

Non-signatories in Arbitration Proceedings With Focus on a Third Party Beneficiary and Equitable Estoppel Doctrines in the United States

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The United States has used legal theoretical constructions such as equitable estoppel and the third party beneficiary under which non-signatories of an arbitration agreement can be bound to the arbitration agreement of others.¹⁾ The third party beneficiary theory has been used when a signatory defendant argues that a non-signatory plaintiff is bound by an arbitration agreement, or a non-signatory defendant argues that a signatory plaintiff is required to arbitrate the plaintiff's claims against the non-signatory. On the other hand, equitable estoppel has developed as two distinct theories. According to the first theory, if a non-signatory party knowingly accepted the benefits of an agreement, it can be estopped from denying its obligation to arbitrate. The second theory compels a signatory to arbitrate because of the close relationship between the entities involved and the fact that the claims were intimately founded in and intertwined with the underlying contract obligations.

Key Words : Non-signatory, Third Party Beneficiary, Equitable Estoppel, Strand A and B, Intertwined-ness Test, Direct Benefits

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1) James M. Hosking, "The third party non-signatory's ability to compel international commercial arbitration: Doing justice without destroying consent." *Pepperdine Dispute Resolution Law Journal* vol. 4 issue 3, 2004, pp. 484-90, fn 48, 49.

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I. Introduction

In an arbitration proceeding, only those persons or entities having entered into an arbitration agreement can participate in the arbitration proceeding and will be bound by the ensuing arbitral award. By contrast, in litigation, any persons or entities having legal interests can commence court proceedings to protect their interests. Compared to litigation, the principal of procedural party autonomy and the contractual basis of arbitration make arbitration a more useful resolution mechanism, thus contributing to the increasing popularity of arbitration in the international commercial community.

On the other hand, business transactions, especially in the international context, have become complicated, and many affiliates or branches, their directors or stockholders, are required to play a substantial role in entering into a contract concluded by one company of the multinational groups. However, multiparty transactions are frequently entered into via several bilateral contracts which include a bilateral dispute resolution clause of arbitration. Consequently, a dispute arising between two legal entities bound by an arbitration agreement regarding a multiparty project is forced to be resolved by arbitration between these two parties of the arbitration agreement. Other parties are not allowed to participate in that arbitration proceeding, even if they play an active role in a specific project. Non-signatories of arbitration agreements may be bound by the agreement under ordinary contract and agency principles.²⁾

In order to protect third party interest in arbitration, the United States federal courts have set forth theories for binding non-signatories: incorporation by reference, assumption, agency, veil-piercing/alter ego, estoppel, and third party beneficiary under

2) *McAllister Bros., Inc. v. A & S Transp. Co.*, 621 F.2d 519, 524 (2d Cir.1980); *Thomson-CSF, S.A. v. Am. Arbitration Ass'n*, 64 F.3d 773, 776 (2d Cir.1995).

which non-signatories of an arbitration agreement can be bound to the arbitration agreement of others.³⁾ This article reviews the legal theories and case law of the United States employed to resolve the third party problem in arbitration proceedings, focusing on a third party beneficiary and equitable estoppel doctrines.

II. Third Party Beneficiary Doctrine in the United States

1. Basic Concept of Third Party Beneficiary Doctrine

Many U.S. courts have recognized a non-signatory's status as a third party beneficiary to a contract which includes an arbitration agreement as a ground for binding the non-signatory to the agreement, especially when the contracting parties intend the non-signatory to directly benefit from the contract.⁴⁾ The third party beneficiary theory has been used when a signatory defendant argues that a non-signatory plaintiff is bound by an arbitration agreement, or a non-signatory defendant argues that a signatory plaintiff is required to arbitrate the plaintiff's claims against the non-signatory.⁵⁾ The U.S. courts have referred to the Restatement (Second) of Contracts in defining intended beneficiaries and distinguishing incidental beneficiaries.⁶⁾ Any beneficiary not identified in § 302 is an incidental beneficiary which lacks power to enforce obligations created by a promise made for its benefit.⁷⁾ Whether a third party is considered an intended

3) Se-Won Suh, "Enforcement of Arbitral Agreement to Non-signatory in America," *Journal of Arbitration Studies*, vol. 18, no. 1, 2008, p. 92; *The Rice Company (Suisse), S.A. v. Precious Flowers Ltd.* 523 F.3d 528, 536-37 (5th Cir. 2008); *Thomson-CSF, S.A. at 776*; *Hughes Masonry Co., Inc. v. Greater Clark County School Building Corp.* 659 F.2d 836, at 836-37 (7th Cir. 1981).

4) Dwayne E. Williams, "Binding non-signatories to arbitration agreements," *Franchise Law Journal* Vol. 25, 2006, pp. 175-79, fn. 20. *InterGen N.V. v. Grina*, 344 F.3d 134, 146 (1st Cir. 2003) (A third party beneficiary of a contract containing an arbitration clause can be subject to that clause and compelled to arbitrate on the demand of a signatory.)

5) James Otis Rodner, Angélica Marcano, "Jurisdiction of the Arbitral Tribunal in the Case of Multiple Contracts," *Journal of Arbitration Studies*, vol. 24, no. 3, 2014, pp. 1-31.

6) RESTATEMENT (SECOND) OF THE LAW OF CONTRACTS § 302 (1981).

(1) A beneficiary of a promise is an intended beneficiary if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either

(a) the performance of a promise will satisfy an obligation of the promisee to pay money to the beneficiary; or

(b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.

third party beneficiary or incidental third party beneficiary will depend upon the contractual language and the surrounding facts and circumstances when the contracting parties sign the contract.⁸⁾

2. Third Party Beneficiary in the Business Acquisition Context

U.S. courts have looked at the language of a contract whether the language clearly and unambiguously expresses the contracting parties' intent to bind the non-signatories. In line with this reasoning, the courts rejected to apply third party beneficiary doctrine against non-signatories in the cases of *Bridas S.A.P.I.C. v. Government of Turkmenistan*⁹⁾ and *InterGen N.V. v. Grina*.¹⁰⁾

The *Bridas* case was related to a joint venture agreement. An Argentinian corporation brought action to confirm an international arbitration award rendering in its favor against the government of Turkmenistan and oil company wholly owned by government, arising out of joint venture agreement (the "JVA") to conduct hydrocarbon operations in Turkmenistan.¹¹⁾ The court reasoned that the JVA did not evince the requisite clear intent to benefit the Government of Turkmenistan when an instrumentality of a sovereign entered into a contract to develop Turkmenistan's natural resources.¹²⁾

The *Bridas* court mentioned that contracting parties are presumed to be contracting for themselves only, and this presumption may be overcome only if the intent to make a non-signatory a third party beneficiary is clearly written and evinced in the contract.¹³⁾ The court held that this presumption was not rebutted because the contract's integration clause clearly specified the terms of the contract to the parties, which were defined as the "Turkmenian Party" and the "Foreign Party."¹⁴⁾ Further, the court noted that we are again reluctant to bind the Government to the terms of the JVA on a third-party beneficiary theory because the Government has never filed a claim against

7) *Id.* § 302(2).

8) *Id.* § 302, cmt. (a).

9) *Bridas S.A.P.I.C. v. Government of Turkmenistan*, 345 F.3d 347 (2003).

10) *InterGen* at 135.

11) *Bridas* at 347.

12) *Id.* at 361.

13) *Id.*

14) *Id.*

Bridas premised upon the agreement, or otherwise sought to enforce its terms.¹⁵⁾

In InterGen case, the court held that third party beneficiary theory did not require a nonsignatory to arbitrate.¹⁶⁾ InterGen concerned a dispute arising from investment projects with purchase orders and technical services in an ongoing business relationship. InterGen's dispute arose from a series of contractual relationships in relation to the purchase of gas turbines for electrical generating stations owned by subsidiaries of InterGen.¹⁷⁾ An InterGen affiliate, Bechtel Limited, purchased the turbines for the projects pursuant to purchase order agreements with Alstom Power Generation ("APG"), a subsidiary of Alstom Power. At the same time, the InterGen subsidiaries that owned the projects signed support agreements with APG. Both the purchase orders and the support agreements contained arbitration clauses requiring that disputes between the Buyer as Bechtel, and the Seller as APG, be resolved by arbitration.¹⁸⁾ When the generators did not work well, InterGen sued Alstom Power, its agent Grina, and its affiliate Alstom Power, all of whom were non-signatories to the purchase orders and contracts.¹⁹⁾

The court rejected Alstom Power's argument that InterGen was a third party beneficiary of the purchase orders and contracts. The court noted that the law requires "special clarity" to support a finding that contracting parties intended to confer a benefit on a third party, and that the court focused on the specific terms of the purchase orders.²⁰⁾ According to the language of the two purchase orders, the court noted that each purchase order's arbitration clause applied only to "any and all controversies, disputes, or claims between Buyer and Seller wherein the words 'Buyer' and 'Seller' were explicitly defined as Bechtel and APG." Therefore, the court said, InterGen could not be considered as third party beneficiary of the purchase orders and contracts.²¹⁾ Further, the integration clauses in each of the purchase orders precluded the extension of the contracts to third parties.²²⁾

15) Id. See, e.g., *DuPont*, 269 F.3d at 192; *Industrial Electronics Corp. of Wisconsin v. iPower Distribution Group, Inc.*, 215 F.3d 677 (7th Cir,2000).

16) *InterGen* at 146-47.

17) Id. at 134-36.

18) Id. at 138-39.

19) Id. at 140-41.

20) Id. at 146.

21) Id. at 147.

22) Id. at 146-47.

Thus, parties need to pay attention to the language of the arbitration clause and to make sure the language is broad enough to include the intended beneficiaries if parties want to provide the status of a third party beneficiary of an arbitration clause with non-signatories. Further, parties should avoid using the language limiting the arbitration clause to disputes such as between the “parties.”

3. Third Party Beneficiary in Franchise Cases

Two franchise class action cases in *Collins v. International Dairy Queen* show the importance of contractual language in deciding whether non-signatories are bound or entitled to arbitrate.²³⁾ In *Collins*, Dairy Queen franchisees and subfranchisees filed a class action lawsuit against American Dairy Queen Corporation (ADQ) and its parent corporation, International Dairy Queen, Inc. (IDQ).²⁴⁾ Class I and Class II were two types of franchisees under franchise agreements containing arbitration provisions. Class I was the type of the class members who contracted directly with ADQ, and Class II was that of the class members as “subfranchisees” who obtained their franchises from “Territory Operators,” master franchisees that ADQ authorized to grant sublicenses in their territories. ADQ and IDQ were not parties to the subfranchise agreements between the Territory Operators and the subfranchisees, although ADQ reserved the right to approve the agreements.²⁵⁾

The Dairy Queen defendants, ADQ and IDQ, sought to exclude from the plaintiff class all franchisees and subfranchisees whose agreements required arbitration. Dairy Queen raised several defenses in the court: As the parent of ADQ, could IDQ rely on the arbitration clauses in ADQ’s franchise agreements? Were the members of the Poole subclass bound by the arbitration clauses contained in their franchise agreements? Could ADQ and IDQ invoke the arbitration clauses in the subfranchise agreements? Were the subfranchisees bound to the arbitration clauses contained in ADQ’s master franchise agreements with the Territory Operators?²⁶⁾ These questions were resolved by

23) *Collins v. Int’l Dairy Queen, Inc.*, 169 F.R.D. 690 (M.D. Ga. 1997); *Collins v. Int’l Dairy Queen, Inc.*, 2 F. Supp. 2d 1465 (M.D. Ga. 1998).

24) 169 F.R.D. 690; 2 F.Supp. 2d 1465.

25) 169 F.R.D. at 693; 2 F. Supp. 2d at 1467-68.

26) *Williams* at 175.

the Collins court in two separate decisions in 1997 and 1998.

In its first decision, the court held that IDQ was entitled to rely on the arbitration provisions contained in the agreements between ADQ and the plaintiffs because the allegations against the ADQ and its parent, IDQ, were “based on the same facts,” and were “inherently inseparable.”²⁷⁾ Second, the court held that ADQ and IDQ were not entitled to rely on the arbitration provisions in the subfranchise agreements to prevent the subfranchisees from getting notice of the class action because the provisions were applicable only to the parties.²⁸⁾

In its second decision, the Collins court granted, in part, Dairy Queen’s motion to keep certain subfranchisees’ claims pending arbitration, based on the arbitration clauses contained in certain subfranchise and master franchise agreements.²⁹⁾ Considering the clause in Form 302A, which limited arbitration to “any dispute between the parties hereto,” the court stated that the “general language ‘between the parties’” lacked “the certainty of the more precise language, indicating by name the intended beneficiaries and/or the party entitled to invoke arbitration.”³⁰⁾

III. Equitable Estoppel Doctrine in the United States

1. Origins of the Equitable Estoppel Doctrine

Equitable estoppel, as applied in compelling arbitration, has developed as two distinct theories. According to the first theory, called as the direct benefits theory (Strand A), if a non-signatory party knowingly accepted the benefits of an agreement, it can be estopped from denying its obligation to arbitrate.³¹⁾ The second theory compels a signatory to arbitrate because of the close relationship between the entities involved, as well as the relationship of the alleged wrongs to the non-signatory’s

27) 169 F.R.D. at 692-93.

28) *Id.* at 693.

29) 2 F. Supp. 2d 1468-69.

30) *Id.* at 1470-71

31) Matthew Berg, “Equitable estoppel to compel arbitration in New York: A doctrine to prevent inequity,” *Cardozo Journal of Conflict Resolution* Vol.13, No.1. 2011. pp. 172-78.; *Deloitte Noraudit A/S v. Deloitte Haskins & Sells, U.S.*, 9 F.3d 1060, 1064 (2d Cir. 1993); *Thomson-CSF, S.A. v. Am. Arbitration Ass’n*, 64 F.3d 773, 778-79 (2d Cir. 1995).

obligation and duties in the contract and the fact that the claims were “intimately founded in and intertwined with the underlying contract obligations” (Strand B).³²⁾

Strand B has been further split into two sub-theories: The first sub-theory applies when the signatory to a contract with an arbitration clause “must rely on the terms of the written agreement in asserting its claims” against the non-signatory.³³⁾ The second sub-theory applies “when the signatory (to the contract containing the arbitration clause) raises allegations of substantially interdependent and concerted misconduct by both the non-signatory and one or more of the signatories to the contract.”³⁴⁾ The rationale for invoking equitable estoppel based on these two sub-theories is that “arbitration proceedings between the two signatories would be rendered meaningless and the federal policy in favor of arbitration was effectively thwarted.”³⁵⁾

2. Equitable Estoppel in the 5th and 11th Circuits

In the 5th Circuit, the courts have employed equitable estoppel doctrine in two circumstances as mentioned in the case of *Grigson*.³⁶⁾ This test for equitable estoppel was called as intertwined-claims test articulated in the 11th Circuit’s *MS Dealer Service Corp.* case.³⁷⁾ First, this doctrine can be applied when the signatory to a written agreement containing an arbitration clause is forced to rely on the terms of the written agreement in asserting its claims against the non-signatory. When each of a signatory’s claims against a non-signatory makes reference to or presumes the existence of the written agreement, the signatory’s claims arise out of and relate directly to the written agreement, and arbitration is appropriate. Second, this doctrine applies when the

32) Berg at 176; *Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.*, 10 F.3d 753, 757 (11th Cir. 1993); *J.J. Ryan & Sons, Inc. v. Rhone Poulenc Textile, S.A.*, 863 F.2d 315, 320-21 (4th Cir. 1988).

33) *MS Dealer Serv. Corp. v. Franklin*, 177 F.3d 942, 947 (11th Cir.1999) (citing *Sunkist Soft Drinks*, 10 F.3d at 757), in this case, after auto buyer brought state court action against auto dealership and service corporation, alleging that they conspired in fraudulent scheme to defraud a buyer by charging excessive amount for service contract, the service corporation filed petition to compel buyer to arbitrate her claims against it, relying on the Federal Arbitration Act (FAA) and arbitration clause in buyers order that was executed by buyer and dealership, but not by service corporation. The Court of Appeals held that the buyer was equitably estopped from avoiding arbitration.

34) *MS Dealer* at 757; Berg at 176.

35) *MS Dealer* at 757; Berg at 176.

36) *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524 (5th Cir. 2000).

37) *MS Dealer* at 947.

signatory to the contract containing an arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the non-signatory and one or more of the signatories to the contract. To decide otherwise would render the arbitration proceedings between the two signatories meaningless, and the federal policy favoring arbitration would be thwarted.³⁸⁾

In *Grigson*, the plaintiffs, Charles Grigson, River City Films, Inc., and Ultra Muchos, Inc. (the Plaintiffs) who were the trustee and owners of the movie, “Return of the Texas Chain Saw Massacre,” with actors Matthew McConaughey and Renee Zellweger starring, entered into a distribution agreement with Columbia TriStar Home Video, Inc. (TriStar).³⁹⁾ The distribution agreement containing an arbitration clause guaranteed TriStar the distribution rights to the movie and complete discretion with regard to how to exercise them.⁴⁰⁾ After the movie production was completed, McConaughey entered into an agency agreement with Creative Artists Agency, L.L.C. (CAA).⁴¹⁾ In an effort to capitalize on the success of McConaughey in subsequent movies, TriStar delayed the distribution of the movie, and then released the movie in a limited distribution. Plaintiffs sued McConaughey and CAA for tortiously interfering with the distribution agreement, alleging that McConaughey and CAA improperly pressured TriStar to limit the release of the movie.⁴²⁾ McConaughey and CAA, even if they were non-signatories to the Plaintiffs’ distribution agreement with TriStar, moved to compel the arbitration based upon the doctrine of equitable estoppel.⁴³⁾

The 5th Circuit court held that the doctrine of equitable estoppel applied here and thus the Plaintiffs were required to arbitrate their claims against McConaughey and CAA because the facts of the case satisfied the two independent bases specified in the intertwined-claims test which the Eleventh Circuit relied on.⁴⁴⁾ The court noted that the complaint alleges that the theatrical release was delayed initially to take advantage of McConaughey’s post-movie success in another movie, also released by TriStar; that the

38) *Grigson* at 525; *MS Dealer* at 757.

39) *Grigson* at 526; Clayton A. Morton, Tyler G. Doyle, “Equitable estoppel in the context of claims for tortious interference with contractual relations: Has its Texas supreme court gone too far?” *South Texas Law Review* vol. 57, no.3. 2016. pp. 250-52.

40) *Id.*

41) *Id.*

42) *Id.*

43) *Id.*

44) *Id.* at 527.

plan changed to take advantage of both actors' success; that Creative Artists, on behalf of McConaughey, "pressured" TriStar to not make a major release of the movie and, instead, to make only a limited one, to the Appellants' great financial detriment; and that, because of the Defendants' actions, "TriStar failed to exercise its good faith judgment in promoting, exploiting, and distributing" the movie. Thus, these allegations and claims in the complaint are intertwined with, and dependent upon, the distribution agreement. In addition to Appellants relying on the terms of the agreement in asserting their claims, TriStar and Defendants are charged with interdependent and concerted misconduct.⁴⁵⁾

Thus, the court held that a signatory to a contract agreement including an arbitration clause cannot "have it both ways": it cannot, on the one hand, seek to hold the non-signatory liable pursuant to duties under the agreement, which contains an arbitration provision, but, on the other hand, deny arbitration's applicability because the defendant is a non-signatory.⁴⁶⁾ The court further reasoned that refusing to compel arbitration would be especially inequitable because Plaintiffs had alleged that McConaughey, CAA, and TriStar engaged in concerted misconduct.⁴⁷⁾ Thus, in spite of TriStar's (a signatory) misconduct, Plaintiffs tried to avoid the arbitration agreement by suing only non-signatories (McConaughey and CAA).⁴⁸⁾

The 11th Circuit courts have also applied the equitable estoppel theory in arbitration cases such as in the Sunkist case⁴⁹⁾ where the charges against a parent company and its subsidiary were based on the same facts and were inherently inseparable.⁵⁰⁾ In Sunkist, soft drink trademark owner/licensor (Sunkist Growers, Inc.) sued the licensee's parent (Del Monte Corporation), alleging that the parent's management and operation of the licensee (Sunkist Soft Drinks) caused the licensee to violate various terms and provisions of the license agreement. Thus, the parent moved to compel the arbitration pursuant to the arbitration terms of the license agreement.⁵¹⁾ The district court agreed

45) *Id.*

46) *Id.* at 528; Morton at 252.

47) *Intergen* at 528.

48) *Id.*

49) *Sunkist* at 753-54.

50) Gee-Hong Kim, "Arbitration Agreement's Binding Effect on Non-Signatory," *Journal of Arbitration Studies*, vol. 17, no.3, 2007, p. 115.

51) *Sunkist* at 755.

with Del Monte and compelled the case to arbitration.⁵²⁾

On appeal, the Eleventh Circuit affirmed the district court's decision to compel the case to arbitration.⁵³⁾ The court reasoned that the doctrine of equitable estoppel required Sunkist to arbitrate its claims against Del Monte because each of Sunkist's claims presumed the existence of the license agreement.⁵⁴⁾ The court also noted that the arbitration was adequate because Del Monte absorbed SSD into Del Monte's own internal soft drink division.⁵⁵⁾ In effect, this resulted in SSD becoming a part of Del Monte. In this context, the court held that "the nexus between Sunkist's claims and the license agreement, as well as the integral relationship between SSD and Del Monte, leads us to the conclusion that the claims are 'intimately founded in and intertwined with' the license agreement."⁵⁶⁾

3. Equitable Estoppel in the 2nd Circuit

The Second Circuit has applied a different standard depending upon whether a non-signatory is attempting to enforce an arbitration agreement against a signatory, or a signatory is attempting to enforce an arbitration agreement against a non-signatory.⁵⁷⁾

(1) Non-signatory Attempts to Enforce an Arbitration Clause Against a Signatory

The Second Circuit prohibits a signatory from avoiding arbitration with a non-signatory when the disputes the non-signatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed.⁵⁸⁾ In this

52) *Id.* at 756.

53) *Id.*

54) *Id.*

55) *Id.*

56) *Id.* at 758.

57) *Morton* at 260-62; *MAG Portfolio Consultant, GMBH v. Merlin Biomed Group LLC*, 268 F.3d 58, 62 (2d Cir. 2001); *Thomson-CSF, S.A.* at 778-79.

58) *Denney v. BDO Seidman, L.L.P.*, 412 F.3d 58, 70 (2d Cir. 2005) (quoting *Contec Corp. v. Remote Solution Co.*, 398 F.3d 205, 209 (2d Cir. 2005)), in *Denney* case, investors including Thomas Denney in tax shelter brought putative class action against law and accounting firms that offered consulting services about tax shelters. Defendants, including non-signatories to consulting agreements, moved to compel arbitration under clause in consulting agreements. The Court of Appeals held that tax shelter services were within scope of consulting agreement and its arbitration

situation, Denney court stated that a signatory to an arbitration agreement can be compelled to arbitrate its claims with a non-signatory where a careful review of the relationship among the parties, the contracts they signed, and the issues that have arisen among them discloses “that the issues the non-signatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed.”⁵⁹⁾ Further, Sokol Holdings court expressly required that in addition to the “intertwined” factual issues, there must be a relationship among the parties of a nature that justifies a conclusion that the party which agreed to arbitrate with another entity should be estopped from denying an obligation to arbitrate a similar dispute with the adversary which is not a party to the arbitration agreement.⁶⁰⁾

The Second Circuit courts have eventually established a two-part “intertwined-ness” test, under which they “examine whether: (1) the signatory’s claims arise under the ‘subject matter’ of the underlying agreement, and (2) whether there is a ‘close relationship’ between the signatory and the non-signatory party.”⁶¹⁾ For example, in Sokol Holdings, Inc. v. BMB Munai, Inc., the plaintiff (Sokol) entered into a contract with Tolmakov Toleush Kalmukanovitch (Tolmakov) to buy 70% of Tolmakov’s 90% interest in Emir Oil LLP (“Emir”).⁶²⁾ The Emir Contract included an arbitration clause that provided for the arbitration of all disputes arising from the contract in Kazakhstan.

After Tolmakov breached the Emir Contract, Sokol sued the defendant (BMB Munai, Inc.) for tortiously interfering with the Emir Contract by inducing Tolmakov to sell his interest in Emir to BMB instead of Sokol.⁶³⁾ Although BMB did not have a contract with Sokol providing for arbitration, BMB moved to compel arbitration under the Emir Contract, contending that given the circumstances of Sokol’s suit against them Sokol was equitably estopped from refusing to arbitrate. The court noted that according to Sokol’s complaint, BMB came into its close relationship with Tolmakov by wrongfully inducing Tolmakov to breach his contract with Sokol and thus there was no “close relationship” between the signatories and the non-signatories to the Emir Contract that

clause so as to require arbitration of claims against signatory accounting firms; MAG Portfolio, at 62 (quoting Thomson-CSF, at 779).

59) Denney, 412 F.3d at 70.

60) Sokol Holdings, Inc. v. BMB Munai, Inc., 542 F.3d 354, 359 (2d Cir. 2008).

61) Morton at 261; Sokol Holdings, Inc. at 357.

62) Id.

63) Id. at 356

would make it unfair for Sokol to refuse to arbitrate with BMB.⁶⁴⁾ The court reasoned that while Sokol had agreed to arbitrate with Tolmakov, it in no way consented to extend that agreement to BMB, an entity that tortiously subverted Sokol's rights under the Emir Contract.⁶⁵⁾ Accordingly, the court refused to compel arbitration.

(2) Signatory Attempts to Enforce an Arbitration Clause Against a Non-signatory

The Second Circuit's equitable estoppel theory further permits a signatory of a contract agreement containing an arbitration clause to compel a non-signatory to arbitrate where the non-signatory knowingly exploits the benefits of an agreement containing an arbitration clause and receives benefits flowing directly from the agreement.⁶⁶⁾ "The benefits must be directly flowing from the agreement."⁶⁷⁾ In contrast, the "benefit derived from an agreement is indirect," and is therefore insufficient to support estoppel, "where the non-signatory exploits the contractual relation of parties to an agreement, but does not exploit the agreement itself."⁶⁸⁾

This test is almost identical to the test for direct-benefits estoppel under the 5th Circuit law, but the Second Circuit applies this test to only where the signatory attempts to enforce arbitration agreements against non-signatories.⁶⁹⁾ A non-signatory that seeks the benefits of an agreement must also be bound by its burdens, including the duty to arbitrate disputes arising from the agreement.⁷⁰⁾ By seeking the benefits of an agreement it did not sign, the non-signatory "assumes" the entire agreement and impliedly "consents" to be bound by all of the provisions.⁷¹⁾

64) *Id.* at 358.

65) *Id.*

66) MAG Portfolio at 61; *Life Techs. Corp. v. AB Sciex Pte. Ltd.*, 803 F. Supp. 2d 270, 273-74 (S.D.N.Y. 2011).

67) MAG Portfolio at 61; *Life Techs.* at 274.

68) MAG Portfolio at 61; *Life Techs.* at 274.

69) MAG Portfolio at 62.

70) *Morton* at 262.

71) *Id.* at 261

IV. Pros And Cons of Strand B in an Arbitration Context

1. Attack of Strand B as not Grounded in Ordinary Principles of Contract Law

Some commentators in the U.S. believe that Strand B is not based on ordinary principles of contract law and therefore should not be invoked by the U.S. courts.⁷²⁾ According to one commentator, the first strand of equitable estoppel, under which the courts examine whether a plaintiff-nonsignatory is exploiting the contract to his or her benefit such that there is sufficient objective intent to arbitrate, is consistent with the notion that the contract principles should trump over the U.S. policy in favor of arbitration.⁷³⁾ However, according to the commentator, those courts that have used the second strand of equitable estoppel to explore the parties' relationship overreach by elevating the pro-arbitration policy beyond traditional contract principles.⁷⁴⁾ Thus, the commentator argues that the second strand of equitable estoppel shall be eradicated in order to maintain valid contract and agency law principles.

2. Defense of Strand B

Other commentators maintain the position that finding an initial intention to arbitrate is not an easy inquiry and thus the court needs to review the initial intention via in-depth analysis.⁷⁵⁾ These intentions need to be construed liberally because of a federal policy favoring arbitration. One example of a court applying such a liberal construction is where a signatory attempts to avoid a valid arbitration clause by alleging what appears to be a breach of contract claim as a tort claim against a non-signatory.⁷⁶⁾ Further, the proponent of strand B argues that the narrow scope of strand B shall remain valid. One example of such narrow scope is when the charges

72) Alexandra Anne Hui, "Equitable estoppel and the compulsion of arbitration," 60 *Vanderbilt Law Review* vol. 60, 2007. pp. 736-3; J. Douglas Uloth & J. Hamilton Rial, "Equitable estoppel as a basis for compelling non-signatories to arbitrate," *Rev. Litig.* vol. 21, 2002. pp. 597-99.

73) Hui at 726.

74) *Id.*

75) Berg at 181.

76) *Id.*

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 if the parent is not a party to the arbitration agreement. If charges against the parent were tried separately in court and not arbitrated together with those against the subsidiary, the arbitration process would be meaningless because no judicial economy would exist.⁷⁷⁾

V. Concerns and Solutions of the Third Party Problems

1. Common Concerns in Third Party Situations

The first concern is for the position of the original promisor whose consent to the arbitration agreement was conditioned on the prospects of an arbitration with the original promisee (not the third party). Such concerns come to reality when it is the third party claiming against the promisor, either by way of arbitration (in which case the court is concerned that the promisor did not bargain on arbitrating with the particular third party) or by litigation (in which case the court is concerned that the promisor bargained on resolving disputes by arbitration).⁷⁸⁾

The second concern is for the position of the third party who has been forced to participate in an arbitration proceeding, either as respondent in an arbitral claim by the promisor or as a plaintiff in litigation that one is subsequently compelled to arbitrate. In these cases, the third party is not given the opportunity to negotiate the original agreement, or may not have enjoyed the collateral benefits of other terms in the main contract which justified including the arbitration provision.⁷⁹⁾

2. Possible Solutions to the Third Party Problems

Since the above third party problems can impede the efficiency and certainty of arbitration, especially in the context of international commercial arbitration, possible solutions must be sought.

77) *Id.*

78) Hosking at 501.

79) *Id.*

(1) Creating a Formal Test for Third Party Arbitration

One possible option is in line with a principle that an arbitration agreement will bind a third party non-signatory if this is consistent with the intention of all parties. The non-signatory will also be permitted to compel arbitration of a dispute within the scope of the agreement.⁸⁰⁾ The justification for this option comes from the use of intention as a touchstone not only in the U.S., but also in the international legal community. Pursuing this option requires formalizing it into a substantive rule of arbitration law ideally in the form of an international agreement (e.g., an amendment to the New York Convention) or a model law that provides a basis for harmonization at domestic law (e.g., International Arbitration Rules of the Korean Commercial Arbitration Board⁸¹⁾, or an amendment to the UNCITRAL Model Law).

(2) Relying Upon General Contract Law

Another option is to strictly treat third party issues as a matter of contract law and to apply the general principles of contract and agency to handle the issues of extending the arbitration agreement to a non-signatory third party.⁸²⁾ With this option, the “ordinary principles of contract and agency” would constrain the ability of a third party to compel and to be compelled to arbitrate. This option aims at adhering to existing general legal doctrine rather than creating a special third party test for international commercial arbitration agreements. Such principles as third party beneficiary should then be applied on the same basis as any other contract. Thus, for example, the United States courts need to forego the vague “pro-arbitration policy of the Federal Arbitration Act” and reliance on the uncertain “equitable estoppel” theory (at least in the strand B).⁸³⁾

80) *Id.*, at 502., fn 501.

81) International Arbitration Rules of the Korean Commercial Arbitration Board
Article 21. Joinder of Additional Parties

1. The Arbitral Tribunal may allow third parties to be joined provided that one of the following conditions is met. A third party being joined as a party shall hereinafter be referred to as the “Additional Party.” (a) All parties and the Additional Party have all agreed in writing to the joinder of the Additional Party to the arbitration proceedings; or (b) The Additional Party is a party to the same arbitration agreement with the parties and the Additional Party has agreed in writing to the joinder in the arbitration proceedings.

82) *Id.*; Thomson-CSF S.A. at 773.

83) *Id.*; *McBro Planning & Dev. Co. v. Triangle Elec. Constr. Co.*, 741 F.2d at 342 (11th Cir. 1984).

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