Can Arbitration Be Enforced Against Non-Signatories to a Contract?

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To those of you kind enough to visit this site regularly – no, you are not seeing double. On December 18, 2018 we addressed the United States District Court's examination of binding nonsignatories to arbitration agreements[1]. Recently, the South Carolina Supreme Court undertook its own analysis of when arbitration may be enforced against nonsignatories to a contract including an arbitration clause. *Wilson, et al v. Willis*, *et al* 2019 WL 1549924, (April 10, 2019).

The *Wilson* appeal stems from some fourteen suits instituted by various Plaintiffs against an insurance agent and the broker who put her in charge of the subject insurance office, the insurance agency and insurance companies for which these entities sold policies. Plaintiffs alleged multiple causes of action, in response to which Defendants denied the substantive claims. After a significant period of time, the issue of arbitration first arose when three Defendants moved to compel arbitration and dismiss the actions. Their argument was based upon an arbitration clause included in an early agency contract entered into by certain Defendants and the agency. The circuit court denied the motion to compel arbitration following which the court of appeals reversed and remanded. The matters came before the Supreme Court on writs of certiorari.

The court of appeals relied, in large part, upon its determination that Plaintiffs were equitably estopped from arguing their nonsignatory status precluded enforcement of the contractual arbitration provision against them, reasoning they sought to benefit from enforcement of other provisions of the agency agreement and were thus required to submit their claims to arbitration. As a result, the Supreme Court focused much of its analysis upon equitable estoppel.

State and federal courts have issued myriad opinions emphasizing the importance of and favor for arbitration. The Federal Arbitration Act applies in both state and federal courts to any arbitration agreement involving interstate commerce, unless the parties have otherwise agreed. So powerful is the FAA that any state law that positions arbitration clauses on unequal footing with contracts generally is preempted if the FAA is applicable. Favor aside, arbitration necessarily includes the waiver of one's fundamental right to access to the courts. Consequently, it is based upon agreement of the parties. That established, South Carolina has recognized multiple theories of contract and agency law pursuant to which nonsignatories to arbitration agreements may be bound, including incorporation by reference, agency and, at issue here, estoppel. The general structure of equitable estoppel followed by the federal courts and embraced by some states is frequently identified as the direct benefits test. Pursuant to direct benefits estoppel, a nonsignatory is estopped from refusing compliance with an arbitration agreement when he or she receives a direct benefit from the contract in which the arbitration agreement is included. If the nonsignatory has encouraged enforcement of other parts of the contract, to his or her benefit, and received benefits flowing directly from the agreement, he may be bound by the arbitration agreement on the basis of estoppel, even though the agreement does not bear his signature.

In its effort to effectively and fairly assess the positions of the parties, the *Wilson* court looked for further clarification of direct benefits estoppel, reaching out to other jurisdictions, and accepting their determinations. Specifically, it arises when a claim is dependent upon the existence of the contract and cannot stand alone; the alleged liability is seeded in the contract or must be determined by its terms. By exception, however, if the claim is founded in statute, tort or other common law duties, direct benefits estoppel is not triggered, even if the claim refers or relates to the contract or would not exist "but for" the contract.

Recognizing that the difference between direct and indirect benefits is not always readily apparent, the court found it important to try to distinguish indirect benefits, as they are not sufficient to compel arbitration. Benefits are indirect when the nonsignatory exploits the contractual relationship of the actual parties thereto but does not go so far as to exploit the contract itself.

Here, the court found the agreement requiring arbitration was executed by certain Defendants purely for the benefit of the parties thereto, in the establishment of their business relationships; Plaintiffs were not even aware of the agreement until such time as certain Defendants relied upon it in an effort to compel arbitration. Consequently, the court also found Plaintiffs did not seek to procure any direct benefit from that agreement and could not be compelled to subject their claims to arbitration.

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[1] *Binding Nonsignatories to Arbitration Agreements*