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Compelling Signatories To Arbitrate With Non-Signatories

In his International Arbitration column, John Fellas discusses non-signatories to arbitration agreements, highlighting the issue that U.S. courts hold that a non-signatory may rely upon an arbitration clause against a signatory, but not the other way around. No U.S. case has fully articulated the rationale for this theory or fully explained why these two situations should be treated differently.

By **John Fellas**

This article is about non-signatories to arbitration agreements. The issue I address concerns a difference in the approach taken by U.S. courts when a non-signatory seeks to rely on an arbitration clause *against a signatory* versus when a *signatory* seeks to rely on an arbitration clause against a *non-signatory*. When it comes to one particular non-signatory theory—the "intertwined claims" estoppel theory (about which more below)—U.S. courts hold that a non-signatory may rely upon an arbitration clause *against a signatory*, but not the other way around.

In *Thomson-CSF, SA v. Am. Arb. Ass'n* , 64 F.3d 778 (2d Cir. 1995), the U.S. Court of Appeals for the Second Circuit articulated the approach of the courts in this way: "the circuits have been willing to estop a *signatory* from avoiding arbitration with a nonsignatory when the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed" (emphasis in original)—the inference being that courts would not estop a *non-signatory* from avoiding arbitration with a signatory on an intertwined estoppel theory. But no U.S. case has fully articulated the rationale for this theory or fully explained why these two situations should be treated differently. That is what I propose to do here.

Theories for Binding Non-Signatories

It is well-known that there are various different theories for holding that those who did not sign an arbitration agreement may be bound by, or permitted to rely upon, such agreement. Most of these theories are not specific to arbitration, but apply more generally to all types of contracts, and, as the Second Circuit put it in *Thompson-CSF*, "arise out of common law principles of contract and agency law." The court could have added principles of corporate law to this list. Thus, non-signatories have been permitted to rely upon, or have been held to be bound by, arbitration agreements under principles of contract law (e.g., incorporation by reference, assignment, assumption, the third party beneficiary doctrine), agency law (e.g., where an agent with actual or apparent authority can bind a non-signatory principal), or corporate law (e.g., where a subsidiary can bind a non-signatory parent corporation based upon a piercing of the corporate veil).

In addition to these principles, the doctrine of estoppel has also been relied upon by courts in the non-signatory context. And in *GE Energy Power Conversion Fr. SAS, Corp. v. Outokumpu Stainless U.S.,* 140 S. Ct. 1637 (2020), the Supreme Court recently held that the New York Convention does not preclude

JOHN FELLAS *is an arbitrator with Fellas Arbitration and an adjunct professor of law with New York University School of Law. He can be reached at fellas@fellasarbitration.com*

a non-signatory from relying upon domestic law doctrines of estoppel to enforce an arbitration agreement.

Estoppel Doctrines

There are at least two distinct types of estoppel doctrine that apply in the non-signatory context: the "direct benefits" estoppel theory and the "intertwined" estoppel theory. The direct benefits theory bears the hallmark of any estoppel doctrine—prohibiting a party from taking inconsistent positions or seeking to "have it both ways" by "rely[ing] on the contract when it works to its advantage and ignor[ing] it when it works to its disadvantage." *Tepper Realty Co. v. Mosaic Tile Co. ,* 259 F.Supp. 688, 692 (SDNY 1966).

The direct benefits doctrine reflects that core principle by preventing a party from claiming rights under a contract but, at the same time, disavowing the obligation to arbitrate in the same contract. As the Second Circuit stated in *MAG Portfolio Consult, GMBH v. Merlin Biomed Grp. LLC,* 268 F.3d 58, 61 (2d Cir. 2001), "where a company 'knowingly accepted the benefits' of an agreement with an arbitration clause, even without signing the agreement, that company may be bound by the arbitration clause."

By contrast, the intertwined estoppel theory looks not to whether any benefit was received by the non-signatory, but rather at the nature of the dispute between the signatory and the non-signatory, and, in particular, whether "the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped [signatory] party has signed." *Smith/Enron Cogeneration Ltd. P'ship, Inc. v. Smith Cogeneration Int'l, Inc.,* 198 F.3d 88, 98 (2d Cir. 1999). But this account of the intertwined estoppel theory raises an immediate question: what does it have to with estoppel?

As noted, the intertwined estoppel theory runs only one way; it operates only to estop *a signatory* from avoiding arbitration with a non-signatory. But it is hard to see why the estopped signatory is doing anything that should trigger the estoppel doctrine as it is traditionally understood. After all, the *signatory* is not in any way taking inconsistent positions or trying to have it both ways. If anything, it is *the non-signatory* who is trying to have it both ways.

Take a case where signatory A enters into an arbitration agreement with signatory B, and non-signatory X invokes the intertwined estoppel theory seeking to compel A to arbitrate. In resisting arbitration with non-signatory X, signatory A is not trying to have it both ways at all; A is not trying to take the benefit of one part of its contract with B, yet disavowing the rest. To the contrary, A is being perfectly consistent, and sticking precisely to the terms of the contract it entered into, saying in essence: "When I entered into an arbitration agreement, I agreed to arbitrate with signatory B, but never with non-signatory X, and I maintain that contractual position." Indeed, if anyone can be charged with trying to have it both ways, it is non-signatory X. Non-signatory X, who never agreed to arbitrate with A, now claims the benefit of the arbitration clause—and *only* the arbitration clause—contained in a contract to which it is not a party, in order to compel A to arbitrate.

But this only deepens the puzzle. After all, signatory A seeks only to adhere to the terms of its arbitration agreement, which did not include any agreement to arbitrate with non-signatory X. By contrast, non-signatory X claims the benefit of an arbitration clause in a contract it never entered, while, at the same time, not purporting to assume any obligations under that contract. Why is it that it is *signatory A* who should be *estopped* from arbitrating with non-signatory X?

Rationale for the Intertwined Estoppel Doctrine

The answer is that, despite it being labelled an "estoppel" theory, the intertwined estoppel doctrine applies despite the absence of the core features that typically trigger estoppel. Rather than being concerned with preventing a party from having it both ways, the true rationale underlying the intertwined estoppel theory is to preserve the efficacy of the arbitration process. It is no surprise, therefore, that the intertwined estoppel doctrine is not one of

general application, but, rather, has been developed by U.S. courts solely for the arbitration context.

That the intertwined estoppel theory has as its central aim the preservation of the efficacy of the arbitration process is clear when one looks at the typical fact pattern of an intertwined estoppel case. The theory normally finds its occasion when signatory A and signatory B have a dispute—as to which one or other party may have commenced arbitration proceedings—and signatory A commences a lawsuit against non-signatory X, in circumstances where *that dispute* is intertwined with the dispute between A and B. Non-signatory X then responds by asking the court to compel A to arbitrate, relying upon the arbitration clause in the agreement between A and B.

Without the intertwined estoppel doctrine, signatory A to an arbitration agreement could easily sidestep its arbitration agreement with signatory B by commencing a lawsuit against a non-signatory party who has some relationship with B—for example, an agent or employee or officer or board member of a corporation—in connection with the same dispute that is subject to the arbitration agreement. The Seventh Circuit expressed this precise concern in *Hughes Masonry v. Greater Clark Cty. Sch. Bldg*, 659 F.2d 836, 841 n.9 (7th Cir. 1981) (emphasis added):

"we believe Hughes [the signatory], in the peculiar circumstances before us, is estopped from denying J.A. [the non-signatory] the benefit of the arbitration clause with regard to claims that are as intimately founded in and intertwined with the underlying contract obligations as Hughes' claims appear to be here. The outcome urged by Hughes would have the tail wagging the dog, since *it would allow a party to defeat an otherwise valid arbitration clause simply by alleging that an agent of the party seeking arbitration has improperly performed certain duties under the contract* and thereby committed tort that is so integrally related to the subject of arbitration between the principal parties as to constitute a bar to such arbitration."

Similarly, in *J.J. Ryan Sons v. Rhone Poulenc Tex.,* S.A, 863 F.2d 315 (4th Cir. 1988), the Fourth Circuit permitted a non-signatory parent corporation to compel a signatory to arbitrate for the same reason (emphasis added):

"When the charges against a parent company and its subsidiary are based on the same facts and are inherently inseparable, a court may refer claims against the parent to arbitration even though the parent is not formally a party to the arbitration agreement … . *If the parent corporation was forced to try the case, the arbitration proceedings would be rendered meaningless and the federal policy in favor of arbitration effectively thwarted*."

The same rationale animated the court's decision in *Arnold v. Arnold Corp.*, 920 F.2d 1269, 1281 (6th Cir. 1990). In that case, a signatory to a stock purchase agreement with a corporation commenced a lawsuit against certain non-signatory officers and board members of that same corporation, as well as against the non-signatory broker-dealer that assisted in the stock purchase agreement. The Sixth Circuit affirmed the district court's decision to grant the non-signatories' motion to compel the signatory to arbitrate precisely to preserve the efficacy of the arbitration process. If the signatory "can avoid the practical consequences of an agreement to arbitrate by naming nonsignatory parties as [defendants] in his complaint, or signatory parties in their individual capacities only, the effect of the rule requiring arbitration would, in effect, be nullified."" (citation omitted).

It is submitted, therefore, that the rationale for the intertwined estoppel theory has little to do with estoppel as it is traditionally understood but, rather, is to ensure that parties to arbitration agreements do not undermine their effectiveness by commencing collateral litigation about disputes subject to arbitration. After all, when parties commit themselves to arbitration, they are agreeing to resolve a dispute by arbitration *instead of* litigation.

If parties to arbitration agreements were permitted to avoid their obligation to arbitrate by suing a non-signatory on a claim intertwined

with a dispute governed by an arbitration agreement, this would undermine the viability of the arbitration process. What would be the point in agreeing to resolve a dispute by arbitration if full-bore collateral litigation were an inevitable feature of it?

Why the Intertwined Estoppel Theory Operates as a One-Way Street

While this account of the rationale for the intertwined estoppel theory makes sense as a matter of policy, it bring us back to the fundamental question that we raised at the outset: why does the intertwined estoppel doctrine operate as one-way street, estopping only signatories, but not non-signatories? After all, if a signatory should be compelled to arbitrate with a non-signatory when the dispute between them is intertwined with a dispute subject to arbitration, why not the other way around?

The reason lies in the foundational principle of arbitration, namely, that it "is a matter of consent, not coercion" *Volt Info. Scis., Inc. v. Bd. of Trs.*, 489 U.S. 468, 479 (1989). When it comes to consent, there is a fundamental difference between, on the one hand, a court's decision to compel a signatory to arbitrate with a non-signatory and, on the other, a decision to compel a non-signatory to arbitrate with a signatory.

When a court grants non-signatory X's motion to compel arbitration of a dispute with signatory A (who signed an arbitration agreement with signatory B), there is some element of consent on both sides. First, even though X never signed an arbitration agreement with A, through its motion to compel, X is expressing its consent to arbitrate a dispute with A that is intertwined with the dispute that A agreed to arbitrate with B. Second, while signatory A did not specifically consent to arbitrate with non-signatory X, it did consent to arbitrate a dispute with B that is intertwined with its dispute with X.

Consider the reverse situation, however, where signatory A seeks to compel non-signatory X to arbitrate a dispute that is intertwined with a dispute covered by A's arbitration clause with B. While A—through both its arbitration agreement with B and its motion to compel—expresses its consent to arbitrate both a dispute with B and an intertwined dispute with non-signatory X, X has never expressed any consent to arbitrate with anyone.

Thus when a non-signatory seeks to compel a signatory to arbitrate, there is some element of consent on both sides. By contrast, when a signatory seeks to compel a non-signatory to arbitrate, there is only consent on one side—by the signatory. In *Thomson-CSF*, the Second Circuit affirmed the district court's decision to deny a signatory's motion to compel a non-signatory to arbitrate on an intertwined estoppel theory precisely because "[a]t no point did Thomson [the non-signatory] indicate a willingness to arbitrate with E S [the signatory]. Therefore, the district court properly determined these estoppel cases to be inapposite and insufficient justification for binding Thomson to an agreement that it never signed."

Conclusion

It is worth stressing, however, that the intertwined estoppel doctrine sits uneasily with the foundational principle of arbitration noted above—namely that arbitration "is a matter of consent, not coercion." Yes, it is the case that signatory A agreed to arbitrate a dispute with signatory B. And it is also the case that the dispute non-signatory X seeks to arbitrate with signatory A is factually intertwined with the dispute that A agreed to arbitrate with B.

However, the inescapable fact remains that A never specifically agreed to arbitrate any dispute with non-signatory X. Notwithstanding the absence of this robust form of consent, in applying in intertwined estoppel doctrine, the primary aim of the courts is to preserve the efficacy of the arbitration process, by ensuring that a party who entered into an arbitration agreement does not avoid its obligation to arbitrate by commencing collateral litigation against a non-signatory to that agreement.