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PERSPECTIVE

9th Circuit weighs in on using equitable estoppel to compel arbitration

By Angela Kleine and Neil S. Tyler

Can you compel arbitration without an arbitration agreement? The 9th U.S. Circuit Court of Appeals recently weighed in with two decisions. In *Stafford v. Rite Aid Corporation* (2021 DJDAR 4917) and *Franklin v. Community Regional Medical Center, et al.* (2021 DJDAR 4920), the defendants sought to compel arbitration via equitable estoppel, based on arbitration agreements between the defendants and third parties. The 9th Circuit came to opposite conclusions in these two cases. The decisions show that the nature of the parties' business and relationships, and the allegations in the complaint, can shape whether a dispute is arbitrable

Stafford v. Rite Aid Corp.

Plaintiff Byron Stafford filed a putative class action against Rite Aid Corporation alleging that the pharmacy fraudulently inflated prescription drug prices, resulting in customers being overcharged for co-payments. According to plaintiff, the prices Rite Aid listed on prescription drug claim forms, through its pharmacy benefits manager, determined the price that plaintiff was charged for prescription drugs. Plaintiff claimed that because the pharmacy reported an improperly high price to the pharmacy benefits manager, he paid more for the drugs than he should have. Plaintiff asserted Unfair Competition Law, Consumer Legal Remedies Act, unjust enrichment, and negligent misrepresentation claims.

Rite Aid and plaintiff did not have a contract between them containing an arbitration clause. But, Rite Aid moved to compel arbitration based on the theory of equitable estoppel, arguing that plaintiff's claims were intertwined with Rite Aid's contracts with the pharmacy benefits managers, which did contain arbitration clauses. Under California law, plaintiffs can be bound by arbitration clauses in contracts they did not sign if the claims asserted are "dependent upon, or founded in and inextricably intertwined with, the underlying contractual obligations of the agreement contained the arbitration clause." (Citation omitted.) The district court denied Rite Aid's motion to compel, finding that the principles of equitable estoppel did not bind plaintiff to the arbitration provisions in contracts he did not sign because his claims were based on Rite Aid's alleged fraudulent actions rather than any breach of Rite Aid's contracts with the pharmacy benefits managers. Rite Aid appealed, and the 9th Circuit affirmed.

The 9th Circuit similarly held that equitable estoppel was inapplicable to plaintiff's claims because he was not seeking damages for Rite Aid's breach of its contracts but rather alleged fraud. The 9th Circuit therefore found "irrelevant" Rite Aid's contracts with the pharmacy benefits managers because "Rite Aid's duty not to commit fraud is independent from any contractual requirements with the pharmacy benefits managers." Because plaintiff's claims did not depend on Rite Aid's contractual obligations, the Court held that equitable estoppel did not bind plaintiff to the arbitration agreements in contracts to which he was not a party.

Franklin v. Cmty. Reg'l Med. Ctr.

On the same day *Stafford* came out, the 9th Circuit issued its opinion in *Franklin*, a putative wage-and-hour lawsuit asserting claims under the Fair Labor Standards Act, California Labor Code, and UCL. Plaintiff was employed as a nurse by staffing agency United Staffing Solutions Inc., and USSI assigned her to work at the defendant hospital. USSI and plaintiff signed two arbitration agreements — one in plaintiff's employment agreement and another in the assignment contract governing her wages, overtime, shifts, and reimbursements at the hospital. The hospital was not a signatory to either contract, and no contracts existed between either (a) the hospital and plaintiff or (b) the hospital and USSI. Instead, the hospital contracted with a managed service provider to source nursing staff like plaintiff, and the managed service provider in turn contracted with USSI to provide the nursing staff for the hospital, with the hospital retaining supervision over plaintiff. The hospital paid the managed service provider, which then paid USSI, which then paid plaintiff for her work.

Plaintiff alleged the hospital failed to pay her for work she performed, provide accurate itemized wages statements, or reimburse her for travel expenses. The hospital moved to compel arbitration.

The district court granted the hospital's motion under the theory of equitable estoppel. It found that even though the hospital was a non-signatory to the arbitration provisions, plaintiff's statutory claims against the hospital were intimately founded in and intertwined with her contracts with USSI. Plaintiff appealed, and the Ninth Circuit affirmed.

The 9th Circuit ultimately followed *Garcia v. Pexco*, LLC, 217 Cal. Rptr. 3d 793 (Ct. App. 2017), which held that an employee's Labor Code claims against a staffing agency's non-signatory client were subject to arbitration because they were "intimately founded in and intertwined with" his employment contract with the staffing agency that contained binding arbitration provisions. The 9th Circuit in *Franklin* found that "[i]t does not matter that *Franklin's* allegations are leveled only at the Hospital and not USSI" because "[i] n matters of equity, such as the application of equitable estoppel, it is the substance of the plaintiff's claim that counts, not the form of its pleading." Based on the allegations and claims asserted in the complaint, the Court found that plaintiff's employment with USSI "is central to her claims." Because USSI was responsible for various employment practices plaintiff alleged were violated (including paying her), and plaintiff's other claims required reference to the terms of her contracts with USSI, plaintiff could not avoid arbitration simply because she had sued only the hospital and omitted any mention of USSI in her complaint.

Takeaways

Stafford and *Franklin* are reminders that the way business and contractual relationships are structured can subject even the most carefully drafted arbitration provisions to an uncertain future. Applying the same principles of equitable estoppel, the *Stafford* court found the plaintiff's fraud-based claims were not subject to arbitration, while the *Franklin* court found the plaintiff's employment-related claims must be arbitrated. These two decisions — issued the same day by the same court (albeit different panels of judges) — demonstrate the fact-specific analysis involved if a motion to compel is not based on a direct agreement containing an arbitration provision between the plaintiff and defendant. ■

Angela Kleine *is a partner in Morrison & Foerster's Class Actions + Mass Torts practice where she defends companies in complex consumer and commercial disputes.*

Neil Tyler *is an associate with the firm, focusing on the defense of labor and employment, consumer class action, and commercial litigation matters.*