

## The Supreme Court Steps Into The Chapter 75 Fray

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Over recent years, North Carolina's antitrust and trade regulation bar has watched two developments with great interest. One is the growing attempt, through both legislation and litigation, to define conduct in a variety of industries as *per se* unfair and deceptive trade practices, with resulting treble damages remedies. The second is the intense debate over the unresolved question of who, other than a direct purchaser of an item, can bring unfair and deceptive trade practices claims related to the purchase of that item.

Those developments have largely played out without the input of the North Carolina Supreme Court, leaving substantial questions about what the high court would do when presented with these issues. The Supreme Court shed some light on these topics in December 2007, when it decided **Walker v. Fleetwood Homes, Inc.**, 362 N.C. 63, 653 S.E.2d 393 (2007). That opinion seemingly answered certain questions about these issues, but it left other questions unresolved.

### Background of Walker

Walker concerned claims brought by a father and his adult daughter for defects in a manufactured home built by Fleetwood Homes. The purchase was what is referred to in the industry as a "buy for" transaction. The daughter selected the home and was to live in it, but she was disabled and could not qualify for credit. Instead, her father financed and bought the home on her behalf – a fact that was apparently known by the retailer but not disclosed on the documents provided to Fleetwood Homes. The purchase documents solely disclosed the father as the buyer.

The home had numerous defects, which Fleetwood Homes did not correct. The daughter never lived in the home, and the plaintiffs attempted to rescind the purchase. Those attempts were rebuffed.

The plaintiffs sued Fleetwood Homes, as well as the retailer and finance company. The claims against the retailer and finance company were resolved before trial, and the causes of actions against Fleetwood Homes were whittled down. The plaintiffs ultimately went to trial against Fleetwood Homes on the father's claims for breach of warranty and both plaintiffs' claims for unfair and deceptive trade practices.

As the case was tried, the unfair and deceptive trade practices claims almost exclusively piggybacked on the provisions of the North Carolina Manufactured Housing Board Act (the “Act”) and its regulations. Therefore, to understand the unfair and deceptive trade practice claims, one must understand the Act.

The Act is an occupational licensing statute that establishes the Manufactured Housing Board and requires certain members of the manufactured housing industry to be licensed by the Board. As with other occupational licensing statutes, the Act provides for conditions of licensure, including requiring licensees to comply with certain professional standards. Among those standards, it provides that a license may be denied, suspended or revoked, or the licensee may be fined, if the licensee has employed “unfair methods of competition” or committed “unfair or deceptive acts or practices.” G.S. Section 143-143.13(a)(7).

In framing the disciplinary provisions in the Act, the General Assembly did not define what constituted an “unfair method of competition” or “unfair or deceptive act or practice.” Instead, the agency adopted regulations that define some of the industry practices that constitute unfair practices that can give rise to discipline under G.S. Section 143- 143.13. Those include “failure to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeated failure to respond promptly to consumer complaints and inquiries.” 11 N.C.A.C. 8 .0907(1) and (4).

Like other occupational licensing statutes, the principal purpose of the Act is to regulate the conduct of its licensees through the regulator’s ability to revoke, suspend or otherwise discipline a licensee. But, unlike other occupational licensing statutes, the Act provides a private right of action for “any buyer of a manufactured home” who has suffered any loss or damage from any violation of the Act. G.S. Section 143-143.12(c). Pursuant to this provision, injured buyers can recover against the bond that licensees are required to provide.

The Walker plaintiffs tied their unfair and deceptive trade practices claims closely to these regulatory provisions. They submitted verdict forms asking the jury to find that Fleetwood Homes violated the regulatory provisions, copying the regulations almost verbatim. There were no other issues submitted to the jury that asked them to find any other conduct by Fleetwood Homes to support the G.S. Section 75-1.1 claim.

The jury returned a verdict finding that Fleetwood Homes had acted in violation of the regulations and finding that both plaintiffs were entitled to damages. Based on those jury findings, the Superior Court entered judgment for both plaintiffs. It pointed to the two jury responses that found regulatory violations and held that those acts “are specifically delineated and defined as unfair and deceptive commercial acts or practices” by the agency charged with licensing members of the manufactured housing industry.

The Court of Appeals affirmed the judgment's conclusion that Fleetwood Homes was liable to both plaintiffs on their G.S. Section 75-1.1 claims, but it remanded for a new trial on damages. Judge Jackson dissented from the Court of Appeals' decision as to the daughter's claim. Judge Jackson would have held that the daughter lacked standing as an indirect purchaser, whether that standing was based on G.S. Section 75-16 or on the private right of action contained in the Act itself, G.S. Section 143-143.12(c). With that background, the Supreme Court took up the case.

### **Regulations as the Basis for a Section 75-1.1 Claim**

Before the Supreme Court, the principal issue on the merits was whether, and in what fashion, a violation of the manufactured housing regulations could give rise to a claim under G.S. Section 75-1.1. The plaintiffs contended that, by passing G.S. Section 143-143.13, the General Assembly had intended to proscribe unfair and deceptive trade practices in the manufactured housing industry. They further contended that the Manufactured Housing Board's regulations defined the standard of practice in the industry – including specifically defining certain conduct related to repairs and responses to customer complaints – as unfair and deceptive trade practices. They thus argued that violation of the regulations constituted a *per se* violation of G.S. Section 75-1.1 or that, at a minimum, the Superior Court properly concluded that, on the facts of this case, the regulatory violations constituted violations of G.S. Section 75-1.1.

In contrast, Fleetwood Homes argued that it was improper and dangerous to allow a private plaintiff to leverage regulations promulgated for the purpose of license disciplinary proceedings into a *per se* claim under Section 75-1.1 and a corresponding treble damage remedy. It further argued that violations of these particular regulations governing repairs and responses to complaints amounted simply to variations on a breach of warranty claim. Fleetwood Homes argued that its violation of these regulations did not give rise to liability under G.S. Section 75-1.1 at all, let alone *per se* liability under the statute.

The Walker case arose against the backdrop of legislative expansion of the number of statutes whose violations constitute *per se* violations of G.S. Section 75-1.1. In recent years, the General Assembly has been quite active in enhancing private enforcement of a wide range of statutes by specifically providing that violations of those provisions are also *per se* violations of Chapter 75. This burgeoning legislative growth in unfair trade practice law was well-chronicled by Don Esposito in "Legislative Expansion of the Scope of North Carolina's Unfair Trade Practices Act" in the March 2005 *Antitrust News*.

But the vast majority of those statutes are quite different from the Manufactured Housing Board Act at issue in Walker. In the lion's share of such statutes, the General Assembly has described a specific industry practice that it views as *per se* "unfair and deceptive." Most often,

the General Assembly has made explicit its intention to create a Section 75 remedy for the violation. See, e.g., G.S. Section 25A-44 (Retail Installment Sales Act violation); G.S. Section 42A-10 (vacation rental agreement violation).

The Manufactured Housing Board Act stands in stark contrast to those statutes. It is an example of a small handful of occupational licensing statutes that (1) allow the occupational licensing board to take disciplinary action against licensees who engage in unfair or deceptive trade practices but (2) do not go on to explicitly define the scope of the conduct that the General Assembly views as unfair or deceptive. The Act also makes no attempt to link a violation of this licensing statute to a cause of action under Chapter 75. Other examples of such statutes include the Motor Vehicle Dealers and Manufacturers Licensing Law, G.S. Section 20-294(6), the Mortgage Lending Act, G.S. Section 53-243.12(m), and the state check-cashing license provisions, G.S. Section 53-283(5).

As a matter of professional governance, these statutes have certain salutary benefits. These statutes give the occupational licensing agencies the latitude to define – whether by regulation or by administrative case law – what sorts of practices are so unfair that discipline of a licensee is justified. They thus permit the agencies to employ their expertise about industry standards – expertise often not shared by members of the General Assembly – and to do so in fact-specific ways that the General Assembly could not in passing statutes of general applicability.

Specifically with respect to the Manufactured Housing Board Act, the agency employed its experience in the industry to determine that “failure to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeated failure to respond promptly to consumer complaints and inquiries” were unfair practices that could justify discipline on a license. 11 N.C.A.C. 8.0907(1) and (4). But, could the agency’s definition of that practice as unfair and deceptive give rise to treble damage liability? That was the question before the court.

The Walker court ruled that violations of the Manufactured Housing Board regulations were not *per se* Section 75-1.1 violations. In doing so, it rejected more broadly the argument “that a violation of a licensing regulation is a UDTP [unfair and deceptive trade practice] as a matter of law.” 362 N.C. at 71, 653 S.E.2d at 399. But the Walker court went on to rule that violations of the Manufactured Housing Board regulations “may be evidence of a UDTP” and “are potentially relevant to any claim that defendant violated § 75-1.1.” *Id.*

Applying those principles to the Walker case, the Supreme Court ruled that, because the jury had been given a special verdict form with interrogatories that “were derived nearly verbatim from a licensure regulation, and violations of this regulation by themselves are insufficient to prove a UDTP claim,” the verdict form was insufficient to provide the court a basis to find a

violation of G.S. Section 75-1.1. *Id.* at 72, 653 S.E.2d at 399. The Supreme Court therefore vacated the finding of Section 75-1.1 liability and remanded to the Superior Court for a new trial where it “may submit to the jury additional interrogatories seeking information which, if found by the jury, may be sufficient to support a finding of fact that defendant committed a UDTP.” *Id.*, 653 S.E.2d at 400.

The Walker decision leaves open some questions – both practical and legal. The interesting practical question is exactly what additional interrogatories the Walker plaintiffs would need to include in a special verdict form in order to support a finding of a violation of Section 75-1.1. Some might argue that, even if there were no Manufactured Housing Board regulations at all, jury findings that the defendant had “failed to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeatedly failed to respond promptly to consumer complaints and inquiries” would themselves constitute Section 75-1.1 violations. On the other hand, some might argue – as Fleetwood Homes did – that these sorts of interrogatories simply constitute a finding that Fleetwood Homes breached a warranty, which is insufficient to give rise to Section 75-1.1 liability. The Supreme Court gave no guidance about what more the jury must find in order to support a determination that Fleetwood Homes violated Section 75-1.1, and the court pointedly declined to address Fleetwood Homes’ argument that the conduct in this case simply amounted to a breach of warranty. Therefore, it is not at all clear what sort of jury interrogatories, over and above the interrogatories finding regulatory violations, plaintiffs will need to offer to establish a Section 75 violation in this and other cases that seek to piggyback on similar regulations.

The appellate courts will soon have the occasion to flesh out this practical issue. When Walker was remanded, the Superior Court did not hold a new trial at all. Instead, it used the same special verdict form and jury interrogatories that had been answered by the jury at the initial trial as the basis for a new judgment for the plaintiffs. The trial court found again that Fleetwood Homes had committed a Section 75-1.1 violation. Fleetwood Homes has appealed the judgment. It will likely contend that the Supreme Court required additional jury findings above and beyond a finding of a regulatory violation in order to constitute a Section 75-1.1 violation and there were no such additional findings here, where the Superior Court entered judgment based on the same verdict form that the Supreme Court had rejected.

Moreover, the Walker decision leaves open certain legal questions about the interaction between regulations and unfair and deceptive trade practices law. To be sure, the Walker court took a broad stance against basing Chapter 75 claims exclusively on the violation of occupational licensing regulations. It drew a sharp distinction between certain statutory violations, which in some cases have been held to give rise to *per se* Chapter 75 claims, and licensing regulation violations, which it indicated could not constitute *per se* Chapter 75 violations.

One open question may occur with respect to certain regulations where (like the Manufactured Housing Board regulations), the agency has defined particular conduct that it considers to be unfair and deceptive, but (unlike the Manufactured Housing Board regulations) the underlying statute does provide a private right of action for unfair and deceptive trade practices. That situation currently exists with certain insurance regulations. The Department of Insurance has defined certain conduct to constitute an unfair and deceptive trade practice, *see, e.g.*, 11 N.C.A.C. 4 .0314 through 4 .0318, 4.0422, 12 .0561, 12 .1018, and it has done so pursuant to its authority to enforce a statute (G.S. Section 58-63-10) whose violation can constitute a *per se* Chapter 75 violation. Can violation of one of those insurance regulations give rise to *per se* Chapter 75 liability?

The Walker decision could be read to support either position. The Walker court did attempt to draw the line between statutes and regulations as a basis for a Chapter 75 violation. The court did not evidence any willingness to permit plaintiffs to try Chapter 75 claims simply by providing the jury with interrogatories tracking the language of regulations, regardless of the nature of the regulations. On the other hand, the Supreme Court did find it significant that the Manufactured Housing Board regulations were not adopted pursuant to a statute whose violation itself constitutes a Chapter 75 violation. In the insurance context, where the General Assembly did intend to create *per se* UDTP liability for statutory violations, would the courts permit the agency to promulgate regulations interpreting those statutes that themselves gave rise to *per se* UDTP liability? The Supreme Court could arguably view such a claim very differently than the one before it in Walker.

One additional open question after Walker may be how the court would react if, in the course of a disciplinary proceeding, there were an agency finding that a licensee committed acts that constituted unfair and deceptive trade practices under a regulation such as the one at issue here. Would such a finding give rise to Section 75-1.1 liability as a matter of law, whether as a matter of the decision establishing a *per se* violation or as a matter of *res judicata*?

Presumably the courts would hold that an agency finding of an unfair and deceptive trade practice under a regulation such as those at issue in Walker cannot give rise to *per se* Chapter 75 liability. If there must be something more than a finding of a violation of a licensing regulation (as the Walker court held), then the fact that an agency has found a violation, rather than a jury, should not matter – the jury must find something more to support a Section 75-1.1 claim. However, the bar should watch for that and other applications of the Walker decision to shake out over the coming years.

### **Indirect Purchaser Claims**

The bar's interest in the Walker decision on the merits paled in light of its anticipation of the court's decision on the preliminary issue of who had standing to bring those claims. Based on the dissent in the Court of Appeals, the Supreme Court considered the question of whether the daughter could maintain an action when she had not been the direct purchaser of the home, but instead had her father purchase the home on her behalf as a "buy for" purchase. In addressing this issue, the Supreme Court took its first foray into the heated debate over indirect purchaser standing. It addressed the two issues raised by the dissent in the Court of Appeals: First, whether the daughter's standing was governed, not by Section 75-16, but instead by the narrower private right of action under Section 143-143.12(c). And, second, whether the daughter had standing if the general Section 75-16 standing provision applied.

In its brief, Fleetwood Homes focused exclusively on the first of these arguments. Fleetwood Homes argued that, because the plaintiffs were relying upon violations of the Manufactured Housing Board regulations to establish their claims, they had standing only if they could state a private right of action under the Manufactured Housing Board Act itself, Section 143-143.12(c). That section limits the private right of action on a surety bond to "buyers," which was defined in the statute in a way to exclude the daughter. Indeed, Fleetwood Homes did not independently discuss whether the daughter had standing under the language of Section 75-16.

The Walker court rejected Fleetwood Homes' argument that Section 75-16 did not apply. The court ruled that the Manufactured Housing Board Act right of action was not an exclusive remedy. Because the daughter was proceeding under Section 75-16, her standing was determined by that statute, rather than the Manufactured Housing Board Act.

This holding is not surprising in light of the Walker court's decision on the merits. As outlined above, the Walker court distanced the plaintiffs' Section 75-1.1 claim from the Manufactured Housing Board regulations by holding that its Section 75-1.1 claim required the jury to make additional findings over and above a violation of those regulations. Because the court analyzed the Section 75-1.1 claim on its own merits, separate from the issue of the regulatory violations, it is natural that the court would analyze the issue of standing under Section 75 as well. The Walker court then addressed the issue of much more general interest – whether indirect purchasers have standing to bring a claim under the language of Section 75-16 – an issue that Fleetwood Homes had not argued. The court thus provided some guidance on an issue that has been percolating for more than three decades. Some background is in order.

The federal and state courts have taken different sides of the indirect purchaser debate into which the Walker court waded. In **Illinois Brick Co. v. Illinois**, 431 U.S. 720 (1977), the U.S. Supreme Court held that indirect purchasers do not have claims under the Clayton Act. The Illinois Brick court ruled that, where there was an alleged price fixing conspiracy among

concrete block manufacturers, an action could be maintained only by their direct purchasers (masonry subcontractors) rather than by their indirect purchasers (owners of the buildings built with the concrete blocks). Although the language of the Clayton Act provides an action for “[a]ny person who shall be injured in his business or property,” the court reasoned that providing an action for indirect purchasers would risk duplicative recovery for both direct and indirect purchasers. Furthermore, even if there were no duplicative recovery, creating such an action would pose insuperable problems in managing litigation, proving damages and apportioning damages between direct and indirect purchasers.

In **Hyde v. Abbott Laboratories, Inc.**, 123 N.C. App. 572, 473 S.E.2d 680 (1996), the North Carolina Court of Appeals had the opportunity to interpret the similar provision of Section 16 of Chapter 75, which provides a private right of action for violations of both the state law antitrust provisions and the Unfair and Deceptive Trade Practices Act. The claims in Hyde were similar to those in Illinois Brick: indirect purchasers (infant formula consumers) maintained that a price fixing conspiracy among manufacturers had affected the price that was passed through the direct purchasers (retailers) to the consumers. Notwithstanding the similarity of the claims, the Court of Appeals rejected Illinois Brick as a matter of state law and determined that G.S. Section 75-16 provides a private right of action to both direct and indirect purchasers. It did so even though the court did not find any significant difference between the language of G.S. Section 75-16 and Section 4 of the Clayton Act, which both provide an action to “any person” injured by a violation. In so ruling, North Carolina joined most other states, which allow some form of indirect purchaser antitrust claims.

The decade after Hyde has been marked by both substantial uncertainty and significant efforts to pull the law related to indirect purchasers in opposite directions. Those developments are chronicled in previous articles in the *Antitrust News*, most thoroughly in Henry L. Kitchen Jr., “An Update on Indirect Purchaser Litigation Under North Carolina Law” in the March 2006 issue, and Jason D. Evans, “Indirect Purchaser Antitrust Actions in N.C. Seven Years After Hyde v. Abbott Laboratories, Inc.” in the June 2003 issue. Those articles are commended for a more complete description of the lay of the land. While there have been efforts to move the law in each direction, the predominant trend appears to have been toward permitting more actions by indirect purchasers. At the federal level, the rumblings about overruling Illinois Brick crystallized last year with the recommendations of the Antitrust Modernization Commission that Congress overrule Illinois Brick and allow actions by indirect purchasers.

In Walker, the Supreme Court took its first look at this issue and took a stand on the side of expansive indirect purchaser standing, at least in the factual scenario presented in that case. At length, the Walker court discussed the reasoning of the Court of Appeals both in Hyde and in the decision below in Walker. It adopted the Court of Appeals’ reasoning that the language of Section 75-16 providing a cause of action to “any person” injured is broad and, in order to

promote the remedial purposes of Section 75-16, is to be interpreted broadly enough to cover indirect purchasers such as the daughter in Walker.

Plaintiffs will contend that Walker has settled the indirect purchaser argument under Section 75, once and for all. And certainly the Supreme Court has indicated its willingness to adopt the Hyde principles.

But those arguing against indirect purchaser standing are not completely without hope. In presenting Walker to the Supreme Court, Fleetwood Homes did not dispute that the daughter would have standing under the language of Section 75-16. Therefore, the issue of how to interpret Section 75-16 was not fully presented to the Supreme Court by the litigants. The Supreme Court could take a different view if the issue were more completely joined.

Moreover, the Supreme Court's analysis focused on the unusual facts of Walker. The Supreme Court reasoned that the daughter had standing because she was the real consumer in the transaction. The father never intended to play any role except sign for a loan so that his daughter could buy a home.

This scenario does not present the ills of the usual Illinois Brick fact pattern, where class action claims are brought by both the intermediate consumers of the raw product (e.g., concrete bricks, rubber) and the ultimate consumer of the finished products (e.g., buildings, tires). In such a case, the courts have legitimate concerns about trying to manage litigation and to unscramble the egg to apportion damages between the two sets of consumers who consume different products (raw vs. finished) at different stages of the manufacturing process. Comparatively, it is easy to manage litigation and apportion damages in a case like Walker, where there are two plaintiffs who both simultaneously purchase a finished product as part of the same transaction. Therefore, defendants in the typical Illinois Brick context will certainly continue to argue that the Section 75-16 holding in Walker is distinguishable and that Section 75-16 does not provide indirect purchaser standing in other factual situations.

As with the issue on the merits, although the Supreme Court has lifted some of the fog surrounding standing under Chapter 75, there will be litigants who attempt to flesh out the precise contours of the Walker decision.