2003 WL 21212007 (S.C.A.G.)

Office of the Attorney General

State of South Carolina
May 21, 2003

*1 The Honorable James H. Merrill
Member
House of Representatives
308-A Blatt Building
Columbia, South Carolina 29211

Dear Representative Merrill:
Your letter references "a controversy [which] has erupted in the Charleston port community over whether the South Carolina State Ports Authority (SPA) has the unilateral legal authority to terminate a license agreement that was signed in August of 1999 with Charleston International Ports, LLC (CIP). You state that "[t]he license agreement allowed CIP to operate a break bulk cargo business on port facilities at the Charleston Naval Base for a period of thirty (30) years with profits to be shared between CIP and the SPA." By way of background, you further indicate the following:
The SPA alleges that CIP is in violation of the terms of the license agreement and has announced by a vote of the SPA Board that the license agreement has been terminated "for default." CIP denies the allegation of default and argues that the license agreement requires such disputes to be arbitrated according to the terms of the agreement pursuant to the S.C. Code of Laws governing the process of arbitration.

This week SPA made an attempt to seize operations control of the facility. The SPA has written letters to CIP's tenants and cargo customers directing them to begin sending their payments to the SPA. CIP responded by writing letters to the same tenants and customers disputing SPA's unilateral authority to terminate the agreement and asking the tenants and customers to honor their contractual obligations by continuing to send payments to CIP until the dispute is resolved.

These actions have caused the dispute to rise to the level of urgency. Tenants and customers are not caught in the middle of this controversy, and it now threatens to disrupt the orderly business of the port community.

You request an opinion regarding the following legal issues:
1. Does the SPA Board have the legal authority to unilaterally terminate the license agreement for cause between the SPA and CIP without arbitration of differences?

2. If arbitration is required to resolve disputes arising under the agreement, which party has the legal authority to operate the facility until the dispute is resolved?

Limitations of an Opinion of this Office to Resolve Questions of Fact

We begin our analysis by noting one caveat: your questions ultimately involve a contractual dispute between the State Ports Authority and CIP. Thus, final resolution of those questions may well turn upon issues of fact which cannot be determined by an opinion of this Office, but only adjudicated by a court. In a previous opinion of this Office, we expressed the following reservation concerning the difficulties in attempting to resolve contractual disputes through the issuance of an opinion of the Attorney General:

[a] legal opinion cannot resolve such obviously critical questions as precisely what expectations the parties may have had or what reliance was placed upon any representations made ....

*2 Because this Office does not have the authority of a court or other fact-finding body, we are not able, in a legal opinion, to adjudicate or investigate factual questions. Unlike a fact-finding body ... we do not possess the necessary fact-finding authority and resources to adequately determine the difficult factual questions present here.

Op. S.C. Atty. Gen., Op. No. 85-132 (November 15, 1985).

Those same reservations and limitations are present here. Only a court can resolve the issues of fact which may be highly relevant to any final resolution of the question raised by your letter. However, with that caveat in mind and based solely upon the information provided, we will attempt to set forth the applicable law which a court would likely consider.

Contract Between SPA and CIP

You have forwarded the relevant contract between SPA and CIP to this Office. A brief review of the pertinent contractual provisions is thus in order. Stamped at the top of the contract in bold capital letters and underlined is the following statement:
CONFIDENTIAL: This Agreement Is Subject To Arbitration Pursuant to S.C. Code Ann. §§ 15-48-10 et seq. As Modified In This License By The Agreement Of The Parties.

Paragraph 47 of the Agreement deals with arbitration specifically. Such Paragraph broadly provides in pertinent part that [a]ny controversy or dispute arising out of or relating to this License shall be determined by arbitration in Charleston, South Carolina.

If either party elects to commence arbitration, such party (herein called the "petitioner") shall give notice of the controversy to be submitted to arbitration (herein called the "arbitration notice") to the other party (herein called the "respondent") and simultaneously therewith shall select an arbitrator and notify the respondent of his/her identity.

The procedure for the selection of an arbitrator is also set forth in Paragraph 47.

Paragraph 28 of the Agreement addresses "Default by CIP." This provision enumerates a number of grounds for which CIP is deemed to be in default. Among these are the failure to pay any fee owed to SPA; failure to proceed with due diligence to remedy any breach of the License Agreement; abandonment of the premises by CIP; application by CIP for the appointment of a receiver, trustee or liquidator or filing by CIP for bankruptcy; and adjudication of CIP as a bankrupt or as insolvent. Upon default, SPA is granted certain remedies therefor. Among these is the right to "reenter and repossess any or all of the Premises provided, nevertheless, that the SPA shall apply the operating net income from the Premises to the existing debt service, if any, associated with the Premises, equipment, and machinery ...."

Likewise, Paragraph 29 specifies certain grounds for default by SPA. Among these are the failure to proceed with due diligence to remove and remedy any breach, as well as the lapse of 60 days after written notice of any uncured default. Subsection (c) of Paragraph 29 also provides that

> *3 [n]o expiration or termination of the License shall relieve the SPA of any of its liabilities and obligations under this License. Without limiting the generality of the foregoing, the SPA shall be responsible to CIP to the full extent allowed or provided at law for any and all obligations arising prior to such termination.

In addition to the foregoing grounds for termination "for cause" by either side, Subsection 31 affords SPA the right to terminate the License without cause. This Subsection provides as follows:

31. The SPA's Termination Without Cause.

> The SPA may terminate this License without cause. Since CIP's injury associated with termination without cause is impossible or impracticable to compute, the parties will further agree, in writing, to a liquidated damage formula. Such formula, at the minimum, will provide for the SPA's payment of the debt service associated with the Premises, capital improvements at the Premises, equipment, and machinery; and a payment to CIP of an amount equal to the fair market value of CIP's portion of pre-tax net income which would otherwise inure during the balance of the un-terminated relationship, calculated by historical performance between the parties. Fair market value shall be computed using the net present value methodology, and discount rates not exceeding those of comparable duration Treasury Bonds or Treasury Notes.

Finally, Paragraph 27 affords to CIP the right to quiet enjoyment of the property with certain exceptions. Such Paragraph provides as follows:

27. Right of Entry & Quiet Enjoyment. The SPA agrees that CIP, upon compliance with all of the covenants, agreements, and provisions of this License, shall lawfully and quietly license, occupy, and enjoy the Premises during the term hereof without hindrance or molestation. However, the Authority and the SPA and their agents shall be entitled, in a reasonable manner, to enter the Premises during normal business hours:
a. to view, inspect, or market the Premises;

b. to make any alteration, improvement, or repair to the Premises; or

c. for any other purpose relating to the operation, maintenance, or redevelopment of the Premises or of the Charleston Naval Complex.

In an emergency situation, the Authority and the SPA and their agents may enter the Premises at any time.

The SPA and CIP shall conduct periodic joint inspections of the Premises which shall be scheduled by agreement, but which shall be conducted not less frequently than annually.

Law Concerning Arbitration

The public policy of South Carolina is one of strong support for arbitration. In that regard, the State Supreme Court has stated unequivocally that "... [t]his Court favors arbitration of disputes," Bazzle v. Green Tree Financial Corp., 351 S.C. 254, 261, 569 S.E.2d 349 (2002).

This State has adopted the Uniform Arbitration Act. S.C. Code Ann. Sec. 15-48-10 et seq. In order for an arbitration agreement to be enforceable under South Carolina law, § 15-48-10(a) requires that "the notice provision [be] ... typed in underlined capital letters, or rubber-stamped prominently, on the first page of the contract." Zabinski v. Bright Acres Associates, 346 S.C. 580, 587, 553 S.E.2d 110 (2001).

> *4 In addition, we note that the Federal Arbitration Act, 9 U.S.C.A. § 1 et seq. provides that a written provision in any maritime transaction or a contract evidencing a transaction involving commerce

> to settle by arbitration a controversy thereafter arising out of such contract or transaction ... shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

The United States Supreme Court has interpreted the phrase "involving commerce" broadly to mean "affecting commerce" which indicates a Congressional intent to exercise its commerce power in full. Allied v. Bruce Terminix Co. v. Dobson, 513 U.S. 265, 274, 115 S.Ct. 834, 130 L.Ed.2d 753 (1995). To that end, the Court applies a 'commerce in fact" test requiring the transaction to have "in fact" involved interstate commerce. Id.

Parties may agree "to enter into a contract providing for arbitration under rules established by state law rather than rules established by the FAA [Federal Arbitration Act]." Zabinski, id., at 590. However, "[w]hile the parties may agree to enforce arbitration agreements under state rules rather than FAA rules, the FAA will preempt any state law, that completely invalidates the parties' agreement to arbitrate." Zabinski, id., at 592; Volt Info. Scis. Inc. v. Board of Trs., 489 U.S. 468, 109 S.Ct. 1248, 103 L.Ed.2d 488 (1989); Munoz v. Green Tree Fin. Corp., 343 S.C. 531, 542 S.E.2d 360, n. 2 (2001). In Soil Remediation Co. v. Nu-Way Envtl. Inc., 323 S.C. 454, 476 S.E.2d 149 (1996), for example, the South Carolina Supreme Court, in reliance upon Doctor's Assocs. v. Casarotto, 517 U.S. 681, 116 S.Ct. 1652, 134 L.Ed.2d 902 (1996), held that § 15-48-10(a) directly conflicts with Section 2 of the Federal Arbitration Act.

As the Court emphasized in Zabinski, "[t]he policy of the United States and South Carolina is to favor arbitration of disputes." 346 S.C. at 596. While "[a]rbitration is a matter of contract, and a party cannot be required to submit to arbitration any dispute which he has not agreed to submit ...," Zabinski, supra, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration. Towles v. United Healthcare Corp., 338 S.C. 29, 524 S.E.2d 839 (Ct. App. 1999). Furthermore, the public policy designed to promote arbitration is so strong that the State Supreme Court has warned that

> ... unless the Court can say with positive assurance that the arbitration clause is not susceptible to an interpretation that covers the disputes, arbitration should be ordered. ... A motion to compel arbitration made pursuant to an arbitration clause in a written contract should only be denied where the clause is not susceptible to any interpretation which would cover the asserted dispute.

Zabinski, supra, citing Tritech Elec., Inc. v. Frank Miltall & Co., 343 S.C. 396, 540 S.E.2d 864 (Ct. App. 2000); S.C. Pub. Serv. Auth. v. Great Coal., 312 S.C. 559, 437 S.E.2d 22 (1993).

Questions Presented Here

*5 With that background in mind, we turn to the questions presented by your request. We will address each question in turn.

> I. Does the SPA Board have the legal authority to unilaterally terminate the license agreement for cause between SPA and CIP without arbitration of differences?

No. In Paragraph 47, the Agreement makes it clear that "[a]ny controversy or dispute arising out of or relating to this License shall be determined by arbitration in Charleston, South Carolina." In Zabinski, the Supreme Court interpreted almost identical language in a partnership agreement as virtually all-inclusive, commenting as follows:
[t]he arbitration agreement in the instant cases states that "any controversy or claim arising out of the partnership agreement" should be settled by arbitration if it cannot be settled by the partnership. Therefore, any claim pursuant to the partnership agreement is arbitrable. Further, any tort claims between the partners that relate to the partnership

agreement are arbitrable .... Finally, the winding up of the partnership is covered by the arbitration agreement because it concerns issues that are the direct result of the partnership agreement.

346 S.C. at 596.

Your letter indicates that "[t]he SPA alleges that CIP is in violation of the terms of the license agreement and has announced by a vote of the SPA Board that the license agreement has been terminated 'for default.'" You further state that "CIP denies the allegation of default ...." Assuming this characterization of the events, this is the type of dispute which is clearly arbitrable. In light of the fact that the Agreement itself provides that "[a]ny controversy or dispute arising out of or relating to this License Agreement shall be determined by arbitration," and inasmuch as you indicate that the dispute concerns whether or not CIP has breached its agreement, such an issue is patently arbitrable. (emphasis added). Given also the fact that the Supreme Court has stated that any doubt whatsoever must be resolved in favor of arbitration, it is our opinion that the dispute in question is subject to arbitration.

II. If arbitration is required to resolve disputes arising under the agreements, which party has the legal authority to operate the facility until the dispute is resolved?

The answer is CIP. As noted above, Paragraph 28(b)(1) of the Agreement states that any Default which is uncured for 30 days after written notice gives SPA the right to "reenter and repossess any or all of the Premises ...." At the same time, Paragraph 27 states that CIP, upon compliance with "all the covenants, agreements and provisions of this License, shall lawfully and quietly license, occupy, and enjoy the Premises during the term hereof without hindrance of molestation." Again, the apparent central issue surrounding this dispute is whether CIP is in "default" of the Agreement. Both parties have agreed to arbitrate "[a]ny controversy or dispute arising out of or relating to this License ...." Accordingly, as noted above, it is our opinion that the dispute in question is subject to arbitration.

***6** With that in mind, we note that the law in this area strongly favors preservation of the status quo until arbitration can occur. Numerous decisions have concluded that while a court cannot replace the arbitrator by itself deciding issues subject to arbitration, the judiciary does possess authority to issue an injunction to protect the status quo pending arbitration. For example, in Erving v. Virginia Squires Basketball Club, 468 F.2d 1064 (2d Cir. 1972), the Second Circuit affirmed the District Court's granting of an injunction enjoining the plaintiff from playing for any other team pending determination of the dispute by arbitration. The Second Circuit emphasized that an injunction was the only means of preserving the status quo during the pendency of the arbitration. In Merrill Lynch, Pierce, Fenner & Smith, Inc v. Bradley, 756 F.2d 1048 (4th Cir. 1985), our own Fourth Circuit concluded that such equitable relief by a trial court to preserve the status quo furthered rather than frustrated the policies underlying the Federal Arbitration Act by insuring that the dispute resolution would be a meaningful process. And, in Saver Getriebe KG v. White Hydraulics, Inc., 715 F.2d 348 (7th Cir. 1983, cert. denied, 464 U.S. 1070, 104 S.Ct. 976, 79 L.Ed.2d 214 (1984), the Seventh Circuit noted that the plaintiff's contractual right to arbitrate the dispute would be rendered virtually worthless if the defendant could transfer the manufacturing rights in question before the matter was arbitrated.

Hughley v. Rocky Mountain Health Maintenance Organization, Inc., 927 P.2d 1325 (Colo. 1996) expressed well the underlying policy considerations regarding the critical need to preserve the status quo pending arbitration. There, the Court recognized that

> [i]ndeed, preliminary relief is particularly appropriate where resort to arbitration may prove futile if the status quo is not preserved pending the selection and appointment of an arbitrator prior to the arbitrator's exercise of jurisdiction over the dispute. ... To hold otherwise, that trial courts have absolutely no authority to provide interim relief in the arbitration context, would present a serious impediment to the fulfillment of our public policy favoring the voluntary establishment of an arbitral process for the peaceful resolution of disputes. In fact, if the status quo were in jeopardy and injunctive

> relief were not available, the promise of arbitration would ring hollow because in the event the party seeking relief should prevail at arbitration, [he or] she may otherwise be denied an effective remedy because the status quo was not maintained. Therefore, to avoid frustration of the arbitral process, under appropriate circumstances, a trial court's grant of injunctive relief is proper so long as it does not invade the province of the arbitrator by reaching the merits of the dispute ....

927 P.2d at 1329. In short, the relevant case law strongly emphasizes that the status quo must be maintained while the arbitration process is allowed to proceed.

*7 More specifically, courts have resolved the specific issue raised by your second question in favor of arbitration. These courts stress that one party generally cannot resort to self help measures in lieu of arbitration even when such measures are authorized by the contract itself. For example, in Thunderstik Lodge, Inc. v. Reuer, 585 N.W.2d 819 (S.D. 1998), the Court held that a lease provision requiring arbitration of differences limits the lessor to the remedy of arbitration and excludes other remedies of self-help such as forcible entry and detainer. In that case, it was noted that South Dakota had adopted the Uniform Arbitration Act. The lease agreement in Thunderstik provided for arbitration in the event that "differences between the parties" arose. As here, a separate provision in the lease authorized the Lessor to reenter and take possession of the property upon default by the lessee.

The Court in Thunderstik Lodge concluded that arbitration was first required, notwithstanding the right of reentry clause in the lease. As the Court opined,

> [w]e read this contract as requiring the parties to arbitrate this dispute. As all other remedies are foreclosed, the Reuers cannot proceed with forcible entry and detainer ....

585 N.W.2d at 822. Thus, the self-help remedy of forcible entry and detainer could not be resorted to in lieu of arbitration.

Moreover, the Court's analysis in Big Y Foods, Inc. v. Conn. Properties Tri-Town Plaza, 985 F.Supp. 232 (D.Conn. 1998) is particularly instructive with regard to this situation. There, the landlord, Tri-Town, alleged that its tenant, Big Y Foods, violated the lease in several aspects. The lease in question expressly granted the landlord the right to repossess the property upon breach 10 days after written notice thereof and Tri-Town asserted this right. However, the lease agreement in broad terms made arbitrable all disputes arising out of or related to the contract or its breach.

The Court rejected Tri-Town's argument that "paragraphs 7(m) and 8(a) give it the option to proceed directly to summary process whenever a significant default involving termination of the Lease occurs." In the Court's view, such a position would undermine the whole policy of arbitration. The Court's reasoning was as follows:
[a]doption of Tri-Town's position would eviscerate the language of 8(g) mandating that any controversy arising out of the Lease be referred to arbitration. Such an interpretation would typically limit those matters that would be referred to arbitration under the Lease to minor breaches that did not rise to the level of language limiting the scope of the arbitration clause. To the extent that the arbitration clause and the clause permitting resort to summary process conflict, the policy favoring arbitration prevails.

Tri-Town also maintains that the "at its option" language in paragraphs 8(a) and 7(m) means that Tri-Town has the choice to proceed to arbitration or summary process. This language, however, does not provide a choice between summary process and arbitration, but rather a choice of remedies, including re-entry and return of possession for certain defaults. The "at its option" language is internal to paragraphs 8(a) and 7(m). Paragraph 8(g) - the arbitration clause - sets forth no option or exception for summary process. Tri-Town does not have the "option" of resorting to summary process. Tri-Town does not have the "option" of resorting to summary process until after an arbitration panel, in compliance with paragraph 8(g) has found that a default has occurred. (emphasis added).

*8 985 F.Supp. at 235-236. Thus, a repossession clause, when read in conjunction with a broad arbitration clause, such as is present here, has been deemed by the courts to be applicable only after arbitration occurs.

Conclusion

Assuming the facts presented by your letter, it is our opinion that a court would find that arbitration is applicable here. Moreover, it is our opinion that CIP - not SPA - has the legal authority to operate the facility until the dispute is resolved by arbitration. [1]

Both state and federal law strongly favor arbitration for the settlement of disputes. All doubts must be resolved in favor of arbitration and courts generally bend over backwards to insure that the arbitration process is not disrupted. Case law is supportive of the principle that one party may not resort to self-help measures in lieu of arbitration. Here, the parties have agreed to resolve any controversy or dispute arising out of or relating to the License Agreement by arbitration. Accordingly, a court would likely deem the dispute referenced in your letter as arbitrable and that the status quo - in this instance, quiet enjoyment of the property by CIP - be maintained pending arbitration of the dispute.

Again, this opinion assumes the facts as presented. This Office is unable to resolve questions of fact through an opinion of the Attorney General. Nevertheless, we believe a court would support enforcement of the arbitration process in this instance.

Yours Very Truly,

Henry McMaster

Footnotes

1 This opinion addresses only a situation where a broad agreement to arbitrate is in place. Obviously, we make no comment herein as to situations where an arbitration agreement is not present. Moreover, this opinion does not address any invocation by SPA of the termination "without cause" provision of the Agreement. Your letter states that the Default provision (Paragraph 28) of the Agreement was relied upon by SPA and we assume this to be the case.

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