Supreme Court No. 80480-0

SUPREME COURT OF THE STATE OF WASHINGTON

BLAKELY COMMONS CONDOMINIUM ASSOCIATION, LLC,

Respondent,

v.

BLAKELY COMMONS LLC,

~~Petitioner~~. Appellant.

FILED
SUPREME COURT
STATE OF WASHINGTON
2007 DEC -3 P 3:58
BY RONALD R. CARPENTER
CLERK

BRIEF OF ~~PETITIONER~~ Appellant

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TABLE OF CONTENTS

Page

I. INTRODUCTION 1

II. ASSIGNMENTS OF ERROR 2

III. STATEMENT OF THE CASE 3

A. BLAKELEY COMMONS WAS FINANCED, PURCHASED, AND CONSTRUCTED USING INTERSTATE COMMERCE. 3

B. THE BLAKELEY HOMEOWNERS AGREED TO ARBITRATE CLAIMS ARISING FROM WARRANTIES AS TO DESIGN, CONSTRUCTION, AND MATERIALS. 5

C. THE ASSOCIATION CLAIMS BREACH OF WARRANTY AND ALLEGES DEFECTIVE MATERIALS. 6

D. THE TRIAL COURT DENIES ARBITRATION AS TO SOME CLAIMS AND ORDERS ARBITRATION OF OTHER CLAIMS. 6

IV. ARGUMENT 8

A. STANDARD OF REVIEW 8

B. THE FEDERAL ARBITRATION ACT APPLIES TO ALL CONTRACTS, SUCH AS THE BLAKELEY AGREMENTS, THAT IN THE AGGREGATE REPRESENT ECONOMIC PRACTICES RATIONALLY SUBJECT TO FEDERAL CONTROL 8

C. REAL ESTATE SALES AND CONSTRUCTION INVOLVE COMMERCE AS REQUIRED BY THE FAA. 13

1. Residential Real Estate Construction And Sale Is Activity Within Congress's Regulatory Powers Under the Commerce Clause....13

2. *Citizens Bank* Applied General Commerce Clause Precedent To Determine The Scope Of The FAA....16

D. THE FEDERAL ARBITRATION ACT APPLIES TO THE BLAKELEY COMMONS PURCHASE AND SALE AGREEMENTS AND WARRANTY ADDENDUMS....18

E. BECAUSE THE FEDERAL ARBITRATION ACT APPLIES, IT PREEMPTS THE WASHINGTON CONDOMINIUM ACT AS TO THESE TRANSACTIONS....22

F. THE TRIAL COURT ERRED IN HOLDING THAT *SATOMI* CONTROLS THIS CASE....24

1. *Satomi* Does Not Control Because The Interstate Nexus In This Case Is Much Greater Than That In *Satomi*....24

2. Satomi Was Wrongfully Decided Because The FAA Applies To Real Estate Transactions....26

G. THE ASSOCIATION IS BOUND BY THE BLAKELEY HOMEOWNERS' ARBITRATION AGREEMENTS....30

V. CONCLUSION....32

TABLE OF AUTHORITIES

Cases

Allied-Bruce Terminix Cos. v. Dobson,
513 U.S. 265 (1995) 9, 12, 19, 20, 23

Basura v. U.S. Home Corp.,
98 Cal. App. 4th 1205, 120 Cal. Rptr. 2d 328 (2002) 25

Bay Colony Condo. Owners Ass'n v. Origer,
586 F. Supp. 30 (N.D. Ill. 1984) 15, 27

Citizens Bank v. Alafabco, Inc.,
539 U.S. 52 (2003) ..... passim

Gilmer v. Interstate/Johnson Lane Corp.,
500 U.S. 20, 111 S. Ct. 1647, 114 L. Ed. 2d 26 (1991) 29

Gonzales v. Raich,
545 U.S. 1, 125 S. Ct. 2195, 162 L. Ed. 2d 1 (2005) 18, 28, 29

Groome Resources Ltd., LLC v. Parish of Jefferson,
234 F.3d 192 (5th Cir. 2000) 14, 27

Intern. Ass'n. of Fire Fighters, Local 46 v. City of Everett,
146 Wn.2d 29, 42 P.3d 1265 (2002) 9

Jones v. Gale,
405 F. Supp. 2d 1066 (D. Neb. 2005) 14, 19

Kamaya Co., Ltd. v. American Property Consultants, Ltd.,
91 Wn. App. 703, 959 P.2d 1140 (1998) 29

Katzenbach v. McClung,
379 U.S. 294, 85 S. Ct. 377, 13 L. Ed. 2d 290 (1964) 16, 17, 20, 21

Klay v. Pacificare Health Sys., Inc.,
389 F.3d 1191 (11th Cir. 2004) 31

Lost Creek Mun. Util. Dist. v. Travis Indus. Painter, Inc.,
827 S.W.2d 103 (Tex. App. 1992) 22

Mandeville Island Farms, Inc. v. American Crystal Sugar Co.,
334 U.S. 219, 68 S. Ct. 996, 92 L. Ed. 1328 (1948) 10, 16, 17

Marina Cove Condo. Owners Ass'n v. Isabella Estates,
109 Wn. App. 230, 34 P.3d 870 (2001) 11, 23

McCarney v. Nearing, Staats, Prelogar & Jones,
866 S.W.2d 881 (Mo. App. 1993) 22

McKay Building v. Juliano,
949 So. 2d 882 (Ala. 2006) 21, 25, 28

McLain v. Real Estate Bd. of New Orleans,
444 U.S. 232, 100 S. Ct. 502, 62 L. Ed. 2d 441 (1980) 14, 27

Meadowbrook Condo. Ass'n v. S. Burlington Realty Corp.,
152 Vt. 16, 565 A.2d 238 (1989) 31

Metro Industrial Painting Corp. v. Terminal Construction Corp.,
287 F.2d 382 (2nd Cir. 1961) 22

Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.,
460 U.S. 1, 103 S. Ct. 927, 74 L. Ed. 2d 765 (1983) 9

Munoz v. Green Tree Fin. Corp.,
542 S.E.2d 360 (S.C. 2001) 20

Old Coach Development Corp., Inc. v. Tanzman,
887 F.2d 1227 (3rd Cir. 1989) 19

Perry v. Thomas,
482 U.S. 483 (1987) 9, 23, 24

Satomi Owners Ass'n v. Satomi LLC,
139 Wn. App. 175, 156 P.3d 460 (2007) ..... passim

Scott v. Cingular Wireless,
160 Wn.2d 843, 161 P.3d 1000 (2007) 9

Shepard v. Edward Mackay Ents., Inc.,
148 Cal. App. 4th 1092 (2007) 21, 25, 28

Southland Corp. v. Keating,
465 U.S. 1, 104 S. Ct. 852 (1984) 9, 22, 23

Stein v. Geonerco, Inc.,
105 Wn. App. 41, 17 P.3d 1266 (2001) 8

Stuart v. Coldwell Banker Commercial Group, Inc.,
109 Wash.2d 406, 745 P.2d 1284 (1987) 31

Washington Mfd. Housing Ass'n v. Pub. Util. Dist. No. 3 of Mason County,
124 Wn.2d 381, 878 P.2d 1213 (1994) 14, 27

Wickard v. Filburn,
317 U.S. 111, 63 S. Ct. 82, 87 L. Ed. 122 (1942) 16, 17, 18

Wise v. Tidal Constr. Co.,
583 S.E.2d 466 (Ga. App. 2003) 9, 21, 25, 28

Zuver v. Airtouch Comms., Inc.,
153 Wn.2d 293, 103 P.3d 753 (2004) 9

Statutes

12 U.S.C. § 1701 15

12 U.S.C. § 2601 15

15 U.S.C. § 3601 ..... 15, 28

15 U.S.C. § 3607 15

15 U.S.C. § 3608 15

42 U.S.C. § 3601 15

42 U.S.C. § 5403 14

9 U.S.C. § 2 ..... 1, 8, 9

Cal. Corp. Code § 31512 23

RCW § 64.34 ..... 1, 5, 6

RCW § 64.34.100(2) 2, 23

RCW 64.34.030 2

RCW 64.34.204(1) 31

RCW § 64.34.224 ..... 3, 19, 20

RCW § 64.34.300 30

RCW § 64.34.304(1)(d) 30

RCW § 64.34.443 31

RCW § 64.34.445 31

RCW § 64.55.100(4) 23

I. INTRODUCTION

The Federal Arbitration Act (9 U.S.C. § 2) requires courts to enforce written agreements to arbitrate, and preempts any State laws that restrict enforcement. The buyers of the Blakeley Commons condominium units (the "Blakeley Homeowners") agreed in writing to arbitrate their disputes with that condominium's developer and declarant, Petitioner Blakeley Village, LLC ("Blakeley Village").[1]

The Respondent Blakeley Commons Condominium Association, LLC (the "Association") brought this action on behalf of those Blakeley Homeowners. When Blakeley Village moved to compel arbitration pursuant to the Federal Arbitration Act, however, the Superior Court refused to enforce the written arbitration agreements.

The Superior Court wrongly held that this case was governed by the 2-1 majority opinion in *Satomi Owners Ass'n v. Satomi LLC*.[2] The *Satomi* majority declined to apply the Federal Arbitration Act "solely because some construction materials came from outside Washington State."[3] "[U]nder the circumstances here," that majority held, the Act did not preempt the Washington Condominium Act (RCW 64.34), which

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[1] Blakeley Village is incorrectly designated in the case caption as "Blakeley Commons, LLC."

[2] 139 Wn. App. 175, 156 P.3d 460 (2007).

[3] *Id.* at 178.

provides an unwaivable right to bring certain claims for breach of condominium warranties in court.[4]

The Superior Court erred in blindly following this precedent, because Blakeley Village showed that the contracts at issue here involve interstate commerce and are well within the power of Congress to regulate. Because the Federal Arbitration Act preempts State law to the furthest extent of Congress's Commerce Clause power, *Satomi* was either wrongly decided or, at the very least, is confined to its unique facts and should not have been followed in this case.

II. ASSIGNMENTS OF ERROR

The Superior Court erred by failing to enforce the Blakeley Homeowners' agreements to arbitrate their claims. It wrongly held that the *Satomi* decision controlled this case, and by implication that the Federal Arbitration Act did not preempt the Washington Condominium Act as to these contracts, despite undisputed evidence that the transactions evidenced by these contracts involved interstate commerce. The Superior Court's error raises the following issue of law: Does the Federal Arbitration Act apply to residential condominium sales contracts such as the ones involved in this case, and so preempt RCW 64.34.100(2) and 64.34.030?

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[4] *Id.* (citing RCW 64.34.100(2))

III. STATEMENT OF THE CASE

A. Blakeley Commons Was Financed, Purchased, And Constructed Using Interstate Commerce.

None of the facts relevant to this appeal are disputed.

Between 2001 and 2004, Blakeley Village, a Washington State corporation, developed the Blakeley Commons condominiums in Seattle, Washington. The Blakeley Commons condominium project consists of 109 residential condominium units in small apartment buildings. The individual unit owners collectively own the common areas and common structural elements of the buildings, and each owner individually owns the interior of his unit.[5]

Blakeley Village sold all 109 condominium units. Only 79 of the units went to Washington State residents. Of the other 30 units, one was purchased by a Canadian, ten by Californians, two each by purchasers from Hawaii, New Jersey and Oregon, and one each by purchasers from Colorado, Connecticut, Idaho, Louisiana, Maine, Massachusetts, Minnesota, Montana, New York, Nevada, Tennessee, Utah, and Virginia.[6]

Blakeley Village and many of the homeowners relied on interstate financing. Construction was financed in part by a loan from a Delaware company (GMAC Commercial Finance, LLC), and twenty-nine of the

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[5] RCW 64.34.224(1).

[6] CP 555.

homeowners (including twenty-two Washington State residents) obtained their mortgage loans from various out-of-State lenders.[7]

Blakeley Village also bought insurance for the Blakeley Commons project out of State, purchasing that insurance coverage from two New York corporations.[8]

Construction of Blakeley Commons also relied heavily on interstate commerce. Like most large construction projects, this project used materials from all over the world. In fact, approximately 75% of the construction materials used to build Blakeley Commons traveled in interstate commerce, from at least 19 States and at least 5 foreign countries.[9] For example, the railings, pavement, insulation, windows, and exterior siding and trim came from Canada, awnings came from France, mirrors and interior doors were imported from China, appliances came from Mexico and Southeast Asia, and dozens of other components of the units and common areas and elements came from States other than Washington.[10]

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[7] CP 558.
[8] CP 558.
[9] CP 677.
[10] CP 679-683.

B. The Blakeley Homeowners Agreed to Arbitrate Claims Arising From Warranties as to Design, Construction, and Materials.

Each purchaser entered into a Purchase and Sale Agreement with a Warranty Addendum.[11] The Warranty Addendum provides for arbitration of all warranty claims by the Purchaser or the Association, expressly including warranties created by the Washington Condominium Act:

> The Seller and Purchaser agree that the Seller's and the Declarant's warranties to the Purchaser and to the Purchaser's successors and transferees, for the Unit and all Common Elements in the Condomium identified above are limited to the terms stated in this Warranty Addendum ("Warranty"). The implied warranties of quality under the Washington Condominium Act, RCW Chapter 64.34 are modified by this Warranty and all provisions of this Warranty apply to all warranties from the Seller to the Purchaser, including the implied warranties of quality under the Washington Condominium Act.
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> ********
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> 7. Seller's Right to Arbitration. At the option of Seller, Seller may require that any claim asserted by Purchaser or by the Association under this Warranty or any other claimed warranty relating to the Unit or Common Elements must be decided by arbitration, in King County, Washington, under the Construction Arbitration Rules of the American Arbitration Association....The decision rendered by the arbitrator shall be final and binding without appeal or review and may be enforced in any court of competent jurisdiction.[12]

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[11] CP 13-14.

[12] CP 16.

The Warranty Addendum also requires purchasers to bind successor purchasers, if any, to its terms.[13]

C. The Association Claims Breach of Warranty And Alleges Defective Materials.

On January 30, 2006, the Association brought this action against Blakeley Village and its construction company and contractors, "on behalf of itself and all unit owners with respect to matters affecting the condominium's common and limited common elements."[14] The Association asserted breach of warranty under the Washington Condominium Act (RCW 64.34), and related claims based on alleged "defective workmanship, materials and/or conditions" affecting the Blakeley Commons common elements.[15]

D. The Trial Court Denies Arbitration As To Some Claims And Orders Arbitration Of Other Claims.

On July 17, 2006, Blakeley Village moved to stay the trial court proceedings and compel arbitration.[16] On August 8, 2006, the trial court ordered the case stayed pending the resolution of the appeal in *Satomi Owners Ass'n v. Satomi LLC*, 139 Wn. App. 175, 156 P.3d 460 (2007) – a case in which the defendants sought to enforce warranty arbitration

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[13] CP 20.

[14] CP 6, 11.

[15] CP 8-11.

[16] CP 153-68

clauses in condominium purchase and sale agreements.[17] In both cases, the issue was whether the Washington Condominium Act's provision of a judicial forum for certain condominium warranty claims was preempted by the Federal Arbitration Act.

On June 11, 2007, the Court of Appeals issued its opinion in *Satomi*. The two judge majority held that "under the circumstances here," the Federal Arbitration Act could not apply "solely because some construction materials came from outside Washington State."[18]

On July 19, 2007, the condominium Association in this Blakeley case moved to lift the stay and deny mandatory arbitration.[19] On August 3, 2007, the trial court granted the Association's motion.[20] The trial court's entire stated reason for granting the motion was: "[t]he *Satomi* decision controls."[21]

On August 17, 2007, the trial court clarified that its Order of August 3, 2007 applied only to claims based on the Washington Condominium Act, and ordered arbitration of all <u>other</u> claims.[22] As a result, this case is now on a bifurcated track, in which some claims are in

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[17] CP 323-26

[18] 139 Wn. App. at 178.

[19] CP 348-554

[20] CP 739-41

[21] CP 740.

[22] CP 750-52.

arbitration while others, based on identical facts and similar legal theories, remain in court.

On September 4, 2007, Blakeley Village filed a notice of appeal as of right as to the trial court's Order of August 3, 2007 as clarified, and sought direct review by the Supreme Court.[23]

IV. ARGUMENT

A. Standard of Review

Appeal of a trial court order denying arbitration is as of right.[24] Review is *de novo*.[25] The trial court's determination of whether a statute is preempted by federal law is also reviewed *de novo*.[26]

B. The Federal Arbitration Act Applies To All Contracts, Such As The Blakeley Agreements, That In The Aggregate Represent Economic Practices Rationally Subject To Federal Control.

The Federal Arbitration Act provides that a "written provision in any...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."[27] The Federal Arbitration Act expresses a strong federal policy in favor of arbitration,

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[23] CP 753-62.

[24] *Stein v. Geonerco, Inc.*, 105 Wn.App. 41, 44, 17 P.3d 1266 (2001).

[25] *Satomi*, 139 Wn. App. at 178.

[26] *Robertson v. State Liquor Control Bd.*, 102 Wn. App. 848, 853, 10 P.3d 1079 (2000).

[27] 9 U.S.C. § 2.

under which as a matter of substantive federal law, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration," whether the issues concern the text of the contract or state contract law.[28] Washington State shares this strong pro-arbitration policy, as our Supreme Court has expressly held numerous times.[29]

The Federal Arbitration Act requires that arbitration agreements be enforced "within the full reach of the Commerce Clause."[30] It applies to any written contract, otherwise enforceable, that "evidenc[es] a transaction involving commerce.'"[31] That phrase, as the United States Supreme Court has repeatedly held, is the equivalent of the term of art "affecting commerce," and "signal[s] the broadest possible exercise of Congress' Commerce Clause power."[32]

The most recent United States Supreme Court precedent regarding the scope of the Federal Arbitration Act applies squarely to the Blakeley

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[28] *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).

[29] *Scott v. Cingular Wireless*, 160 Wn.2d 843, 858, 161 P.3d 1000 (2007); *Zuver v. Airtouch Comms., Inc.*, 153 Wn.2d 293, 301, 103 P.3d 753 (2004); *Intern. Ass'n. of Fire Fighters, Local 46 v. City of Everett*, 146 Wn.2d 29, 51, 42 P.3d 1265 (2002).

[30] *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 56 (2003) (quoting *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

[31] *Southland Corp. v. Keating*, 465 U.S. 1, 10-11, 104 S.Ct. 852 (1984) (quoting 9 U.S.C. § 2).

[32] *Citizens Bank*, 539 U.S. at 56; *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 273-74 (1995).

contracts. In that case, *Citizens Bank v. Alafabco, Inc.*, a local bank sought to compel arbitration under its debt-restructuring contract with the defendant, a local construction company.[33] As the transaction was between citizens of the same State, and its effect on interstate commerce was negligible, the Alabama Supreme Court held that the Federal Arbitration Act did not apply because the financing transaction had no substantial effect on interstate commerce.[34]

The United States Supreme Court reversed because the Alabama Supreme Court had used the wrong test.[35] The State court had wrongly asked whether "the individual...transactions, taken alone" substantially affect interstate commerce.[36] Instead, as in any other issue regarding the scope of the Commerce Clause, the Court held that the proper test is whether "in the aggregate, the economic activity in question would represent 'a general practice...subject to federal control.'"[37] That general

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[33] 539 U.S. at 54.

[34] *Id.* at 55.

[35] *Id.* at 56-57.

[36] *Id.* at 56.

[37] *Id.* at 57 (quoting *Mandeville Island Farms, Inc. v. American Crystal Sugar Co.*, 334 U.S. 219, 236, 68 S.Ct. 996, 92 L.Ed. 1328 (1948)) (ellipsis in original).

practice, to be subject to federal control, need merely "bear on interstate commerce in a substantial way." *Id.*[38]

The U.S. Supreme Court held that, using the proper test, the Federal Arbitration Act applied because of three facts: First, even though this particular transaction was intrastate, it was closely related to transactions that were not in that the original loans had been used for out-of-State projects.[39] Second, the debt was secured in part by construction materials that originated out of State.[40] Third, in the aggregate, commercial lending was self-evidently a national business.[41] Notably, the Court did not require the party seeking arbitration to prove that commercial lending was part of interstate commerce.

Similarly here, the Blakeley Commons contracts and transactions depended on and were interconnected with out-of-State financing transactions. The subject property secured out-of-State loans. The

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[38] For this reason, *Marina Cove Condo. Owners Ass'n v. Isabella Estates*, 109 Wn.App. 230, 34 P.3d 870 (2001), upon which the Association relied in its trial court briefs, should not be considered good law. The Court of Appeals in that case held that because the particular condominium sales and warranty contracts at issue did not by themselves have a substantial effect on interstate commerce, the FAA did not apply. As the *Satomi* Court recognized, this reasoning has been entirely discredited by *Citizens Bank*, which expressly rejected the test used by the *Marina Cove* appellate court. *See Satomi*, 139 Wn. App. 184-85.

[39] 539 U.S. at 57.

[40] *Id.*

[41] *Id.* at 58.

warranties cover construction materials that originated out of State. And in the aggregate, home construction and sales is a national business.

The facts of another recent United States Supreme Court on this issue are also instructive. In *Allied-Bruce Terminix Cos., Inc. v. Dobson*, homeowners brought an action against their local exterminator franchise for breach of a termite-extermination contract.[42] The exterminator sought to compel arbitration under the contract, and the Alabama courts held that the Federal Arbitration Act did not preempt an Alabama statute barring arbitration because the home exterminator contract did not involve interstate commerce.[43] Although it is difficult to imagine a more quintessentially 'local' contract than a bug-killing service plan for a single household, the United States Supreme Court reversed.[44] The Court held that neither the parties intention nor any reasonable expectations they could have had were relevant – rather, the contract's actual, undisputed, interstate nexus was what mattered.[45] Significantly, that nexus consisted of two facts: (1) the contract's guarantor was an out-of-State entity, and (2) the pesticides and construction materials the defendant had used to kill

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[42] 513 U.S. at 268

[43] *Id.* at 269.

[44] *Id.* at 282.

[45] *Id.* at 281

bugs and repair the house were manufactured outside the State (even though they were used inside the State). *Id.*

Similarly here, 28% of the Blakeley contracts were with out-of-State residents, and the materials used to construct the condominium homes purchased under the Blakeley contracts and placed under warranty by those contracts were used manufactured outside this State (even though they were later used inside this State).

C. Real Estate Sales And Construction Involve Commerce As Required By The Federal Arbitration Act.

1. Residential Real Estate Construction And Sale Is Activity Within Congress's Regulatory Powers Under the Commerce Clause.

Blakeley Village brought forth ample proof of the interstate nexus between the contracts here and interstate commerce. But based on the principles established by *Citizens Bank*, such specific proof was not even necessary because the contracts were part of an economic activity that in the aggregate represent a general practice subject to federal control – namely, residential real estate sales.

Blakeley Village agreed to arbitrate within an agreement to sell a home and to warrant its materials, construction, and design. The Washington Supreme Court, among many others, has recognized that Congress has the power to regulate the real estate industry and to preempt contrary State law. In *Washington Mfd. Housing Ass'n v. Pub. Util. Dist.*

No. 3 of Mason County, 124 Wn.2d 381, 385, 878 P.2d 1213 (1994), the Court reasoned that "[i]t is clear state laws establishing stricter construction...standards are federally preempted" by the National Manufactured Housing Safety Standards Act (42 U.S.C. § 5403). The United States Supreme Court similarly reversed the dismissal of an antitrust action against local real estate brokers because "whatever stimulates or retards the volume of residential sales, or has an impact on the purchase price, affects the demand for financing and title insurance" – which are activities in interstate commerce. *McLain v. Real Estate Bd. of New Orleans*, 444 U.S. 232, 246, 100 S.Ct. 502, 62 L.Ed.2d 441 (1980).

Even more specifically, a Federal Court of Appeals has held that "the commercial transaction of purchasing a home...fits well within the broad definition of economic activity," and allows Congress to regulate under the Commerce Clause. *Groome Resources Ltd., LLC v. Parish of Jefferson*, 234 F.3d 192, 205 (5th Cir. 2000) (upholding judgment and rejecting constitutional challenge to Fair Housing Amendment Act); *see also Jones v. Gale*, 405 F. Supp.2d 1066, 1077-78 (D. Neb. 2005) ("a number of courts have also recognized that the sale of real estate is activity affecting interstate commerce"). As these cases demonstrate, Congress has freely and constitutionally regulated many aspects of the real

estate industry, including but not limited to financing, disclosures, and safety standards.[46]

Indeed, Congress has specifically regulated the rights of condominium owners and their associations against developers in the Condominium and Cooperative Abuse Relief Act of 1980 (15 U.S.C. §3601, *et seq.*).[47] Congress expressly found in that statute that the federal government regulates "the cooperative and condominium housing markets" through various laws, and that "the creation of many condominiums and cooperatives is undertaken by entities operating on an interstate basis." 15 U.S.C. §3601(a)(4). The only court to address the constitutionality of that Act has accordingly agreed that this federal statute is a valid exercise of Congress's Commerce Clause powers because "[t]here is a rational basis for Congress's finding that [certain lease terms] might interfere with the interstate sale of condominiums" – and are therefore within interstate commerce. *Bay Colony Condo. Owners Ass'n v. Origer*, 586 F. Supp. 30, 33 (N.D. Ill. 1984).

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[46] *See also*, *e.g.*, Real Estate Settlement Procedures Act, 12 U.S.C. § 2601 *et seq.*; Fair Housing Act, 42 U.S.C. § 3601 *et seq.*; National Housing Act, 12 U.S.C. § 1701 *et seq.*

[47] *See* 15 U.S.C. § 3607 (owners or association may terminate self-dealing management contract with developer); 15 U.S.C. § 3608 (certain auxiliary condominium facility leases are voidable).

2. *Citizens Bank* Applied General Commerce Clause Precedent To Determine The Scope Of The Federal Arbitration Act.

Under the previously noted U.S. Supreme Court precedent binding upon this Court, there simply is no distinction between the scope of Congress's power to regulate real estate transactions in general and its power to regulate real estate transactions by requiring enforcement of arbitration agreements therein.

This point is further confirmed by the fact that the *Citizens Bank* Court cited to and discussed three seminal Commerce Clause cases as examples of the kind of general practice that is subject to federal control for Federal Arbitration Act purposes: *Katzenbach v. McClung*; *Mandeville Island Farms, Inc. v. American Crystal Sugar Co.*, and *Wickard v. Filburn*.[48]

Katzenbach held that the federal Civil Rights Act applied to a local neighborhood barbecue restaurant because discriminatory practices could affect the volume of raw materials it buys – some of which travels in interstate commerce.[49] *Mandeville Island Farms* similarly held that the Sherman Act applies to in-state price-fixing of beets – based on the

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[48] 529 U.S. at 57-58.

[49] *Katzenbach v. McClung*, 379 U.S. 294, 300, 85 S.Ct. 377, 13 L.Ed.2d 290 (1964).

aggregated effects on national beet prices.[50] And *Wickard* upheld a federal law that restrained a farmer from growing wheat for his own personal consumption – because growing wheat at home could mean less purchase of wheat from another State.[51] As these cases demonstrate, purely intrastate economic activity is generally within the scope of the Commerce Clause (and thus the Federal Arbitration Act) as long as the type of activity in the aggregate bears on interstate commerce.[52]

The widespread agreement that Congress may regulate residential real estate transactions follows naturally from the interstate commerce principles set forth in the previously discussed *Wickard*, *Katzenbach*, and *Mandeville Island Farms*, cases. Congress and the courts have recognized that the national real estate market does not consist of hermetically sealed separate State markets. As the record here confirms, condominium unit purchasers, insurers, and mortgage lenders come from other States and even other nations. Like the local beet sales in *Mandeville Island Farms*, the local restaurant meals in *Katzenbach*, or the home-grown crops for home consumption in *Wickard*, real estate transactions and home sales that superficially seem "local" have, in the aggregate, a substantial impact

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[50] *Mandeville Island Farms, Inc. v. American Crystal Sugar Co.*, 334 U.S. 219, 236, 68 S.Ct. 996, 92 L.Ed. 1328 (1948).

[51] *Wickard v. Filburn*, 317 U.S. 111, 128-29, 63 S.Ct. 82, 87 L.Ed. 122 (1942).

[52] *Citizens Bank*, 539 U.S. at 58.

upon the national real estate, construction, development, insurance, and financing markets, as well as on the movement of purchasers, goods, and funds across State (and national) borders.

Moreover, when the Supreme Court recently reaffirmed the sweeping scope and language of *Wickard*, in *Gonzales v. Raich*, it also confirmed that the record need not establish to a certainty that some local, *de minimis* economic activity would have in the aggregate a substantial effect on interstate commerce.[53] The Court held that Congress may regulate the seemingly "local" activity if there is merely a "rational basis" for believing there would be an aggregate effect on interstate commerce.[54] This extremely low interstate commerce threshold is met in this case.

D. The Federal Arbitration Act Applies To The Blakeley Commons Purchase and Sale Agreements And Warranty Addendums.

Applying these well established, black letter principles of Commerce Clause jurisprudence, the Blakeley Commons contracts are well within the scope of Congress's Commerce Clause power (and thus the Federal Arbitration Act), for at least three reasons.

First, because the transactions themselves occurred between citizens of different States (and even countries). *See Old Coach*

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[53] *Gonzales v. Raich*, 545 U.S. 1, 16, 22, 125 S.Ct. 2195, 162 L.Ed.2d 1 (2005).

[54] *Id.*

Development Corp., Inc. v. Tanzman, 887 F.2d 1227, 1232 (3rd Cir. 1989)(interstate sale of land is activity protected by the dormant Commerce Clause); *Jones*, 405 F. Supp.2d at 1078 (D. Neb. 2005) (same). Thirty out of the 109 condominium units in the Blakeley Project were bought by out-of-State residents. Moreover, because the common elements of Blakeley Commons are expressly covered by the Warranty Addendum and are owned by all of the unit owners as "undivided interests" under Washington law,[55] when out-of-State residents bought units, they entered into a joint ownership relationship with State residents. By the same token, the State citizens entered into a joint ownership relationship with out-of-State citizens. As in *Allied-Bruce*, when an out-of-State party transacts with a State citizen, that by definition involves interstate commerce.

Second, these contracts involve interstate commerce because twenty-nine buyers utilized out-of-State mortgage lenders to finance their condominium purchases.[56] Thus, approximately 27% of the contracts at issue were financed by out-of-State loans, and a considerable fraction of Blakeley Commons – including those collectively held common areas and

[55] RCW 64.34.224(1).

[56] CP 558.

elements – secures those loans to out-of-State financial institutions.[57] As in *Citizens Bank*, these contracts involve interstate commerce because of their close connection to the national commercial lending business, including the securitization of loans across State lines. The South Carolina Supreme Court, similarly, held that the Federal Arbitration Act applies to a home equity loan contract between homeowners and a builder, residents of South Carolina, because the builder assigned the loan to a Delaware corporation which disbursed the funds from a Minnesota bank. The fact that the homeowners were unaware of this, and had no intention of making an interstate transaction, was irrelevant.[58]

Third, the Federal Arbitration Act applies here because the contracts warranty the condominium's construction materials at issue in this case – and 75% of those construction materials moved in interstate commerce. As in *Allied-Bruce*, the use of out-of-State construction materials involves interstate commerce. *See also Katzenbach*, 379 U.S. at 300 (use of raw materials from out of State makes restaurant's treatment of its in-State customers a matter for Commerce Clause regulation).

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[57] *See* RCW 64.34.224(5) (common elements not subject to encumbrance except as part of encumbrance of unit).

[58] *Munoz v. Green Tree Fin. Corp.*, 542 S.E.2d 360, 364 (S.C. 2001); *and see Hedges v. Carrigan*, 11 Cal. Rpt. 3d 787 (Cal. App. 2004)(FAA applies to homeowner's action alleging residential construction defects where financing was a Fair Housing Act loan and defendant belonged to a national realty organization).

Indeed, many jurisdictions have held that the Federal Arbitration Act applies to a home's construction, warranty, or sales contract because materials used in that home's construction traveled across State lines. For example, in *Shepard v. Edward Mackay Ents., Inc.*, 148 Cal.App.4th 1092, 1095-96, 56 Cal.Rptr.3d 326 (2007), a homeowner sued his developer for breach of warranties and related claims based on alleged construction defects. Based on a State statute limiting arbitration, the trial court denied the developer's motion to enforce the parties' arbitration agreement. The California appellate court reversed, solely because the use of building materials from out of State placed the transaction within the scope of the interstate commerce clause.[59]

Similarly, in *McKay Building v. Juliano*, 949 So.2d 882, 886 (Ala. 2006), the Alabama Supreme Court held that the Federal Arbitration Act applied to a home remodeling contract because some materials used were from out of State.

The Georgia Court of Appeals similarly held in *Wise v. Tidal Constr. Co.*, 583 S.E.2d 466, 469 (Ga. App. 2003), that the Federal Arbitration Act applied to a home construction warranty simply because most building materials pass in interstate commerce. *See also McCarney*

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[59] *Shepard v. Edward Mackay Ents., Inc.*, 148 Cal.App.4th 1092, at 1100-1101, 56 Cal.Rptr.3d 326 (2007).

v. Nearing, Staats, Prelogar & Jones, 866 S.W.2d 881, 888 (Mo. App. 1993) (Federal Arbitration Act applies to construction contract between Missouri residents solely because contractor used materials from 29 out-of-State suppliers); *Lost Creek Mun. Util. Dist. v. Travis Indus. Painter, Inc.*, 827 S.W.2d 103, 105 (Tex. App. 1992) (Federal Arbitration Act applies to contract to paint reservoir because paint was manufactured out of State and surety was located out of State).

E. Because The Federal Arbitration Act Applies, It Preempts The Washington Condominium Act As To These Transactions.

As the United States Supreme Court has held, the purpose of the Federal Arbitration Act was to assure that when parties agree to arbitrate, "their expectations would not be undermined by federal judges, or...by state courts *or legislatures*."[60]

The Federal Arbitration Act does not merely embody a policy in favor of arbitration – it also "withdrew the power of the states to require a judicial forum" for disputes covered by a written arbitration agreement.[61] The Supreme Court of the United States has repeatedly held that the Federal Arbitration Act preempts any State statute that targets the

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[60] *Southland Corp.*, 465 U.S. at 13 (emphasis added) (quoting *Metro Industrial Painting Corp. v. Terminal Construction Corp.*, 287 F.2d 382, 387 (2nd Cir. 1961) (Lumbard, Chief Judge, concurring)) (ellipsis in original).

[61] *Southland Corp.*, 465 U.S. at 10.

enforcement of arbitration agreements.[62] The Court set forth the rule bluntly and without qualification: "state courts cannot apply state statutes that invalidate arbitration agreements."[63]

The condominium Association here relies on the provisions of the Washington Condominium Act which state "[a]ny right or obligation declared by this chapter is enforceable by judicial proceeding" and "provisions of this chapter may not be varied by agreement, and rights created by this chapter may not be waived."[64] The United States Supreme Court has held, however, that the Federal Arbitration Act preempts a State statute with parallel language – namely, the similar provision in Cal. Corp. Code §31512 that states any agreement "purporting to bind any person ... to waive compliance with any provision of this law or any rule or order hereunder is void."[65] The United States Supreme Court similarly held that the State law was preempted in *Perry v. Thomas*, where the State statute

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[62] *Perry v. Thomas*, 482 U.S. 483, 491 (1987); *Southland Corp.*, 465 U.S. at 15-16.

[63] *Allied-Bruce*, 513 U.S. at 273.

[64] RCW 64.34.100(2), 64.34.030; *and see Marina Cove Condominium Owners Ass'n v. Isabella Estates*, 109 Wn. App. 230, 236-37, 34 P.3d 870 (2001) (right to judicial enforcement of WCA warranty claims is not waivable). Since this case began, the WCA has been amended to permit arbitration, but as review of the arbitrator's decision is *de novo*, the WCA still effectively nullifies an agreement to submit disputes to *binding* arbitration. *See* RCW 64.34.100(2) (2005); RCW 64.55.100(4) (2005).

[65] *Southland Corp.*, 465 U.S. at 6, 16.

allowed employees to bring an action for collection of wages regardless of any written arbitration agreement.[66] The Federal Arbitration Act preempts the Washington Condominium Act just as it preempts any other State statute targeted at arbitration agreements.

F. The Trial Court Erred In Holding That *Satomi* Controls This Case.

1. *Satomi* Does Not Control Because The Interstate Nexus In This Case Is Much Greater Than That In *Satomi*.

Whether *Satomi* was rightly decided or not, this case should have a different result because the record here shows a much stronger nexus with interstate commerce than the record in *Satomi*.

The *Satomi* majority expressly limited its opinion to the record before it. The very first sentence of the opinion defines the issue as whether the Federal Arbitration Act preempts the Washington Condominium Act "*solely* because some construction materials came from outside Washington state."[67] The holding is given as "[w]e hold that *under the circumstances here*, the commerce clause does not reach so far, and the state statute controls."[68]

The *Satomi* majority based its reasoning on the relative sparseness of the record. Unlike Blakeley Village here, the *Satomi* developer

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[66] *Perry*, 482 U.S. at 486, 491.

[67] *Satomi*, 139 Wn. App. at 178.

[68] *Id.* (emphasis added)

"relie[d] upon a single fact: that construction materials came from outside Washington state."[69] The majority acknowledged that *Citizens Bank* controlled the case, and noted with approval the case of *Basura v. U.S. Home Corp.*, 98 Cal.App.4th 1205, 120 Cal.Rptr.2d 328 (2002), which held that the Federal Arbitration Act applied to a home construction contract between owners and the developer because the developer used interstate materials, advertising, and contractors.[70] It distinguished these cases solely because "[i]n neither case...was the presence of interstate materials the *only* interstate aspect of the case."[71] This, it reasoned, was significant because "no court has held that the use of materials from other states is, *by itself*," enough to trigger FAA protection."[72] (The majority was incorrect in its premise. *See Shepard*, 148 Cal.App.4th at 1100-01 (the use of material from other states triggers Federal Arbitration Act protection); *McKay Building*, 949 So.2d at 886 (same); *Wise*, 583 S.E.2d at 469 (same)). Again, the *Satomi* decision emphasized that, unlike other contracts in which the Federal Arbitration Act applied (and unlike the

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[69] *Id.* at 188.

[70] *Id.* at 185.

[71] *Id.* at 189 (emphasis added).

[72] *Id.* (emphasis added).

Blakeley Commons contracts), the contracts in the *Satomi* case all "involved a Washington company and Washington residents."[73]

Satomi is at best a case in which the defendant simply failed to bring forward quite enough proof of the obvious to pass a very low interstate commerce threshold. The much fuller record in this Blakeley case merits a different holding – for this case involves contracts that were (in part) between residents of different States, by which Washington State residents became co-owners of property with out-of-State parties, contracts that were inextricably linked to financing transactions securing that same property to out-of-State lenders, contracts that included warranties for materials which mostly traveled in interstate commerce, contracts that have a strong nexus with interstate commerce, and contracts that reflect a general practice that is subject to regulation under Congress's Commerce Clause Power. On this record, the Federal Arbitration Act preempts the Washington Condominium Act's judicial enforcement and anti-waiver provisions.

2. *Satomi* Was Wrongfully Decided Because The Federal Arbitration Act Applies To Real Estate Transactions.

Satomi was in error because at the very least there is a rational basis for finding that condominium sales are, in the aggregate, "a general

[73] *Id.* at 188.

practice...subject to federal control," so that the Federal Arbitration Act applies to such sales contracts. *Citizens Bank*, 539 U.S. at 57; *and see Washington Mfd. Housing Ass'n*, 124 Wn.2d at 385 (Congress can preempt housing construction standards); *McLain*, 444 U.S. at 246 (residential sale volume and price has impact on interstate commerce); *Groome Resources*, 234 F.3d at 205 (Congress may regulate home purchases under the Commerce Clause); *Bay Colony Condo Owners Ass'n*, 586 F. Supp. at 33 (Condominium and Cooperative Abuse Relief Act is within Congress's Commerce Clause Power because of interstate purchases, financing, and development of condominium units). The *Satomi* majority should not have asked whether these particular transactions were interstate, but rather whether Congress had the power to regulate condominium sales contracts in general. In bluntly holding that "the commerce clause does not reach so far," it set a precedent of breathtaking force. The very existence of the national condominium market shows that this holding was error.

As Congress found in enacting the Condominium and Cooperative Abuse Relief Act, "the creation of many condominiums and cooperatives is undertaken by entities operating on an interstate basis." 15 U.S.C.

§3601(a)(4).[74] It is not relevant in this regard that Blakeley Village itself is not an out-of-State entity, because Congress's Commerce Clause power "may be exercised in individual cases" through the Federal Arbitration Act "without showing any specific effect upon interstate commerce" of that particular case by itself. *Citizens Bank*, 539 U.S. at 56-57. As the United States Supreme Court recently held, "[w]e have never required Congress to legislate with scientific exactitude.... That the regulation ensnares some purely intrastate activity is of no moment." *Raich*, 545 U.S. at 17, 22. The *Satomi* majority implicitly overruled the Congressional finding that condominium development as a class has sufficient interstate impact to be subject to Commerce Clause regulation, even though such a finding must be upheld so long as it has a mere "rational basis." *Raich*, 549 U.S. at 22.

The *Satomi* majority erred in other ways as well. It was simply incorrect, for example, when it stated that no other court had held that the use of construction materials from other States triggers the protections of the Federal Arbitration Act.[75] It asserted that the transactions before it "ha[d] none of the earmarks" of economic activity subject in the aggregate

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[74] *See Raich*, 545 U.S. at 21 (Congressional findings in public record are appropriate proof of interstate ramifications of local commerce).

[75] *See Shepard*, 148 Cal.App.4th at 1100-01; *McKay Building*, 949 So.2d at 886; *Wise*, 583 S.E.2d at 469.

to federal control,[76] but failed even to hint at what those "earmarks" might be, as would have been appropriate given the unbroken seven-decade history in the United States Supreme Court of upholding Congressional regulation under the Commerce Clause of virtually any and all economic activity.[77] Although *Citizens Bank* considered both the immediate transaction and the transactions that led up to it, the *Satomi* decision myopically characterized the transactions at issue as simply being "the giving of the warranty" rather than the sale of the condominium apartments and common elements, the development of the condominium project, or the intertwined financing and sale of real estate.[78]

In short, the 2-judge majority decision in *Satomi* was an unwonted and poorly reasoned relapse into the sort of "judicial hostility" towards arbitration that prompted Congress to enact the Federal Arbitration Act in the first place. *Kamaya Co., Ltd. v. American Property Consultants, Ltd.*, 91 Wn. App. 703, 709, 959 P.2d 1140 (1998) (quoting *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24, 111 S.Ct. 1647, 114 L.Ed.2d 26 (1991).) It should not continue to guide this State's courts.

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[76] *Satomi*, 139 Wn. App. at 188.

[77] *See Raich*, 549 U.S. at 35 (Scalia, J. concurring).

[78] *Compare Citizens Bank*, 539 U.S. at 57 to *Satomi*, 139 Wn. App. at 189.

G. The Association Is Bound By The Blakeley Homeowners' Arbitration Agreements.

It is expected that the Association will argue, as it did in the trial court, that it is not bound by the Blakeley Homeowners' written agreements to arbitrate. This contention, if made, need not long delay this Court. This issue was dispatched in *Satomi*, which correctly held that a condominium Association "necessarily" brings its action as the representative of the homeowners (not on its own behalf), and is therefore bound by the homeowners' agreements.[79]

The Washington Condominium Act makes all the Blakeley Homeowners, and only the Blakeley Homeowners, members of the Association.[80] A homeowners' association may litigate on the owners' behalf as to matters related to the condominium, but it may litigate on its own behalf only "in connection with its own functions and activities."[81] For example, a condominium Association could litigate on its own behalf for breach of a contract to which the Association itself was a party. But where, as here, the Association litigates on its homeowners' behalf, the Association stands in the homeowners' shoes, and is subject to any

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[79] 139 Wn. App. at 180.

[80] RCW 64.34.300.

[81] *Satomi*, 139 Wn. App. at 180 (citing RCW 64.34.304(1)(d); William B. Stoebuck & John W. Weaver, Washington Practice: Real Estate: Transactions § 12.5, at 40 (2d ed. 2004)).

defenses and limitations that may be asserted against the homeowners it represents.[82]

As held in *Satomi*, the Association's Condominium Act claim belongs to the condominium owners – not to the Association.[83] The Association alleges damage to the units and to the common and limited-common elements of Blakeley Commons, which are owned under Washington law by the owners – not by the Association.[84] Moreover, the Washington Condominium Act implied warranty runs to the unit purchasers – not to the Association.[85] The Association on behalf of the unit owners is bound by those unit owners' agreements to arbitrate.[86]

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[82] *Id.* at 180; *and see Stuart v. Coldwell Banker Commercial Group, Inc.*, 109 Wash.2d 406, 413-14, 745 P.2d 1284 (1987) (where homeowners' association brought actions in representative capacity, it was subject to same defenses and limitations as if brought by homeowners); *see also Klay v. Pacificare Health Sys., Inc.*, 389 F.3d 1191, 1202-03 (11th Cir.2004) ("associations suing in a representative capacity are bound by the same limitations and obligations as their members"); *Meadowbrook Condo. Ass'n v. S. Burlington Realty Corp.*, 152 Vt. 16, 565 A.2d 238, 241 (1989) (condominium association's claim is "only as good as that of its constituent members.")

[83] *Satomi*, 139 Wn. App. at 180. The Superior Court here correctly held that the non-WCA claims were arbitrable, so they are not before this Court. See Order of August 17, 2007

[84] CP 6-11; *Satomi*, 139 Wn. App. at 180 (citing RCW 64.34.204(2), (4), 64.34.224(1), 64.34.228(1)).

[85] *Satomi*, 139 Wn. App. at 180 (citing RCW 64.34.443, RCW 64.34.445).

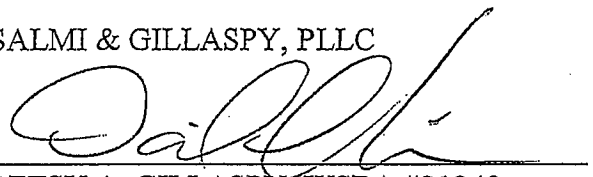
[86] *Id.*

V. CONCLUSION

Because the record shows that the transactions evidenced by the contracts here constitute economic activity that, in the aggregate, would represent a general practice subject to federal control under the Commerce Clause, Blakeley Village respectfully requests that this Court reverse the Superior Court's order denying arbitration and lifting the stay of the case.

RESPECTFULLY SUBMITTED this 3rd day of December, 2007.

SALMI & GILLASPY, PLLC



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