme Court decided was substantively unconscionable. Id.

The same thing cannot be said in this case. The New Mexico Supreme Court has not yet addressed the Patton preemption analysis. There is, then, no binding authority which forecloses this Court from deciding that the district court erred in rejecting Defendants' Patton preemption argument – not only with regard to Figueroa but also all of its progeny upon which the district court relied (RP 212). See Deerman v. Bd. of County Comm'rs, 1993-NMCA-123, ¶ 19, 116 N.M. 501 ("We should refrain from construing a decision by the [New Mexico] Supreme Court as resolving issues that are not addressed in the decision."); supra Walker; accord State v. Jones, 2010-NMSC-012, ¶ 39, 148 N.M. 1 (Of two cases cited by a party in support of argument, "neither case expressly considered the . . . issue, and

thus neither can be relied on as authority[.]"). To so conclude would achieve the right result on the FAA preemption issue.

3. The District Court Erred in Ruling that the Arbitration Agreement is Substantively Unconscionable as a Matter of Law Given Defendants' Efforts to Make a Substantive Conscionability Showing.

Standard of Review: This Court "review[s] de novo the denial of a motion to compel arbitration." Bargman, 2013-NMCA-006, ¶ 11. "Whether a contract is unconscionable [also] presents a question of law . . . review[ed] de novo." Id.

Preservation: The following arguments were preserved by the second status hearing, the summary judgment briefing, and the district court's memorandum decision. Supra pp. 11-12.

The district court's analysis of the substantive unconscionability issue does not accurately depict Defendants' argument or correctly apprehend the applicable law. Most obviously, the court makes no mention of Bargman, upon which Defendants premised their argument that they should be afforded an opportunity at an evidentiary hearing to more fully develop the evidence they had presented to show that the small claims arbitration exception does not make the Arbitration Agreement unreasonably or unfairly one-sided. (Cf. RP 185-86 with RP 214.) Instead, perhaps because it involved the same small claims arbitration exception as in this case, the court focused on Cecil. (RP 214.) It is clear that the court read Cecil because, unlike Plaintiffs (RP 163; RP 194; RP 196), the court noted that the

defendants in Cecil had not presented any evidence (RP 214). The court's failure to apprehend the analytical significance of that detail, or evidentiary distinction, explains why the court erred in treating the analytical standard applied in Cecil as dispositive rather than the analytical standard in Bargman.

As between the two cases, Bargman more clearly helps show the error in the district court's analysis. As a result, Defendants begin with an overview of Bargman and the analytical principles that can be derived from it.

Bargman, like earlier substantive unconscionability cases before it (i.e., Cordova; Rivera; Figueroa; Ruppelt), involved an arbitration agreement which included an arbitration exception for the defendants' presumably most likely claims. See 2013-NMCA-006, ¶¶ 14-16, 18. Bargman differed, however, in that the defendants argued that this Court should depart from the earlier cases by applying a different analytical approach to deciding whether the arbitration exception made the agreement substantively unconscionable. In the earlier cases, both the Supreme Court and this Court had held that arbitration exceptions made the arbitration agreements substantively unconscionable – i.e., "unfairly and unreasonably one-sided" – as a matter of law. Cordova, 2009-NMSC-021, ¶ 32 (emphasis added); accord Rivera; Figueroa; Ruppelt. The defendants in Bargman argued that this Court should "recognize[] that the parties' rights do not have to be identical and that courts should entertain evidence tending to show that a particular

[arbitration] exclusion is not unreasonably or unfairly one-sided." 2013-NMCA-006, ¶ 13.

In responding to the argument, the Court framed the appeal as one which required it to resolve, "whether under our Supreme Court cases and this Court's cases,

> (1) there now exists a bright-line, fixed, and inflexible rule that the exception from arbitration of . . . claims . . . most likely to be pursued by the defendant . . . are substantively unconscionable because that exception is unreasonably or unfairly one-sided and against New Mexico public policy"
>
> or
>
> "(2) as the case law stands, the issue is to be analyzed and on a case-by-case basis based on evidence presented on the issues of unreasonableness, unfairness, one-sidedness, and public policy."

Id. ¶ 12.

After recognizing at the outset of its analysis that Rivera, Cordova, Figueroa, and Ruppelt were "controlling New Mexico precedent," Bargman, 2013-NMCA-006, ¶ 12, the Court reviewed and reiterated the substantive unconscionability principles expressed in them. E.g., id. ¶ 14 ("Our Supreme Court [in Rivera] applied the rule that '[c]ontract provisions that unreasonably [and unfairly] benefit one party over another are substantively unconscionable[.]'" (quoting Rivera, 2011-NMSC-033, ¶¶ 46, 54)); id. ¶ 15 ("'While we agree that arbitration obligations do not have to be completely equal, and that parties may freely enter

into reasonable agreements to exempt certain claims from arbitration, we refuse to enforce an agreement where the drafter unreasonably reserved the vast majority of its claims for the courts, while subjecting the weaker party to arbitration on essentially all of the claims that party is likely to bring.'" (quoting Figueroa, 2012-NMCA-012, ¶ 30 (alterations omitted))).

In doing so, the Court arrived at the following insights. "Nothing in [Cordova, Rivera, Figueroa, Ruppelt] expressly lays down a bright-line, inflexible rule that excepting from arbitration any claim most likely to be pursued by the defendant drafter will void the arbitration clause as substantively unconscionable." Bargman, 2013-NMCA-006, ¶ 17. "As our case law stands, cases should still be examined on a case-by-case basis." Id. "It is noteworthy that in none of the foregoing cases did the defendant drafter of the arbitration provision offer evidence tending to prove it was not unreasonable or unfair to except certain claims from arbitration even if they were the claims most likely to be pursued by the defendant." Id.

In other words, the Court recognized that there is room under New Mexico law for a substantive conscionability showing to be made regarding a presumably one-sided arbitration exception – i.e., one that it appears the defendant would be the most likely to invoke. Depending upon the record before it, a court must adjust its analytical approach accordingly.

When the defendant drafter presents evidence to rebut the presumption that an arbitration exception makes an arbitration agreement substantively unconscionable, case-specific analysis must occur. In analyzing the evidence, a court must keep in mind that the parties' "arbitration obligations do not have to be completely equal, and that parties may freely enter into reasonable agreements to exempt certain claims from arbitration[.]" Figueroa, 2013-NMCA-077, ¶ 30. The dispositive consideration is whether the defendant has made a showing that the exception is a reasonable and fair one such that enforcing the agreement would not result in unreasonable and unfair favorability toward the defendant. See Bargman, 2013-NMCA-006, ¶¶ 22-24.

When a defendant does not present such evidence, the presumed one-sidedness of the arbitration exception becomes outcome-determinative as a matter of law. See Ruppelt, 2013-NMCA-014, ¶ 18 ("By excepting disputes pertaining to collections . . . from arbitration, Defendants chose the forum to resolve their disputes that were presumptively deemed to be 'most likely,' while simultaneously forcing Plaintiff . . . to arbitrate her most likely disputes."); id. ¶ 17 ("We do not rule out the possibility that probative evidence could be offered in this type of case."; "Here, however, Defendants declined the suggestion made at oral argument that this Court consider remanding the matter for further factual development

regarding the facial one-sidedness of the exempted claims."); id. ¶ 18 ("As a result, we conclude that the [a]greement is unfair and unreasonably one-sided.").

Read with those principles in mind, Cecil does not depart from them. In Cecil, the Court reiterated that substantive unconscionability must be determined on a case-by-case basis, citing Bargman. Cecil, No. 32,433, ¶ 6. The Court treated the small claims arbitration exception as presumptively one-sided, based on both prior precedent and the plaintiff's unrebutted evidence. Id. ¶¶ 7-9. The Court rejected the defendants' argument that there was a reasonable justification for the exception, i.e., that it would be cost-prohibitive to arbitrate such claims due to their having to pay the arbitrators' fees, because the defendants had not presented any evidence showing that to be so. Id. ¶ 10. In support of its rejection of the defense, the Court quoted the statement from Bargman which indicates that the substantive unconscionability analysis a court must undertake differs depending upon whether evidence has been presented to justify an arbitration exception it appears the defendant is most likely to invoke. Id. In the absence of such evidence, the presumed unreasonableness and unfairness of the arbitration exception became outcome-determinative as a matter of law. See id.

In analyzing this case as it did, supra p. 12, the district court clearly missed the analytical significance of the evidentiary distinction recognized in Bargman and reiterated in Cecil. The district court did recognize that this case was different

from Cecil because Defendants had presented evidence in seeking to justify the small claims exception. Supra p. 12. But the court did not adjust its analytical approach to apply the standard that applies when a defendant presents evidence to justify an arbitration exception. That is, notwithstanding the fact that the terms of the arbitration agreement give the defendant the right to go to court for its likeliest claim(s), does the evidence show, or if more fully developed would it have the potential to show, that the exception nevertheless is reasonable and fair such that enforcement of the agreement would not result in unreasonable and unfair favorability toward the defendant. Supra pp. 30-31. Instead, the court applied the standard that applies when a defendant does not present such evidence. That is, the exception unreasonably and unfairly enables the defendant to go to court for its most likely claim(s) while subjecting the plaintiff to arbitration for his or her most likely claim(s). Supra pp. 31-32. Judged against that standard, the court deemed the evidence insufficient as a matter of law because it did not do away with the perceived inequality between the parties' rights to litigate their most likely claims. Supra p. 12.

It is unclear from the district court's analysis exactly what led the court analytically astray. Perhaps the court did not cite or otherwise pay attention to Bargman in its analysis because it agreed with Plaintiffs that the evidentiary holding in Bargman no longer remained good law. If so, the court thereby erred as

various considerations show.[3] Or perhaps it was the "overwhelming authority" (RP 212) that Plaintiffs cited, which included Bargman, in support of their argument that the most likely claims standard was outcome-determinative as a matter of law (RP 161-63; RP 194). Whatever the cause, the district court clearly misapprehended the analytical standard that applies to the analysis based on Defendants' efforts to make an evidentiary substantive conscionability showing regarding the small claims arbitration exception.

Notably, in Bargman, the Court did not outright reject the type of conscionability showing regarding the arbitration exception that Defendants sought

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[3] To begin with, in Strausberg the Supreme Court did not overrule, let alone, mention Bargman. See generally Strausberg II, 2013-NMSC-032; cf. supra p. 26 (Deerman), and this Court's lack of any mention of the defendants seeking to present evidence on remand seemingly explains why the Court treated the presumed one-sidedness of the arbitration exceptions as outcome-determinative as a matter of law. See generally Strausberg III, No. 29,238 mem. op. In Cecil, which post-dates the Strausberg trilogy, this Court treated Bargman as good law, including the evidentiary distinction made in it. Supra p. 32. Even more clearly, this Court's opinion in Dalton, which post-dated the parties' briefing and escaped the district court's attention before the court analyzed the substantive conscionability issue, validates the previously-discussed alternative analytical approaches, based on Bargman. See Dalton, 2015-NMCA-030, ¶ 27 (Bargman "clarif[ied] that there is no inflexible rule that one-sided clauses are always unreasonable and cannot be reviewed on a case-by-case basis" and "recognize[ed] the right to address the issue of [substantive] unconscionability by presenting evidence regarding the neutral and other legitimate reasons for an [arbitration] exception."); cf. id. ("Defendant's failure to utilize its opportunity to factually rebut the apparent one-sidedness of the carve-out exception to arbitration was of its own choosing and will not be second-guessed on appeal."). Most recently, the Supreme Court quashed its grant of certiorari in Bargman, supra p. 2, eliminating any doubt as to the opinion's status as good law.

to make in this case. That is, the exception should be considered a reasonable and fair one because under the terms of the Arbitration Agreement it would be cost-prohibitive for the facility to arbitrate small claims against residents. See Bargman, 2013-NMCA-006, ¶¶ 22-24. More specifically, if the facility had to arbitrate a claim for $10,000 or less, it would have to pay not only three arbitrators' fees but also those of its own counsel which, in the aggregate, could exceed the amount at issue. (RP 186; RP 189-90.) Faced with that prospect, the facility likely would forgo trying to collect the amount owed, meaning that the facility would be deprived of a remedy for services that it had provided to a resident which remained unpaid. (RP 186; RP 190-91.) Defendants' efforts to more fully make a substantive unconscionability showing at an evidentiary hearing were cut short by the district court's misapprehension of the analytical approach that applies when a party seeks to make a substantive conscionability showing. Supra p. 12. As a result, the court should be reversed on the issue.

Conclusion

For any or all of the reasons stated, the district court's order invalidating the Arbitration Agreement should be reversed and the case should be remanded for further proceedings consistent with any determination(s) this Court makes regarding the issues raised on appeal.

Statement Regarding Oral Argument

Defendants request oral argument. This appeal presents significant issues regarding the propriety of the district court's waiver, federal preemption, and substantive unconscionability determinations. Oral argument will assist the court in understanding and evaluating the positions of the parties and therefore is likely to aid the decisional process.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that a copy of the foregoing response was served by first class mail upon the following counsel of record

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