

Chicago Daily Law Bulletin®

VOLUME 165, NO. 188

LAW BULLETIN MEDIA

Alarm contractors' argument gets green light to challenge ordinance

The 7th U.S. Circuit Court of Appeals recently considered a dispute between the village of Schaumburg, the Northwest Central Dispatch System and several commercial 911 fire-alarm service companies.

The 7th Circuit's opinion makes it clear that public entities such as the village may pass legislation which results in exclusive operations by commercial enterprises, but that such legislation must be adequately prepared to avoid potential issues with the U.S. Constitution's contracts clause. The case is *Alarm Detection Systems Inc., v. Village of Schaumburg*, No. 18-3316 (7th Cir. 2019).

The events giving rise to the 7th Circuit's opinion date back to the village board's passage of a 2016 ordinance requiring all commercial buildings to send fire-alarm signals directly to Northwest Central Dispatch System.

As written, the ordinance threatened to exclude all but one-alarm system provider from the marketplace in the village because that one provider, Tyco Integrated Security LLC, had an almost two-decade-old exclusive arrangement with Northwest.

The remaining alarm systems providers in the area filed suit arguing that the ordinance effectively requires that all alarm systems must contract with Tyco. The plaintiff companies alleged that the ordinance would cause early termination of outstanding alarm contracts and result in a windfall of \$1 million annually for Tyco and more than \$300,000 annually for the village.

The plaintiff companies brought a variety of claims and further sought a preliminary injunction against the ordinance's enforcement. In addition to the



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contracts clause claim, the suit included claims of violations of the equal protection and due process clauses of 14th Amendment, violations of the Sherman Act and Clayton Act and violations of state tort law.

As the 7th Circuit noted, the claims all raise the same basic problem: The ordinance has an economic cost in that it threatens to exclude from the marketplace all but one alarm system provider.

After a hearing, the U.S. District Court denied the plaintiff companies' motion for preliminary injunction and further granted the defendants' motions to dismiss, concluding that the plaintiff companies had inadequately pleaded their federal claims. The plaintiff companies appealed.

The 7th Circuit began its analysis with the contracts clause claims against the village, Tyco and Northwest. Concerning Northwest and Tyco, the 7th Circuit noted that no claim against them can be

stated because they did not pass the underlying ordinance and the only way to violate the contracts clause is through legislative action.

However, concerning the contracts clause claim against the village, the 7th Circuit found that the plaintiff companies stated a plausible claim and should have been allowed to go forward; future issues to be addressed on remand include whether the village's proffered interests justify the ordinance.

In so holding, the 7th Circuit agreed with the district court and determined that the ordinance would create a significant impairment on the plaintiff companies' contractual rights, but disagreed with the district court that it was clear the village had significant and legitimate public purposes.

The result was that the contracts clause claim against the village was remanded and ultimately was the only claim left standing.

In remanding the contracts claim against the village, the 7th Circuit noted that the village is afforded some deference when it passes legislation that results in impaired contract rights, but how much deference the village gets depends on the impairment's severity and the village's self-interest.

The plaintiff companies' allegations concerning the early termination of contracts as well as the village's self-interest likely makes for minimal deference owed. Either way, concluded the 7th Circuit, the district court's determination was premature in regard to the motion to dismiss.

Accepting a possible claim against the village via the contracts clause, the 7th Circuit continued its analysis by reviewing the plaintiff companies' 14th

Amendment due process and equal protection claims.

The plaintiff companies acknowledge that their claims were not premised on either a fundamental right (for due process purposes) or a suspect classification (for equal protection purposes), so the ordinance needed only a rational basis in support of a legitimate interest.

The 7th Circuit noted that Tyco had already been Northwest's exclusive provider for five years prior to passage of the ordinance and continuing this relationship as opposed to risking safety with a new company is a legitimate interest.

Finally, the 7th Circuit reviewed the plaintiff companies' antitrust claims. To survive the defendants' motion to dismiss, the plaintiff companies needed to show either direct allegations or circumstantial evidence of a conspiracy.

The 7th Circuit noted that there was no direct evidence and the circumstantial evidence alleged in the complaint was lacking. Even though the village received financial benefit from a potential agreement between the defendants, it was clear the village would likely receive those benefits with or without a conspiracy.

Because the complaint failed to

plead a conspiracy, subsequent alleged antitrust claims, including monopolization through willful, anti-competitive acts, also failed. Though dismissal of the antitrust claims was upheld, the 7th Circuit did offer one plausible antitrust claim: A challenge to the exclusive contract entered into between Northwest and Tyco could be seen as an anti-competitive threat when it forecloses a substantial amount of competition.

But the 7th Circuit did not address this issue any further because the plaintiff companies did not challenge Northwest and Tyco's exclusive dealing.