BUT I DIDN’T SIGN AN ARBITRATION AGREEMENT!

By Bruce E. Meyerson

Every student of arbitration knows that arbitration is a matter of contract law. This means, ordinarily, that “a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.” *AT & T Technologies Inc. v. Communications Workers of Am.*, 475 U.S. 643, 648 (1986).

But, despite this hornbook principle, there is a growing trend by courts to make arbitration provisions binding even on parties who never signed an arbitration agreement. This trend is the result of two factors. First, courts have relied upon common law contract and agency principles to extend the both the obligation and the opportunity to arbitrate to noncontracting parties. Second, for the many disputes that fall under the Federal Arbitration Act, some courts have relied upon the strong federal policy favoring arbitration. In accordance with this policy, the parties’ intentions “are generously construed as to issues of arbitrability,” *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985), and any “ambiguities as to the scope of the arbitration clause itself” must be resolved in favor of arbitration. *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 476 (1989). Of course, these rules are not without their limits, as the presumption of arbitrability may be overcome with “clear evidence” that the parties did not intend a claim to be arbitrable. *Harvey v. Joyce*, 199 F.3d 790 (5th Cir. 2000).

Some courts, however, have properly observed that it is incorrect to cite the federal policy favoring arbitration in cases of nonsignatories. “[F]ederal policy favoring arbitration does not apply in a situation like this when a court is determining whether an agreement to arbitrate exists. Rather it applies when a court is determining whether the dispute in question falls within the scope of the arbitration agreement already found to exist.” *California Fina Group, Inc. v. Herrin*, 379 F.3d 311, 316 n. 6 (9th Cir. 2004); e.g., *Fleetwood Enterprises, Inc. v. Gaskamp*, 280 F. 3d 1069, 1073 (5th Cir. 2002).

The purpose of this article is to examine the theories that courts have relied upon to extend the obligation (or the right) to arbitrate to parties regardless of whether they have actually signed an arbitration agreement. There is a preliminary question that must be answered, however—when a dispute arises over whether a nonsignatory should be compelled to arbitrate, who decides that dispute, an arbitrator or a judge?

Who Decides Whether a Nonsignatory is Bound to Arbitrate?

Although courts have expanded greatly the power of arbitrators to decide issues of arbitrability, the initial question of whether a party is bound by an arbitration agreement remains one for a court to decide. *John Wiley & Sons, Inc. v. Livingston*, 376 U.S. 543 (1964). The holding in *John Wiley & Sons* was reaffirmed by the United States Supreme

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Court in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002) where the court explained that “a gateway dispute about whether parties are bound by a given arbitration agreement clause [is] for a court to decide.” *Id.* at 84. Following this principle, the Court of Appeals for the Federal Circuit has held that it is up to a court to determine whether a nonsignatory successor corporation was bound by an arbitration agreement signed by its predecessor. *Microchip Technology Inc. v. U.S. Philips Corp.*, 367 F.3d 1350 (Fed. Cir. 2004).

There are circumstances, however, when issues of arbitrability involving a nonsignatory are decided by the arbitrator. Where parties clearly and unmistakably demonstrate their intent that an arbitrator is to decide arbitrability, the United States Supreme Court has held that arbitrators, not courts, should determine arbitrability. *First Options of Chicago v. Kaplan*, 514 U.S. 938 (1995). The Second Circuit Court of Appeals, citing this principle, held in *Contec Corp. v. Remote Solutions Co.*, 398 F.3d 205 (2d Cir. 2005), that an arbitrator should decide if a nonsignatory should be made subject to arbitration.

Contec Corp. was a successor to Contec L.P., a party to a contract with Remote Solutions (“Remote”) that contained an arbitration provision. In a dispute between Contec Corp. and Remote, Remote opposed arbitration because Contec Corp. was not a party to the original contract. The court of appeals first considered whether a court or an arbitrator should decide whether the dispute between Remote and Contec Corp. was arbitrable. The original arbitration agreement incorporated the American Arbitration Association commercial rules which provide that an arbitrator is to determine “his or her own jurisdiction, including any objections with respect to the existence, scope or validity of the arbitration agreement.” AAA Rule R-7 (a). The appellate court concluded that the issue of whether Contec Corp., a nonsignatory to the arbitration agreement, could compel arbitration with Remote, was a dispute pertaining to the “existence, scope or validity” of the arbitration agreement and therefore it was to be resolved by an arbitrator, not a court.

Importantly, the court recognized that just because a signatory to an arbitration agreement has agreed to arbitrate issues of arbitrability with another party, that does not mean that it must arbitrate with any nonsignatory. The court found that it must first determine whether the “parties have a sufficient relationship to each other and to the rights created under the agreement.” 398 F.3d at 209. Here the court found that there was an “undisputed” relationship between each corporate form of the original parties to the agreement and further, the dispute arose because the parties continued to conduct themselves in accordance with the terms of that agreement. Thus, the court found that a sufficient relationship existed between the parties and it was therefore proper for the court to consider whether Remote should be required to have an arbitrator determine the question of arbitrability. 2

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2 The court in *Contec Corp.* relied upon for support the decision of the First Circuit Court of Appeals in *Apollo Computer v. Berg*, 886 F.2d 469 (1st Cir. 1989). There, in accordance with a “broad form” arbitration agreement in a contract between Apollo and a Swedish company referred to as Dico in the opinion, the court said it was up to an arbitrator to decide whether claims between Apollo and Berg, an assignee of Dico, were arbitrable.
There are a variety of theories upon which courts have relied to permit or impose arbitration on behalf of parties who have not signed an arbitration agreement. These theories derive from the general rule set forth in Section 2 of the Federal Arbitration Act that arbitration agreements are enforceable and revocable on terms applicable to contracts generally. Thus, the doctrines making arbitration agreements binding upon nonsignatories find their source in ordinary contract and agency principles. Thomson-CSF, S.A. v. American Arbitration Ass’n, 64 F.3d 773 (2d Cir. 1995); Letizia v. Prudential Bache Securities, Inc., 802 F.2d 1185 (9th Cir. 1986). Courts generally have been consistent in following these rules. For example, in Thomson-CSF, S.A. v. American Arbitration Ass’n, the appellate court reversed the trial court which found a nonsignatory subject to arbitration without regard to agency or contract rules. The court of appeals held that the district court’s “hybrid approach dilutes the safeguards afforded to a nonsignatory . . . and fails to adequately protect parent companies, the subsidiaries of which have entered into arbitration agreements.” Id. at 780.

The Second Circuit Court of Appeals recently vacated the confirmation of an arbitration award concluding that the arbitrators erred in making a nonsignatory subject to arbitration and in not following established contract or agency law. Sarhank Group v. Oracle Corp., 404 F.3d 657 (2d Cir. 2005). In that case, Sarhank had entered into a contract with Oracle Systems, Inc., a wholly-owned subsidiary of Oracle Corp. The contract contained an arbitration provision. A dispute arose and Sarhank demanded arbitration against both Oracle Systems and Oracle Corp. Oracle Corp. was not a signatory to the agreement with Sarhank, nor did it execute any written agreement to arbitrate with Sarhank. The appellate court first ruled that the district court was required to determine whether Oracle Corp. had agreed to arbitrate. The appellate court noted that the basis of the arbitrators’ ruling was Egyptian law. Because the proceeding was one to enforce the award in the United States, the court found that American federal arbitration law governed. The court held that an “American nonsignatory cannot be bound to arbitrate in the absence of a full showing of facts supporting an articulable theory based on American contract law or American agency law.” Id. at 662.

It is not always necessary to consider one of the following theories which describe the circumstances when a nonsignatory may compel, or may be compelled, to arbitrate. In some instances the arbitration agreement itself may provide the answer. For example, in Sherer v. Green Tree Servicing LLC, 548 F.3d 379 (5th Cir. 2008), the court of appeals held that a party to an arbitration agreement could be compelled to arbitrate with a nonsignatory where that party had agreed to arbitrate any claim arising from “the relationships which result from th[e] [a]greement.” Id. at 382. In that case the court held that such a relationship existed between Green Tree, a loan servicing company, and Sherer, a party who executed a loan served by Green Tree. The court concluded it did
not need to consider theories such as equitable estoppel because the arbitration agreement executed by Green Tree obligated it to arbitrate with certain nonsignatories such Sherer.

Theories on Which Nonsignatories Have Compelled, or Have Been Held Subject to, Arbitration

**Alter Ego.** Although a corporate relationship or affiliation alone rarely has been held sufficient to bind a nonsignatory to an arbitration agreement, there are circumstances where, under applicable state law principles, the relationship between a corporation and a subsidiary may be sufficient to justify piercing the corporate veil to thereby hold a nonsignatory corporation subject to the arbitration agreement of another corporate entity. *E.g.*, *MAG Portfolio Consultant GMBH v. Merlin Biomed Group LLC*, 268 F.3d 58 (2d Cir. 2001). Because of the difficulty generally in establishing the factual basis to pierce the corporate veil, most cases considering this doctrine have not found the nonsignatory to be subject to the arbitration agreement. *E.g.*, *InterGen, N.V. v. Grina*, 344 F. 3d 134 (1st Cir. 2003); *Bridas S.A.P.I.C. v. Government of Turkmenistan*, 345 F.3d 347, 359 (5th Cir. 2003).

The Fourth Circuit, however, has adopted an expansive version of this doctrine, holding that where allegations against a parent corporation 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. *Long v. Silver*, 248 F.3d 309 (4th Cir. 2001); *J. J. Ryan & Sons v. Rhone Poulenc Textile, S.A.*, 863 F.2d 315 (4th Cir. 1988). Similarly, where a nonsignatory has been sued as the alter ego to a signatory to an arbitration agreement, the nonsignatory was permitted to compel arbitration. *Rowe v. Exline*, 63 Cal. Rptr. 3d 787 (App. 2007).

**Equitable Estoppel.** Equitable estoppel is a doctrine which applies where a party is seeking to preclude another party from asserting rights he otherwise would have had against another when his own conduct renders assertion of those rights contrary to equity. The equitable estoppel doctrine has been applied in a number of permutations in the area of arbitration by nonsignatories. *See generally R. J. Griffin & Co. v. Beach Club II Homeowners Ass’n*, 384 F.3d 157 (4th Cir. 2004); *contra DSMC Inc. v. Convera Corp.*, 349 F.3d 679 (D.C. Cir. 2003). As one court stated, the “linchpin for equitable estoppel is equity—fairness.” *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524 (5th Cir. 2000).

One application of the doctrine is where a party to an arbitration agreement has been held to be “estopped” from refusing to arbitrate with a nonsignatory where issues between the parties are “intertwined” with the agreement containing an arbitration provision. *Smith/Enron Cogeneration Ltd. Partnership, Inc. v. Smith Cogeneration Int’l, Inc.*, 198 F. 3d 88 (2d Cir. 1999). A common example of this situation is found in *Letizia v. Prudential Bache Securities, Inc.*, 802 F. 2d 1185 (9th Cir. 1986). After suit was filed against two brokerage account executives, they successfully moved to compel arbitration based upon an arbitration provision in the brokerage agreement. The plaintiff contended that his action against the individual account executives should not be subject to
arbitration because those individuals had not signed the arbitration agreement he signed with the brokerage firm. The court of appeals disagreed noting that all of the allegedly wrongful acts related to the handling of the securities account which contained the arbitration agreement.

In several circuits equitable estoppel has been limited to situations where a nonsignatory seeks to compel arbitration against a signatory to an arbitration agreement, *Javitch v. First Union Sec., Inc.*, 315 F.3d 619 (6th Cir. 2003); *E. I. Dupont de Nemours & Co. v. Rhone Poulenc Fiber & Resin Intermediates S.A.S.*, 269 F.3d 187 (3d Cir. 2001). The reluctance of courts to expand this doctrine to compelling nonsignatories to arbitrate was explained by the United States Court of Appeals for the Fifth Circuit. In *Bridas S.A.P.I.C. v. Government of Turkmenistan*, 345 F.3d 347 (5th Cir. 2003), the court of appeals founds that the “simple fact” that the claims between the parties are “inextricably intertwined . . . is insufficient, standing alone to justify the application of equitable estoppel. . . . Were this to become the case, this expanded version of equitable estoppel would ‘threaten to overwhelm the fundamental premise that a party cannot be compelled to arbitrate a matter without its agreement.’” *Id.* at 361. Similarly, a nonsignatory was not compelled to arbitrate “simply because the signatory alleges a common scheme involving the nonsignatory and another signatory.” *World Rentals & Sales, LLC v. Volvo Constr. Equip. Rents, Inc.*, 2008 WL 466127, *9 (11th Cir. 2008).

In a growing number of cases, however, signatories to arbitration agreements have been permitted to compel nonsignatories to arbitrate. One of the leading cases adopting this version of the equitable estoppel doctrine is *M.S. Dealer Serv. Corp. v. Franklin*, 177 F.2d 942 (11th Cir. 1999). In that case, the court recognized two circumstances when signatories would be able to compel nonsignatories to arbitrate. First, “equitable estoppel applies when the signatory to a written agreement containing an arbitration clause must rely on the terms of the written agreement in asserting its claim against the nonsignatory.” *Id.* at 947; see also *Rowe v. Exline*, 63 Cal. Rptr. 3d 787 (App. 2007)(nonsignatories could compel arbitration where the claims against them presume the existence of and are intertwined with the contract containing an arbitration clause). Second, the doctrine should apply “when the signatory to the contract containing an arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the nonsignatory and one or more signatories to the contract.” *Id.*

In that case, a consumer purchased a car under a contract which incorporated a Retail Installment Contract with MS Dealer. After the consumer brought suit against both the seller and MS Dealer, MS Dealer moved to compel arbitration. The court of appeals held that because the plaintiff alleged collusive behavior on the part of the defendants, and because the customer’s obligation to pay certain charges arose from the purchase contract which contained the arbitration clause, the consumer was estopped from avoiding arbitration.

In other situations, courts have permitted a signatory to bind a nonsignatory to a contract containing an arbitration clause where the claims made by the nonsignatory
arose out of and related directly to the agreement containing an arbitration provision Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc., 10 F.3d 753 (11th Cir. 1993); see Dominium Austin Partners, L.L.C. v. M. J. Emerson, 248 F.3d 720 (8th Cir. 2001). In another variation of this theme, signatories to arbitration agreements have been able to compel nonsignatories to arbitrate where the nonsignatory, during the term of the contract, has “embraced” the contract, but then during litigation attempts to repudiate the arbitration clause in the contract. E.I. DuPont de Nemours & Co. v. Rhone Poulenc Fiber & Resin Intermediates, S.A.S., 269 F.3d at 200; e.g., InterGen N.V. v. Grina, 344 F.3d 134 (1st Cir. 2003). Similarly, a nonsignatory to an arbitration agreement was compelled to arbitrate where it raised claims against a party based on that party’s breach of an agreement which provided for arbitration. International Ins. Agency Serv., LLC v. Revis Reinsurance U.S., Inc., 2007 WL 951943 (N.D. Ill. Mar. 27, 2007); see Ritter v. Grady Automotive Group, Inc., 2007 WL 1454458 (Ala. Sup. Ct. 2007)(spouse of accident victim was compelled to arbitrate a loss of consortium claim where he alleged that the defendant was liable, in part, because of the breach of a contract containing an arbitration provision).

Other courts have held that where a nonsignatory receives a benefit from a contract containing an arbitration provision it is estopped from refusing to comply with the arbitration clause. International Paper Co. v. Schwabedissen Maschinen & Anlagen GMGH, 206 F.3d 411 (4th Cir. 2000). Courts appear to require a “direct” benefit in contrast to an indirect benefit. Javitch v. First Union Sec., Inc., 315 F.3d 619 (6th Cir. 2003). For example, in Bouriez v. Carnegie Mellon University, 359 F.3d 292 (3d Cir. 2004), the appellate court refused to find a minority shareholder of a corporation which was a party to an arbitration agreement was not bound to arbitrate a dispute relating to the agreement where there was no showing that any benefit of the project in dispute would “go to him directly.” Id. at 295; see also Nitro Dist., Inc. v. Alticor, Inc., 453 F.3d 995 (8th Cir. 2006); (benefit to nonsignatories was “at best, indirect and insufficient to support estoppel); Zurich American Ins. Co. v. Watt Indus., Inc., 417 F. 3d 682 (7th Cir. 2005); Truck Ins. Exch. V. Palmer J. Swanson, Inc., 189 P.3d 656 (Nev. 2008)(nonsignatory did not directly benefit from the agreements which provided for arbitration).

The Texas Supreme Court applied the direct benefit standard, requiring a nonsignatory to arbitrate in In re Weekley Homes, 180 S.W.2d 327 (Tex. 2005). In that case, Forsting entered into a construction contract with Weekley, which contained an arbitration clause. After closing, Forsting transferred the home to his family trust, whose sole beneficiary was Von Bargen, his only child. A dispute arose regarding the construction of the home and Weeley undertook repairs. Von Bargen handled all matters relating to the house, the construction problems, the warranty work and the negotiations. When she brought suit against Weekley claiming that dust during the repairs caused her to contract asthma, Weekley moved to compel arbitration. The Texas Supreme Court found that Von Bargen was a direct beneficiary of the construction contract based upon her exercise of rights under the contract and her equitable entitlement to other contractual benefits.
Agency.  Traditional principles of agency law may also bind a nonsignatory to an arbitration agreement. In *Arnold v. The Arnold Corp.*, 920 F.2d 1269 (6th Cir. 1990), the court permitted officers and agents of the defendant corporation to invoke the arbitration agreement in a contract signed on behalf of the corporation, citing the “well-settled principle affording agents the benefits of arbitration agreements made by their principal.” *Id.* at 1282.

It also has been held that an agent can commit its nonsignatory principal to an arbitration agreement. *InterGen N.V. v. Grina*, 344 F.3d 134 (1st Cir. 2003). On the other hand, a nonsignatory cannot compel arbitration merely because he is an agent of a party who is a signatory to an arbitration agreement. *Westmoreland v. Sadoux*, 299 F.3d 462 (5th Cir. 2002), and an agent who signs an arbitration agreement for a disclosed principal may not be bound to arbitrate personally. *Flink v. Carlson*, 856 F.2d 44 (8th Cir. 1998).

Third Party Beneficiary. Courts have consistently recognized that nonsignatory third-party beneficiaries under an agreement containing an arbitration provision may compel arbitration against signatories of the arbitration agreements. *Washington Square Sec., Inc. v. Aune*, 385 F.3d 432 (4th Cir. 2004); *John Hancock Life Ins. v. Wilson*, 254 F.3d 48 (2d Cir. 2001). The general rule, however, is that the contract containing the arbitration provision must reflect an intent to confer a direct benefit on the third party; merely being affected by the contract or having an interest in the contract is insufficient. *Fleetwood Enterprises, Inc. v. Gaskamp*, 280 F. 3d 1069, 1075 (5th Cir. 2002).

Incorporation by Reference. A nonsignatory may compel arbitration against a party to an arbitration agreement when that party has entered into a separate contractual agreement with the nonsignatory which incorporates an agreement containing the arbitration clause. *Thomson-CSF, S.A. v. American Arbitration Ass’n*, 64 F.3d 773 (2d Cir. 1995). An arbitration clause can be incorporated even if the relevant language does specifically refer to it. *World Rentals & Sales, LLC v. Volvo Constr. Equip. Rents, Inc.*, 2008 WL 466127 (11th Cir. 2008).

For example, in *Weathergard Roofing, Co., Inc. v. D. R. Ward Constr. Co., Inc.*, 1 CA-CV 05-0247 (Ariz. App. Feb. 27, 2007), the Arizona Court of Appeals applied the doctrine of incorporation by reference in a construction dispute. After the owner made a demand for arbitration and sought indemnity from the roofing subcontractor. The roofing subcontractor participated in arbitration but preserved its right to subsequently argue that it was not bound by the arbitration provision in the contract between the owner and the general contractor. The court of appeals disagreed citing the doctrine of incorporation by reference.

The subcontract between the general contractor and the roofing subcontractor provided that the subcontractor “shall assume and agree to perform all obligations of [the general] Contractor in the General Contract . . . and shall assume toward Contractor all of the obligations and responsibilities which Contractor assumes toward Owner under the General Contract.” The court found that this language in the subcontract was sufficient
to incorporate the arbitration provision in the prime contract. And because the general contractor was given the same “rights and privileges” against the subcontractor that the owner had against the general contractor, the court reasoned that just as the owner had the right to demand arbitration of the general contractor, the general contractor had the right to demand arbitration against the subcontractor.

**Assumption by Conduct.** A party may be bound by an arbitration clause if its subsequent conduct indicates that it is assuming the obligation to arbitrate. *Gvozdenovic v. United Air Lines, Inc.*, 933 F.2d 1100, 1105 (2d Cir. 1991).

**Conclusion**

The expansion of arbitration to nonsignatories is a rather recent development, undoubtedly related to the growth of arbitration in general. If parties wish to avoid inadvertently becoming subject to an arbitration agreement, they should be aware of these theories and principles, and act accordingly. On the other hand, parties who have not signed an arbitration agreement may deem it in their best interest to be in arbitration. These cases offer guidance on the circumstances when that may be accomplished.