CAHILL GORDON & REINDEL LLP
EIGHTY PINE STREET
NEW YORK, NEW YORK 10005-1702
TELEPHONE: (212) 701-3000
FACSIMILE: (212) 269-5420

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Corporate signatory to a written partnership agreement requiring International Arbitration may not circumvent arbitration by naming non-signatories as defendants

On May 22, 2008, the United States Court of Appeals for the First Circuit held that a corporate signatory to a written partnership agreement cannot circumvent an arbitration clause by naming non-signatories as defendants, provided the claims against the non-signatories are intertwined with the subject matter within the scope of the arbitration clause.[1]

Jumpsource, the plaintiff, had brought suit alleging a number of tort, contract and statutory claims against the defendant, who moved to dismiss on the ground that the agreement provided that all disputes must be submitted to arbitration in China. The district court issued a summary order denying the motion to dismiss. Defendants appealed and the First Circuit reversed, finding that it had appellate jurisdiction to rule on this interlocutory appeal under 9 U.S.C. § 16(a)(1)(C) and remanding the case to the district court for an order granting the motion to compel arbitration.

Suing a non-signatory is one of a number of ways a party may attempt to circumvent an arbitration clause. *Jumpsource* works to foreclose use of this procedural maneuver and reinforce the use of arbitration as a means of resolving disputes. The Supreme Court in recent opinions continues to promote the strong federal policy favoring arbitration stated in the Federal Arbitration Act ("FAA"). The U.S. District Court for the Southern District of New York, in a case involving a similar set of facts, has also cited the strong federal policy favoring arbitration and applied the estoppel doctrine, compelling arbitration where the claims against the non-signatory are intertwined with the underlying agreement containing the arbitration provision.

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1 *Sourcing Unlimited Inc d/b/a Jumpsource. v. Asimco International, Inc.*, No. 07-2574, slip op. at 17-18 (1st Cir. May 22, 2008) (hereinafter *Jumpsource*).

I. Discussion

In *Jumpsource*, plaintiff, a Massachusetts corporation that provides mechanical parts for the U.S. equipment industry, had negotiated a written partnership agreement with John Perkowski, Chairman and CEO of ATL, a Delaware corporation headquartered in China.[2] Under the agreement, plaintiff agreed to turn over certain of its China manufacturing operations to ATL. The agreement indicated how the companies would split the profits and ATL agreed not to circumvent plaintiff in relationships with its existing customers. The agreement concluded with a broadly worded arbitration clause and a complementary choice-of-law clause providing that the "agreement . . . be governed by . . . the laws of The P.R. China . . . . Any action to enforce arising out of, or relating in any way to, any provisions of this agreement shall be brought in front of a P.R. China arbitration body."[3] Though Perkowski was also the chairman of Asimco, a subsidiary of ATL, the agreement was not signed by any subsidiary nor did it contain a provision binding all corporate subsidiaries, affiliates, etc.

When the relationship soured, plaintiff filed suit in Massachusetts Superior Court in June 2007, asserting a number of tort, contract and statutory claims. Notably, the complaint named only Asimco and Perkowski - not ATL - as defendants. The complaint alleged that in addition to the written partnership agreement with ATL, Jumpsource had entered into an oral agreement with Perkowski under which Asimco would deliver parts produced by the Jumpsource-ATL partnership to their U.S customers, invoice those customers and split the profits with Jumpsource according to the terms of the written Jumpsource-ATL agreement.[4] Jumpsource alleged that this agreement adopted the written agreement's non-compete terms but not its arbitration terms.

Defendants removed the case to the U.S. District Court in Massachusetts and then filed a motion to dismiss. In addition to arguing that the complaint failed to state valid claims, Asimco cited Chapter 2 of the FAA as a basis for dismissal in favor of arbitration. Asimco characterized the oral agreement between Jumpsource and Perkowski as a modification of the Jumpsource-ATL agreement. Asimco argued that on the basis of equitable estoppel, Jumpsource should not be permitted to evade its obligation to arbitrate by suing a non-signatory, noting that the issues Jumpsource sought to litigate are "intertwined with the agreement that [Jumpsource] has signed."[5] Jumpsource responded that its claims derived not from the Jumpsource-ATL agreement, but from the separate oral contract between Jumpsource and Asimco which did not contain any agreement to arbitrate. On November 6, 2007, the district court issued a summary order denying the motion to dismiss, which had the effect of denying arbitration

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[2] *Jumpsource*, at 2-3.

[3] *Id.* at 3-4.

[4] *Id.* at 4.

[5] *Id.* at 7.

in China holding Jumpsource is not a party to any such contract with Asimco. Jumpsource then moved to dismiss defendant's interlocutory appeal for lack of appellate jurisdiction.

II. Appeal of Interlocutory Order Allowed

The First Circuit first discussed the issue of its appellate jurisdiction with respect to an interlocutory appeal regarding an order effectively denying international arbitration. The court noted the FAA creates an explicit statutory exception to the rule against interlocutory appeals in the case of an order disfavoring arbitration.[6] The court explained that precedent disfavors Jumpsource's argument that the Court of Appeals lacks jurisdiction under §16(a)(1)(C) where the party requesting arbitration is not a signatory to the arbitration agreement at issue. In *Intergen N.V. v. Grina*,[7] a case in which neither party was a signatory to a written arbitration agreement, the First Circuit held that "[a] party has the right to appeal immediately from an order denying a motion to compel arbitration." The court distinguished the decisions of two sister circuits[8] rejecting interlocutory appeals on the basis of estoppel when the parties are not signatories to a written arbitration agreement noting that those cases only involved domestic arbitration agreements governed by Chapter 1 of the FAA.[9] Chapter 1 authorizes federal courts to compel domestic arbitration only where there is a "written agreement for arbitration."[10] The D.C. Circuit reasoned this language implies that courts should not compel arbitration when only principles of equitable estoppel would point to such a result.[11] In contrast, Chapter 2, dealing with international arbitrations, employs broader statutory language providing that "A court . . . may direct that arbitration be held in accordance with the agreement at any place therein provided for, whether that place is within or without the United States."[12]

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6 9 U.S.C. § 16(a)(1)(C) (1990).

7 344 F.3d 134 (1st Cir. 2003).

8 *See In re Universal service Fund Telephone Billing Practice Litigation*, 428 F.3d 940 (10th Cir. 2005) and *DSMC Inc. v. Convera Corp.*, 349 F.2d 679 (D.C. Cir. 2003).

9 9 U.S.C. §§ 1-16.

10 9 U.S.C. § 4.

11 *DSMC*, 349 F.3d at 683.

12 9 U.S.C. § 206.

Furthermore, the court noted that the national policy favoring arbitration has extra force when dealing with international arbitration.[13] The Supreme Court, in two recent cases, has reiterated the strong federal policy favoring arbitration. In *Preston v. Ferrer*,[14] the Supreme Court held that when parties agree to arbitrate all questions arising under a contract, the FAA supersedes state laws that refer certain state-law controversies to a judicial forum. The Court explained that Chapter 2's national policy favoring arbitration "applies in state as well as federal courts" and "foreclose[s] state legislative attempts to undercut the enforceability of arbitration agreements."[15] Even more recently, in *Hall Street Assoc. LLC v. Mattel, Inc.*,[16] an important decision holding parties may not contract to expand the scope of judicial review of arbitral awards, the Court cited the national policy favoring arbitration as the reason for only allowing the limited review explicitly stated in 9 U.S.C. §§ 9-11 which is needed to maintain arbitration's essential virtue of resolving disputes quickly.

III. Compelling International Arbitration

The First Circuit then proceeded to discuss the underlying issue of whether the district court erred in denying the motion to compel arbitration.[17] Noting that the context of the case was significant in that the party who was a signatory to the written agreement requiring arbitration was the party seeking to avoid it, the court held application of the doctrine of equitable estoppel was appropriate. The court stated that federal courts "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."[18] As there was no real issue in the case about whether the subject matter of the suit was intertwined with the subject matter subject to the arbitration clause, the court held the dispute was sufficiently intertwined with the Jumpsource-ATL Agreement for application of estoppel to be appropriate. The court noted that "most of Jumpsource's claims either directly or indirectly invoke the terms of the Jumpsource-ATL agreement."[19] Furthermore, "even if there had been an enforceable contract between Jumpsource and Asimco . . . that contract would still require reference to

[13] *Id.* at 13.

[14] *Preston v. Ferrer*, No. 06-1463, slip op. at 1-2 (February 20, 2008).

[15] *Id.* at 2 (citing *Southland Corp v. Keating*, 465 U.S. 1, 16 (1984)).

[16] No. 06–989, slip op. at 2 (March 25, 2008).

[17] *Jumpsource*, at 16-20.

[18] *Id.* at 17 (quoting *Thomson-CSF, S.A. v. Am. Arbitration Ass'n*, 64 F.2d 773, 779 (2d Cir. 1995)) (internal quotation marks omitted).

[19] *Id.* at 17-18.

and be in part based on the underlying Jumpsource-ATL agreement."[20] Thus, the court held Jumpsource was equitably estopped and bound by a written agreement to arbitrate in China "[a]ny action to enforce, arising out of, or relating in any way to, any provisions" of the agreement.

Recently, in a case involving similar facts, the United States District Court for the Southern District of New York has also held the application of equitable estoppel appropriate. In *Birmingham Associates v. Abbott Laboratories*,[21] the plaintiff, Birmingham, along with a group of investors entered into a funding agreement with the defendant's subsidiary related to the development of a stent product. The agreement contained a broad arbitration clause. Concurrently, Abbott entered into a "keep well" agreement with ALVE, its subsidiary, obligating Abbott to guarantee ALVE's performance under the funding agreement. The "keep-well" agreement did not contain an arbitration provision. Plaintiff later sued claiming Abbott improperly terminated the "keep-well" agreement and Abbott moved to compel arbitration. The court granted the motion to compel arbitration, citing the strong federal policy favoring arbitration and the estoppel doctrine under which a non-signatory may compel arbitration where: 1) there is a close relationship between the parties and 2) the signatory's claims against the non-signatory are intertwined with the underlying agreement containing the arbitration provision. The court found the first prong was satisfied since there was a close relationship between Abbott and ALVE because of their parent-subsidiary relationship and the second prong was satisfied because the dispute at issue was directly related to the terms of the funding agreement.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at (212) 701-3403 or cgilman@cahill.com; Jon Mark at (212) 701-3100 or jmark@cahill.com; John Schuster at (212) 701-3323 or jschuster@cahill.com.

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[20] *Id.* at 18.

[21] Case No. 07 Civ. 11332 (S.D.N.Y. Apr. 14, 2008).