

IN THE UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF FLORIDA

Mark and Patricia MIDDLETON,  
Luke & Deborah BECKNELL, Alyn L. & Susan  
BENEZETTE, Tony W. & Diane M. BOSWORTH,  
Paul Jr. & Rosemary BOWMAN, Howard &  
Deborah BREEDLOVE, James & Mary Jo  
BROCK, James T. & M. Dianne BURK, Alfred  
CARDWELL, Bradley & Brenda A. DURCHOLZ,  
Robert W. & Marlene ERB, Benjamin L. FLORA,  
Kent C. GOFF, Alan & Peggy GROSSNICKLE,  
Gregory & Jean HALFAST, H. Ray & Sazan J.  
HAZEN, Thomas L. HESS, David & Alison M.  
HEYDE, Kimberly & Dennis L. HIATT,  
David A. & Kathy HINSHAW, Noel & Linda  
HOKE, Angelo & Christy JULOVICH, J. Keith &  
Joan KLINE, Dale & Karen LEWIS, Vey & Luanne  
LINVILLE, Mary Ann MERTZ, Rex & Cynthia  
MILLER, Ann E. MITCHELL, James & Susan  
PARE, Louis D. & Shelly L. PLUMLEE, George A.  
& Sharon D. RITTER, Thomas & Sandra L. SHARP,  
Dave & Melana SMITH, Eric C. & Nicole J.  
SMITH, John & Cathy SMOLNICKY, Sue &  
Richard SPRUNGER, James & Caroline E.  
STANTON, Isabelle & James STEPHAN,  
Dennis & Julie A. STREETER, John R. & Kristine  
STREETER, John W. & Sharon L. TARRY,  
Dawn & Michael W. THOMAS, Barbara TITUS,  
Thomas O. & Joy TROUTMAN, Pamela UHLIR,  
Debra WADDELL, Rex A. & Lisa K. WEIPER,  
M. Shane WOLFF,

CASE NO: 4:06CV83SPM/WCS

Plaintiffs/Respondents,

vs.

QUIXTAR, INC.,

Defendant/Claimant.

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**MEMORANDUM OF LAW IN SUPPORT OF THE IBOs’  
COMPLAINT FOR DECLARATORY JUDGMENT OR, IN THE  
ALTERNATIVE, TO COMPEL ARBITRATION BEFORE A NEUTRAL  
ARBITRATION BODY AND REQUEST FOR EMERGENCY STAY**

The Plaintiffs seek a declaratory judgment from this court finding that the dispute between the Plaintiffs and Quixtar is not subject to arbitration. In the alternative, the Plaintiffs request an order appointing a neutral arbitration body to conduct the arbitration.

The arbitration provisions of the Quixtar Rules of Conduct are procedurally and substantively unconscionable. Quixtar, with the assistance of JAMS, set out to create an arbitration system that would guarantee that Quixtar would never lose and they “have never lost in arbitration.” These are not the words of counsel, but the words of the United States District Court in Missouri. Judge Dorr’s Order details the numerous ways in which Quixtar set up the arbitration process in a manner that was procedurally and substantively unconscionable.

Quixtar has now instituted an arbitration proceeding against the IBOs. The IBOs are entitled to seek a declaratory judgment to determine their obligation to submit this dispute to arbitration. Necchi S.p.A v. Necchi Sewing Machine Sales Corp., 348 F.2d 693 (2<sup>nd</sup> Cir. 1965). Whether or not the IBOs are required to arbitrate is a matter of contract interpretation and the intent of the parties. Seaboard Coast Line Railroad Co. v. Trailer Train Co., 690 F.2d 1343 (11<sup>th</sup> Cir. 1982).

The alleged arbitration agreement between Quixtar and the IBOs is not a written and signed agreement at all. Instead, Quixtar claims they are entitled to arbitrate this dispute based upon language contained in the IBO Rules of Conduct. The Rules of Conduct are unilaterally promulgated by Quixtar, without the prior knowledge or approval of Quixtar distributors. The IBOs are not given advance notice of proposed rules or an opportunity to “opt out.” There is no negotiation between Quixtar and the IBOs. As Judge Dorr said, it was a “take it or leave it”

situation in which the IBOs either agree to be bound by the Rules of Conduct or they lose their distributorship, which is the “hallmark” of “unequal bargaining position.” Missouri Order at 21.

Quixtar has unfettered discretion in promulgating rules – they pass rules, change rules, amend rules, and delete rules at their pleasure. This is precisely what occurred here when Quixtar adopted Rule 6.5 (apparently in 2004) to make activities arguably subject to a Quixtar imposed non-compete agreement, when those same activities were previously an accepted way of doing business in the Amway/Quixtar distribution system. The IBOs had no knowledge that the rules had been changed and certainly never agreed to the new provisions in Rule 6.5.

Quixtar’s efforts to “game” the arbitration system have now been fully exposed by Judge Dorr’s order. To require the IBOs to submit to arbitration would amount to a denial of due process, especially when the arbitration is administered by JAMS. The fact that Quixtar set out to deny due process to litigants through the arbitration system is sufficient for this court to find that Quixtar is not entitled to arbitrate these claims. Indeed, Quixtar’s failure to disclose to the IBOs the facts that are set forth in Judge Dorr’s order is tantamount to committing a fraud on the IBOs and other Quixtar distributors. Simply put, no reasonable person would have agreed to arbitrate with Quixtar, if they had full knowledge of the extent to which Quixtar had gone to guarantee victory in every arbitration. At a minimum, there was no meeting of the minds and no intention on the part of the IBOs to arbitrate with Quixtar under circumstances where they could never win. As a result, this court should find there is no contractual obligation on the part of the IBOs to arbitrate Quixtar’s claims.

Even if required to arbitrate, the IBOs simply have no confidence in any arbitration administered by JAMS. The fact that JAMS acted in concert with Quixtar to create an arbitration system designed to insure that Quixtar would win every arbitration is clearly sufficient to raise a

reasonable fear on the part of the IBOs that the system is rigged in Quixtar's favor. Because "a reasonable person would have to conclude that an arbitrator was partial to the other party to the arbitration" JAMS should be disqualified and a neutral arbitrator assigned. Apperson v. Fleet Carrier Corporation, 879 F.2d 1344, 1358 (6<sup>th</sup> Cir. 1989); ANR Coal Company, Inc. v. Cogentrix of North Carolina, Inc., 173 F.3<sup>rd</sup> 493, 500 (4<sup>th</sup> Cir. 1999). All that needs to exist for disqualification is "a reasonable impression of partiality." Sheet Metal Workers Int'l Ass'n Local 420 v. Kinney air Conditioning, 756 F.2d 742, 745-46 (9<sup>th</sup> Cir. 1985).

It is axiomatic that an arbitrator acts in a quasi-judicial role, serving in the place of a court of law. The obligation of an arbitrator is to be fair and impartial and do justice to the parties. Kentucky River Mills v. Jackson, 206 F.2d 111 (6<sup>th</sup> Cir. 1953). "In order for arbitration to remain effective, arbitrators must not only be honest, but also above suspicion." International Produce, Inc. v. A/S Rosshavet, 504 F. Supp. 736, 739 (S.D. N.Y. 1980). "Arbitration agreements are aimed at amicable determination of disputes with results which both parties are willing to accept. . . Where imbalance is unnecessarily effected the purpose and advantages of arbitration are defeated." In re: Arbitration between Lobo & Co. and Plymouth Navigation Company of Monrovia, 187 F. Supp. 859, 860 (S.D. N.Y. 1960).

JAMS is a for-profit entity with a pecuniary interest in retaining the Quixtar arbitration contract. This is similar to Floss v. Ryan's Family Steak Houses, Inc., 211 F.3d 306, 314 (6<sup>th</sup> Cir. 2000), wherein a similar arbitration process was invalidated by the Sixth Circuit because "an alleged financial relationship between the employer company and [the arbitration service] compounded by the latter's pecuniary interest in retaining its arbitration service contract, might foster bias in favor of the employer client." See also, Walker v. Ryan's Family Steak Houses, Inc., 400 F.3d 370, 386 (6<sup>th</sup> Cir. 2005) (because the arbitration service selected the pool of arbitrators and had a "potential

bias” toward employers, it was “unlikely that applicants/employees will participate in an unbiased forum.”)

Unless this court acts to ensure that a neutral arbitration body is assigned, the entire arbitration proceeding will be tainted *ab initio*, ultimately resulting in a challenge to any adverse arbitration award. Under these circumstances, a court is authorized to appoint a neutral arbitrator “when the potential bias of a designated arbitrator would make arbitration proceedings simply a prelude to later judicial proceedings challenging the arbitration award.” Masthead Mac Drilling Corp. v. Fleck, 549 F. Supp. 854, 856 (S.D. N.Y. 1982); Erving v. Virginia Squires Basketball Club, 468 F.2d 1064, 1068 (2<sup>nd</sup> Cir. 1972) (court would appoint a neutral arbitrator in the place of the arbitrator named in the contract because “federal law is to be implemented in such a way as to make the arbitration effective.”)

Quixtar claims this dispute must be submitted to a JAMS arbitration because the IBOs agreed to a JAMS arbitration in the IBO Code of Conduct. The problem is that Quixtar concealed from the IBOs the incestuous relationship between Quixtar and JAMS. If the IBOs had been advised of the facts set forth in the Missouri Order, they would never have agreed to a JAMS arbitration. This is similar to Masthead Mac Drilling Corp. v. Fleck, *supra*, wherein the District Court designated the American Arbitration Association to select an arbitrator because the “defendants misrepresented the impartiality of the designated arbitrators by failing to disclose that the arbitrators are or have been business associates of defendants.” 549 F.Supp. at 856. Indeed, in Masthead Mac, the defendants agreed to the appointment of AAA, once the impartiality of the designated arbitrators was called into question, just as Quixtar should have done in this case.

JAMS has proceeded forward with the arbitration despite the IBOs’ objections. The arbitrator assigned by JAMS has denied the IBOs Motion to Disqualify JAMS and immediately

scheduled deadlines and future hearings. The assigned arbitrator claims to have no bias, but this court need not “probe the mind of the arbitrator” nor is it required “to identify evidence of actual bias.” International Produce, Inc. v. A/S Rosshavet, 504 F. Supp. at 739. All that is required for disqualification is “facts reasonably creating the appearance of partiality.” Id.

Any reasonable person in the shoes of the IBOs would feel they could not get a fair hearing under the circumstances presented. Quixtar used JAMS to create an arbitration system that would guarantee they would win. Quixtar’s actions were concealed from the IBOs and went undetected until Judge Dorr’s order exposed the inner workings of Quixtar’s relationship with JAMS and the complicity between the two of them to deny due process to opposing litigants. Under these circumstances, Quixtar’s protestations that they have now changed the rules should fall on deaf ears. Simply because JAMS has now identified the arbitrators who have been “trained” by Quixtar does not eliminate the problem, which is the complicity of Quixtar and JAMS in creating an unfair arbitration system. The simple fact of the matter is that the IBOs, and any reasonable person, would not trust these protestations of innocence, given the history set forth in Judge Dorr’s order.

If required to arbitrate, the IBOs are entitled to a fair and impartial arbitration that is free from any perceived bias. Should this court rule that the IBOs must submit to arbitration, the arbitration should be conducted by a neutral arbitration body. Quixtar’s rules contemplate that if JAMS cannot proceed, the American Arbitration Association would be assigned to administer the arbitration.

Arbitrator Neville had announced his intention to rule on Quixtar’s Motion for Temporary Relief on Monday, February 20, 2006. As a result of counsel’s stipulation, Arbitrator Neville has been requested not to rule until March 1, 2006. The IBOs request the entry of an order staying further proceedings in the JAMS arbitration, pending a ruling on this motion.

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**CERTIFICATE OF SERVICE**

I HEREBY CERTIFY that on this 23<sup>rd</sup> day of February, 2006, I faxed and mailed the foregoing document by first-class mail to John C. Peirce, BRYAN CAVE LLP, 700 13<sup>th</sup> Street NW, Washington, DC 20005.

s/ E.C. Deeno Kitchen  
ATTORNEY