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Commentary

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Introduction

In January 2020, the United States Supreme Court will hear argument in *GE Energy Power Conversion France SAS v. Outokumpu Stainless USA LLC.* The question presented is "whether the Convention on the Recognition and Enforcement of Foreign of Foreign Arbitral Awards (the "New York Convention") permits a nonsignatory to an arbitration agreement to compel arbitration based on the doctrine of equitable estoppel."[1] At issue is an Eleventh Circuit decision that held that the New York Convention's requirement that an arbitration agreement be "signed by the parties" precluded allowing enforcement on a theory of equitable estoppel in cases subject to the Convention (*i.e.*, cases that are not purely domestic).[2]

This is not the first time the Supreme Court will consider the availability of equitable estoppel in the arbitration context. In *Arthur Andersen LLP v. Carlisle*, 556 U.S. 624 (2009), the Supreme Court held that an arbitration clause subject to the purely domestic provisions of the Federal Arbitration Act ("FAA") (*i.e.*, a case not implicating the Convention) may "be enforced by or against nonparties to the contract" when doing so would be consistent with "traditional principles of state law," including "assumption, piercing the corporate veil, alter ego, incorporation by reference, third-party beneficiary theories, waiver, and estoppel."[3] While acknowledging that "courts' application have equitable estoppel to impose an arbitration agreement upon strangers to the contract" may have been "somewhat loose," the Supreme Court disclaimed responsibility for overseeing the vagaries of state law and offered no standard to govern the analysis.[4] Likewise, while the recent Restatement of the U.S. Law of International Commercial and Investor-State Arbitration blesses the concept of arbitration involving nonsignatories on a theory of equitable estoppel, it does not explore the question of when arbitration involving a nonsignatory would be appropriate.[5]

This article explores the issue left open in *Andersen* and by the *Restatement*. Specifically, it reviews how lower courts have approached the issue of when to invoke equitable estoppel to permit an arbitration to go forward and sets forth a conceptual framework for that analysis. Part I identifies the two factors that courts most often consider when deciding whether arbitration by estoppel would be equitable in a particular instance. It also analyzes how the interplay of those two equitable factors can be used to divide arbitration by estoppel cases into four distinct analytical categories. Part II analyzes in-depth the category of case in which arbitration by estoppel is most challenging from an equitable perspective.

I.

As its name suggests, equitable estoppel is first and foremost a question of equity. In particular, two factors

seem to predominate in how courts have approached the question of whether estoppel would be equitable in a particular case: (1) which party is alleging a right to relief on the merits in the underlying dispute, and (2) which party is seeking to compel arbitration.

Factor 1: Is the party bringing the claim the signatory or nonsignatory?

When a nonsignatory invokes a contract it did not sign to claim a right to relief against a signatory to that contract, it is generally accepted that the nonsignatory cannot fairly avoid arbitrating under an arbitration clause in the same contract. In this scenario, the signatory/respondent can argue that equity requires that the nonsignatory/claimant be bound to *all* the provisions of the contract, not merely to the provisions on which the nonsignatory/claimant bases its claim to relief. That argument was persuasive to the U.S. Court of Appeals for the Fourth Circuit in *International Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH*, where the nonsignatory asserted a claim for breach of warranty but tried to resist arbitration under a different clause in the contract containing the warranty provision.[6]

By contrast, when a signatory alleges a claim against a nonsignatory, that argument is not available and this factor does not strongly support compelling the nonsignatory to arbitrate.

Factor 2: Is the party seeking to arbitrate the signatory or nonsignatory?

Similarly, when a nonsignatory seeks to compel arbitration against a signatory, courts have not been particularly troubled by the equity of requiring the signatory to arbitrate under an agreement it signed, albeit with a different party. That is the posture of the *Outokumpu* case pending before the Supreme Court, and when that scenario has arisen in federal cases not involving the New York Convention, courts have regularly compelled signatories to arbitrate.[7] Moreover, the logic supporting this application of equitable estoppel applies regardless of whether the signatory is the claimant or respondent in the underlying arbitration. While the signatory may argue that it did not consent to arbitrate with the particular party now seeking to claim the benefit of the arbitration clause, the signatory cannot contest that it consented to the arbitral seat, arbitral rules, and other key provisions in the arbitration clause. When a signatory seeks to compel arbitration against a nonsignatory, however, the nonsignatory can argue that it never consented to the arbitration clause at all.

The interplay of just these two factors suggests that there are four distinct scenarios of arbitration by estoppel, which present varying degrees of challenges from an equitable perspective.

	Nonsignatory alleges right to relief against signatory	Signatory alleges right to relief against nonsignatory
Nonsignatory seeks to compel arbitration against signatory	Least challenging: The signatory has agreed to arbitrate claims under the contract at issue *and* the nonsignatory cannot easily embrace the portion of the contract on which it bases its right to relief but avoid applying the arbitration clause in that contract.	Medium challenging: The signatory has agreed to arbitrate claims under the contract at issue and cannot easily argue that the nonsignatory is bound to the contract, but not the arbitration clause.
Signatory seeks to compel arbitration against nonsignatory	Medium challenging: The nonsignatory cannot easily embrace the portion of the contract on which it bases its right to relief but avoid applying the arbitration clause in that contract.	Most challenging: The nonsignatory has embraced neither the contract nor the arbitration clause at issue.

II.

As shown in Table 1, the most challenging scenario in which to apply equitable estoppel to compel arbitration between a signatory and a nonsignatory is when the signatory is the party that both alleges a right to relief under a contract and seeks to compel arbitration under that contract. In that circumstance, the nonsignatory cannot intuitively be said to have embraced the contract containing the arbitration clause.

When that circumstance arises, courts in the United States often analyze the equitable considerations at issue through the lens of a doctrine called "direct benefits estoppel." While the elements of direct benefits estoppel are relatively easy to articulate, applying them can be complex and the outcomes difficult to predict. As the U.S. Court of Appeals for the Second Circuit has described it, direct benefits estoppel applies when a nonsignatory knowingly accepts the benefits of a contract it did not sign.[8] The "benefits" in this context "must be direct—which is to say, flowing directly from the agreement" at issue.[9]

This theory of estoppel has generally been applied when the nonsignatory at issue had a formal corporate relationship with the signatory, such as a parent-subsidiary relationship or other close affiliation.[10] In that circumstance, courts seem generally willing to overlook corporate formalities that separate a signatory and nonsignatory, especially when the nonsignatory appears to be the party with a more vested interest in the dispute. However, a more difficult question arises when the nonsignatory is not affiliated with any signatory to the contract in question.

The Second Circuit is currently considering how direct benefits estoppel should apply in that context under New York law. In *Trina Solar US, Inc. v. JRC-Services LLC*, a contract for the sale of solar panels included an arbitration clause. Trina Solar, the manufacturer of the panels, signed the contract, as did JRC-Services, a private administrative and marketing company that purchased the panels. JRC-Services bought the panels for a nonsignatory entity called Jasmin Solar Pty Ltd. The panels were always intended ultimately to be for Jasmin's use, JRC-Services and Jasmin both negotiated the contract with Trina Solar, and Trina Solar delivered the panels directly to Jasmin and sent invoices to both Jasmin and JRC-Services. However, the contract, which included a New York choice of law clause, expressly disclaimed Jasmin as a third-party beneficiary.

When a dispute about payments for the panels arose, Trina Solar initiated arbitration against both JRC-Services and Jasmin, and Jasmin subsequently litigated whether it could be compelled to arbitrate. The district court held that arbitration was appropriate for two reasons: JRC-Services acted as Jasmin's agent and Jasmin was thus bound to the contract as the principal, and, independently, because Jasmin "benefitted directly" from the contract.[11] The district court expressly rejected Jasmin's argument that it could not be required to arbitrate as a nonsignatory because it had never sought to "exploit" or enforce the sales contract between Trina Solar and JRC-Services.[12]

Jasmin appealed from the district court's decision. On appeal, Jasmin argued not only that the district court had overextended the doctrine of estoppel, but also that applying that doctrine to require Jasmin to arbitrate would rewrite the arbitration clause in the Trina Solar-JRC Services sales contract. That clause required arbitration to resolve disputes "between the parties hereto," and the contract elsewhere defined "parties" to mean only the seller (Trina Solar) and buyer (JRC-Services). The Second Circuit heard oral argument on Jasmin's appeal on October 17, 2018, and has yet to render a decision.

Trina Solar thus highlights a number of challenging issues that arise when a signatory pursues a contract claim against a nonsignatory and seeks to compel that nonsignatory to arbitrate. Those issues, some of which continue to be litigated and others of which the parties in that case chose not to focus on, include:

- Choice of law. The district court applied the contract's New York choice of law clause, and Jasmin appears not to have contested its application. But it is not clear why a nonsignatory necessarily should be bound by a contract's choice of law clause when the nonsignatory arguably never agreed to be bound by the contract's terms. Indeed, the logic seems circular: by applying the choice-of-law clause in the contract, the district court effectively applied the contract in order to determine whether Jasmin could be bound by the contract. As an ICC tribunal put it

in another case, applying the law chosen by the contract in this context "would amount to putting the cart before the horse."[13]

- Definition of "direct" benefit. The district court held that Jasmin received a "direct" benefit under the contract because the solar panels at issue "were always intended for Jasmin's use and were delivered directly to Jasmin."[14] But the contract also expressly *excluded* Jasmin as a possible third-party beneficiary, and made it clear that Jasmin itself could not enforce the contract. Moreover, other courts have declined to apply estoppel theories when similarly situated nonsignatories benefit only from the *fact* that a contract exists between other parties rather than the *terms* of the contract itself.[15]

- Effect of estoppel ruling. What does it mean to bind a nonsignatory to an arbitration clause under an estoppel theory if the contract does not anticipate a third party being so bound? This question highlights the difference between finding that a signatory acted as the agent of a nonsignatory (in which case the nonsignatory principal assumes all the obligations of the signatory agent) and finding that the nonsignatory is estopped from disputing that it is bound by the arbitration clause in a contract. What if the arbitration clause does not anticipate a third party being so bound? The arbitration clause at issue in *Trina Solar*, for example, applied to the "parties" to the contract and even went so far as to define "parties" as Trina Solar and JRC-Services. It is not clear whether the scope of that language would include Jasmin even if Jasmin is bound to the clause under an estoppel theory. At least one other court has refused to compel arbitration based on the language of the arbitration clause itself even assuming the nonsignatory at issue was bound to that clause by an estoppel theory.[16] Nor is it clear whether Jasmin would be bound to JRC-Services' substantive obligations under the contract simply because it is bound by the arbitration clause in that agreement.

None of these issues have been resolved definitively, and it is not clear which (if any) of them the Second Circuit will ultimately address in its *Trina Solar* opinion.

Conclusion

Arbitration by estoppel involving nonsignatories is an area of law that is still developing. Not only does it present the complex legal questions described above, it also has meaningful practical considerations for contracting commercial parties. For example, depending on how a "direct benefit" is interpreted, a participant in a supply chain could find itself bound to an arbitration clause several tiers away. Moreover, in today's global economy, the question of which choice of law should apply to the determination of estoppel may be far from academic.

Endnotes

1. Petition for a writ of certiorari (Feb. 7, 2019) by GE Energy Power Conversion France SAS, seeking review of *Outokumpu Stainless USA, LLC v. Converteam SAS*, 902 F.3d 1316 (11th Cir. 2018).

2. *Outokumpu Stainless USA, LLC v. Converteam SAS*, 902 F.3d 1316 (11th Cir. 2018).

3. 556 U.S 624, 631 (2009) (*quoting* 21 R. Lord, *Williston on Contracts* § 57:19 at 183 (4th ed. 2001)).

4. *Id.* at 632.

5. Restatement § 2.3(b) states that a nonsignatory can arbitrate against a signatory to a contract containing an arbitration clause when the nonsignatory "is deemed to have consented to such agreement" or "is otherwise bound by or entitled to invoke the agreement under applicable law." The comments to that section of the Restatement make clear that the words "otherwise bound by" are meant to include equitable estoppel. *Id.* cmt. c; *see also id.* Reporters' Notes § (c).

6. *See Int'l Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH*, 206 F.3d 411, 418 (4th Cir. 2000).

7. *See, e.g., Crawford Professional Drugs, Inc. v. CVS Caremark Corp.*, 748 F.3d 249 (5th Cir. 2014).

8. *See MAG Portfolio Consult, GMBH v. Merlin Biomed Group LLC*, 268 F.3d 58, 61 (2d Cir. 2001).

9. *Id.*

10. *See, e.g.*, *Life Techs. Corp. v. AB Sciex Pte. Ltd.*, 803 F. Supp. 2d 270, 276-77 (S.D.N.Y. 2011) (party estopped was affiliate of contracting party, and contract with arbitration clause expressly bound affiliates).

11. *Trina Solar US, Inc. v. JRC-Services LLC*, 229 F. Supp. 3d 176, 188 (S.D.N.Y. 2017).

12. *Id.* at 188 n.11.

13. Award, ICC Case No. 8385, in J.-J. Arnaldez, Y. Derains & D. Hascher (eds.), *Collection of ICC Arbitral Awards 1996-2000*, 474 (2003), reprinted in *International Arbitration: Cases and Materials* (2d ed.) (Born 2015), at 561, 562.

14. *Trina Solar*, 229 F. Supp. 3d at 189.

15. *See, e.g.*, *Lang v. First American Title Ins. Co.*, No. 12-CV-266S, 2012 WL 5221605 (W.D.N.Y. Oct. 22, 2012) (declining to estop homeowner in dispute with loan title insurer based on insurer's contract with mortgage lender that enabled homeowner to obtain mortgage loan); *Masefield AG v. Colonial Oil Industries, Inc.*, No. 05-CV-2231, 2005 WL 911770 (S.D.N.Y. Apr. 18, 2005) (declining to estop seller's affiliate when seller paid all its proceeds from sale to affiliate).

16. *See Serebryakov v. Golden Touch Transp. of NY, Inc.*, No. 12-CV-3990, 2015 WL 1359047, at *5 (E.D.N.Y. Mar. 24, 2015) (concluding that even if nonsignatory was bound to arbitration clause by estoppel theory, that clause did not encompass claims at issue in the arbitration). ■

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