SUPREME COURT HOLDS THAT A NON-PARTY TO AN ARBITRATION AGREEMENT MAY APPEAL THE DENIAL OF A MOTION TO STAY PENDING ARBITRATION UNDER THE FEDERAL ARBITRATION ACT

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In *Arthur Andersen LLP v. Carlisle*, - U.S. -, 129 S.Ct. 1896 (May 4, 2009), the Supreme Court resolved a conflict of Circuits regarding the interpretation of sections 3 and 16 of the Federal Arbitration Act ("FAA") (9 U.S.C. §§3 and 16). Section 3 of the FAA entitles parties in federal courts to a stay of any action that is "referable to arbitration under an agreement in writing." Section 16(a)(1)(A) of the FAA allows an appeal from an order "refusing a stay of any action under section 3." Two issues were accepted for review: "whether appellate courts have jurisdiction under §16(a) to review denials of stays requested by litigants who were not parties to the relevant arbitration agreements, and whether §3 can ever mandate a stay in such circumstances." 129 S.Ct. at 1899. The D.C. and Tenth Circuits had held that appellate jurisdiction did not exist in such a situation, while the First and Second Circuits had held that appellate jurisdiction did exist.[1]

The case arose from an attempt by the owners of a business to minimize taxes from the sale of the business. Arthur Andersen had served as the company's accountant, auditor and tax advisor, and recommended that the owners consult an investment company, which in turn referred the taxpayers to a law firm. The taxpayers invested in stock warrants through newly created limited liability corporations ("LLCs") which were described as a leveraged option strategy tax shelter involving foreign currency exchange options. The LLCs and the investment company entered into an investment management agreement, which contained an arbitration agreement. The Internal Revenue Service declared the scheme to be an illegal tax shelter, and the taxpayers paid taxes, interest and penalties.

The taxpayers and LLCs sued the investment company, Arthur Andersen, the law firm and others. The defendants which were not parties to the investment management agreement moved to stay and compel arbitration, arguing that principles of equitable estoppel required that the taxpayers and LLCs arbitrate their claims with the investment company. The district court

[1] Compare *DSMC Inc. v. Convera Corp.*, 349 F.3d 679, 684-85 (D.C. Cir. 2003) and *In re Universal Serv. Fund Tel. Billing Practice Litig.*, 428 F.3d 940, 942-43 (10th Cir. 2005) with *Ross v. Am. Express Co.*, 547 F.3d 137, 141 (2d Cir. 2008) and *Sourcing Unlimited, Inc. v. Asimco Intern., Inc.*, 526 F.3d 38, 44 n. 6 (1st Cir. 2008). *See also Becker v. Davis*, 491 F.3d 1292, 1296-97 (11th Cir.2007) and *McCarthy v. Azure*, 22 F.3d 351, 354 (1st Cir.1994) (exercising jurisdiction in analogous situations without discussing the jurisdictional issue) and *May v. Higbee Co.*, 372 F.3d 757, 762 & n. 8 (5th Cir. 2004) (noting conflicts in the decisions of the Fifth Circuit as to this jurisdictional issue).

denied the motion, and the respondents appealed. The Sixth Circuit dismissed the appeal for want of jurisdiction, and held in the alternative that those who were not parties to a written arbitration agreement were categorically ineligible for relief under §3 of the FAA. *Carlisle v. Curtis, Mallet-Prevost, Colt & Mosle*, 521 F.3d 597 (6th Cir. 2008).

The Court took only three paragraphs to reverse on the jurisdictional issue, finding that under the "clear and unambiguous terms" of §16(a), "any litigant who asks for a stay under §3 is entitled to an immediate appeal from denial of that motion – regardless of whether the litigant is in fact eligible for a stay." *Id.* at 1900. Because each Petitioner before the Court was a party in the district court, and had asked for a stay under §3, they were entitled to appeal the denial of their request for a stay. The Court criticized courts that had declined jurisdiction over such appeals as "conflating the jurisdictional question with the merits of the appeal." *Id.*

"The jurisdictional statute here unambiguously makes the underlying merits irrelevant, for even utter frivolousness of the underlying request for a §3 stay cannot turn a denial into something other than 'an order … refusing a stay of any action under section 3.' 9 U.S.C. §16(a)." *Id.* at 1901. The Court rejected concerns that such a result would result in "a long parade of horribles," including frivolous interlocutory appeals, noting that such concerns could not overcome the plain language of the statute, that courts must address merits issues only after accepting jurisdiction, and that there were ways of minimizing the impact of abusive appeals. *Id.*

With respect to the alternative merits holding, the Supreme Court held that a litigant who was not a party to an arbitration agreement could nevertheless obtain a stay pending arbitration under §3 if the applicable state contract law allowed it to enforce the arbitration agreement, whether by estoppel, third party beneficiary doctrine or otherwise. *Id.* at 1901-03.

The Supreme Court's resolution of the inter-Circuit conflict on the jurisdictional issue may be helpful in some reinsurance disputes, eliminating the prospect of different jurisdictional results depending upon the Circuit in which the dispute is pending.

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