IN THE SUPREME COURT OF TEXAS

NO. 04-0865

IN RE MERRILL LYNCH TRUST COMPANY FSB, MERRILL LYNCH LIFE INSURANCE COMPANY, AND HENRY MEDINA, RELATORS

ON PETITION FOR WRIT OF MANDAMUS

Argued March 23, 2005

JUSTICE JOHNSON, joined by JUSTICE WAINWRIGHT, concurring in part and dissenting in part.

As the Court notes, arbitration is a matter of consent and the Federal Arbitration Act generally does not require parties to arbitrate when they have not agreed to do so. *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 478-79 (1989). But parties should be required to arbitrate disputes which, according to law, they have agreed to arbitrate. Our decisions relating to arbitration should facilitate prompt, final resolution of those disputes to the extent reasonably possible. To that end, I agree that the trial court abused its discretion in failing to require Juan and Norma Alaniz to arbitrate their claims against Henry Medina. While I agree that arbitration must be based on an agreement to arbitrate by the parties and no such agreement exists or can be relied on by ML Trust and ML Life, I do not consider that we write on a clean slate with these facts and this issue.

In this case to which the FAA applies, I would follow the stated position of the Federal Fifth Circuit Court of Appeals that equitable estoppel is applicable in cases where a signatory to a contract containing an arbitration clause alleges substantially interdependent and concerted misconduct by both a nonsignatory and one or more of the signatories to the contract. On that basis, I would hold that the trial court abused its discretion in failing to apply the second prong of *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524, 527 (5th Cir. 2000), to equitably estop the Alanizes from refusing to arbitrate claims against ML Trust and ML Life to the extent the claims are based on Medina's alleged misconduct. I would grant relief accordingly.

The Alanizes' petition alleges that, in early 1994, Medina, as agent for ML Life and ML Trust, approached them regarding the creation of an irrevocable trust. The petition then alleges that the wrongful actions of "Defendants" improperly induced the Alanizes to create an irrevocable trust and name ML Trust as trustee, which in turn allowed self-dealing among "Defendants" by ML Trust purchasing life insurance from ML Life with Medina acting as agent. The petition further alleges that "Defendants" violated various provisions of the Property Code, Insurance Code, and Business and Commerce Code; committed breaches of fiduciary duties, fraudulent conversion, theft, negligent misrepresentation, and negligence generally; and were unjustly enriched from the payments made by the Alanizes to ML Trust. Specifically, for example, the Alanizes allege:

> 12. . . . Defendants, including Mr. Medina in his capacity as an agent of Merrill Lynch Trust Company and Merrill Lynch Life Insurance Company, represented to Plaintiffs that Defendants were sophisticated, skilled and experienced in the areas of trusts and life insurance. Defendants also represented to Plaintiffs that they would act in a manner consistent with Plaintiffs [sic] best interests . . . .

> 13. In April, 1994 Defendants arranged for an attorney to draft the Alaniz Irrevocable Trust Agreement at Plaintiffs [sic] expense. Defendants exerted inappropriate and undue influence over the drafting . . . .
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> 14. Defendants knowingly made false and misleading statements of material facts and law to Plaintiff . . .
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> 15. Defendants' actions were done with reckless and intentional disregard of the rights and well being of Plaintiffs . . . [and] to unjustly enrich Defendants . . . .
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> . . . .
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> 20. Plaintiff [will show] that the acts, errors, and omissions of Defendants have amounted to the following . . .
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> 21. . . . [T]he acts, errors, and omissions of Defendants have been a producing/proximate cause of Juan Alaniz' and Norma Alaniz' damages . . . .

The gravamen of the pleaded complaints against ML Trust and ML Life is that the companies acted both through Medina's actions as the companies' agent and in concert with Medina and each other to induce the Alanizes to transfer funds to ML Trust, and that ML Trust then paid life insurance premiums to its affiliate ML Life and paid fees to all defendants.

Several months before the Alanizes even considered purchasing life insurance and setting up an irrevocable life insurance trust they began dealing with Medina as a financial advisor who worked for Merrill Lynch. The scope of the arbitration provision the Alanizes signed when they first began dealing with Medina is broad. It encompasses "all controversies which may arise between us, including but not limited to those involving any transaction or the construction, performance, or breach of this or any other agreement between us, whether entered into prior, on or subsequent to the date hereof." As the Court holds, the pleadings and evidence, together with the scope of the arbitration clause, compel the conclusion that, as to Medina, the Alanizes must arbitrate the claims

on which they sued. ___ S.W.3d ___; *see In re Vesta Ins. Group, Inc.*, 192 S.W.3d 759, 762-63 (Tex. 2006). As the Court also holds, ML Trust and ML Life are not entitled to enforce the arbitration agreement as "affiliates" of Merrill Lynch. But ML Trust and ML Life further urge that the Alanizes should be compelled to arbitrate on the basis of equitable estoppel. This is so, they claim, for two reasons. First, the Alanizes' claims refer to or presume the existence of the Merrill Lynch CMA agreement containing the arbitration clause. Second, the Alanizes' claims raise allegations of substantially interdependent and concerted misconduct by ML Trust, ML Life, and Medina. *See Grigson*, 210 F.3d at 527 ("First, equitable estoppel applies when the signatory to a written agreement containing an arbitration clause must rely on the terms of the written agreement in asserting its claims against the nonsignatory. . . . Second, application of equitable estoppel is warranted when the signatory to the contract containing an arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract. Otherwise the arbitration proceedings between the two signatories would be rendered meaningless and the federal policy in favor of arbitration effectively thwarted." (emphasis omitted)).

We have previously noted that when the FAA applies there is some question as to whether federal law or state law applies to the issue of whether a party to a lawsuit may be compelled to arbitrate its claims. *In re Kellogg Brown & Root, Inc.*, 166 S.W.3d 732, 738-39 (Tex. 2005). We cited *Washington Mutual Finance Group, LLC v. Bailey*, 364 F.3d 260, 267-68 (5th Cir. 2004), in acknowledging the Fifth Circuit's position that federal law generally applies. *In re Kellogg Brown & Root*, 166 S.W.3d at 738-39. The Fifth Circuit explained that "because the determination of

whether a non-signatory is bound by an arbitration provision 'presents no state law question of contract formation or validity,' a court should 'look to the federal substantive law of arbitrability to resolve this question.'" *Bailey*, 364 F.3d at 268 n.6 (quoting *Int'l Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH*, 206 F.3d 411, 417 n.4 (4th Cir. 2000)). Nevertheless, we concluded that state law may also play a role in the decision, and we applied "state law . . . informed by persuasive and well-reasoned federal precedent." *In re Kellogg Brown & Root*, 166 S.W.3d at 739. Subsequently, we noted the importance of maintaining uniformity of state and federal law on this issue, stating that "[w]e remain mindful of the importance of keeping federal and state law uniform so that arbitrability does not depend on where one seeks to compel it." *In re Vesta*, 192 S.W.3d at 763.

Equitable estoppel cannot force parties such as the Alanizes to arbitrate if they have not agreed to do so in the first instance. *See Bridas S.A.P.I.C. v. Gov't of Turkm.*, 345 F.3d 347, 360-61 (5th Cir. 2003) (noting that equitable estoppel could not be used to compel a nonsignatory to arbitrate and distinguishing *Grigson* by noting that in *Grigson* the court "estopped a *signatory* plaintiff from relying upon the *defendants*' status as a nonsignatory to prevent the defendants from compelling arbitration under the agreement. We justified applying equitable estoppel in *Grigson* in part because to do otherwise would permit the signatory plaintiff to 'have it both ways.'"). Thus, equitable estoppel does not, by itself, create an agreement to arbitrate. But here, the Alanizes agreed to arbitrate—the question is with whom and what.

The Alanizes' claims do not fall under the first *Grigson* equitable estoppel prong. The claims do not refer to or presume the existence of the CMA agreement containing the arbitration clause.

But I would hold that because we are dealing with the FAA, under *Grigson*'s second prong the Alanizes are equitably estopped from asserting the lack of an agreement to arbitrate with ML Life and ML Trust as to those claims which depend on actions or omissions of Medina for which the Alanizes are also suing Medina. The Alanizes' agreement to arbitrate encompasses those disputes.

In determining whether an outside party may assert equitable estoppel as a basis for joining arbitration proceedings, the Fifth Circuit has held that "'[t]he lynchpin for equitable estoppel is equity' and the point of applying it to compel arbitration is to prevent a situation that 'would fly in the face of fairness.'" *Hill v. G E Power Sys., Inc.*, 282 F.3d 343, 349 (5th Cir. 2002) (quoting *Grigson*, 210 F.3d at 527). Reviewing the various ways that proceedings could develop in this case, it seems that equity mandates allowing ML Trust and ML Life to participate in the arbitration. Speculating about future developments in lawsuits and legal theories parties might advance is generally not very productive. But at the risk of being nonproductive, one can envision how, if the claims against ML Trust and ML Life which are based on claims the Court holds the Alanizes must arbitrate with Medina are not referred to arbitration, then the possibility, if not probability, exists that Medina is going to be a significant part of the litigation whenever the Alanizes' suit against ML Trust and ML Life is prosecuted. One reason for this comes to mind immediately. If Medina prevails in the arbitration, the Alanizes could press an argument in the lawsuit that even though the arbitration might preclude Medina's personal liability to the Alanizes, his actions are imputable to ML Trust and ML Life because he acted as their agent and they should be held responsible for his actions. If that or some similar (or dissimilar) argument is entertained by the trial court, Medina is sure to be deposed, subpoenaed to testify at trial, etc.

On the other hand, and again without trying to speculate as to all the arguments counsel might develop, one can envision how, if the Alanizes prevail on their claims against Medina in arbitration, ML Trust and ML Life would argue that the arbitration proceedings do not bind them and that they remain entitled to fully litigate any issue involving Medina's allegedly improper actions or omissions before the actions or omissions can be imputed to them. The net result is that Medina ends up deeply enmeshed in the litigation process no matter what happens in arbitration.

The above scenarios do not take into account various other problems presented by requiring the Alanizes to arbitrate only against Medina. For example, what happens if, after Medina and the Alanizes arbitrate, ML Trust and ML Life attempt to sue or hold Medina as a party to the lawsuit to recover damages they must pay the Alanizes resulting from Medina's actions as their agent? If they are for some reason barred or restricted from claiming against Medina because of arbitration proceedings, ML Trust and ML Life will almost assuredly claim that their rights have been impaired by the arbitration in which they were not allowed to participate. But if the trial court allows Medina to be brought into and kept in the lawsuit by ML Trust and ML Life, Medina loses the benefit of having arbitrated his disputes with the Alanizes.

One solution to all of this is the second prong of *Grigson*'s equitable estoppel construct. *Grigson*, 210 F.3d at 527. The Alanizes should be equitably estopped from asserting they have no arbitration agreement with ML Trust and ML Life to the extent the Alanizes claim ML Trust and ML Life are liable because of Medina's misconduct. Their claims that Medina wronged them are disputes the Alanizes, under the law, agreed to arbitrate. The claims against ML Trust and ML Life that rely on Medina's alleged misconduct depend on "substantially interdependent and concerted

misconduct" by Medina, ML Trust and ML Life because they are based on the same allegations of misconduct. *See Brown v. Pac. Life Ins. Co.*, 462 F.3d 384, 398-99 (5th Cir. 2006); *Grigson*, 210 F.3d at 527. There is little, if any, inequity to the Alanizes if ML Trust and ML Life are included in the arbitration to the extent noted above. The facts and claims in arbitration would remain the same and would pose little, if any, increased burden on the Alanizes. The Alanizes are in control of their own fate: they arbitrate only facts and matters underlying the misconduct which they allege both against Medina and as a basis for the companies' liability to them.

In *Brown*, the Fifth Circuit affirmed the trial court's determination that the Browns, signatories to an arbitration agreement, were equitably estopped under *Grigson*'s second prong from asserting that lack of an arbitration agreement precluded their being required to arbitrate with a nonsignatory to the agreement. *Brown*, 462 F.3d at 398-99. In doing so, the court did not question the validity of *Grigson*'s second prong as a basis for applying equitable estoppel to require arbitration. To the contrary, the court noted that "[t]his circuit does not stand alone in approving the use of equitable estoppel against a non-party to an arbitration agreement" and cited cases from the Fourth, Seventh, Eighth, and Eleventh federal circuits. *Id*. at 398 n.9.

In *Meyer v. WMCO-GP, LLC*, 211 S.W.3d 302, 305 (Tex. 2006), a case brought under the Texas General Arbitration Act[1] as opposed to the FAA, the trial court refused to compel arbitration between a signatory and a nonsignatory. The court of appeals affirmed. In holding that the trial court abused its discretion in refusing to compel arbitration, we discussed the two *Grigson* prongs

[1] *See* TEX. CIV. PRAC. & REM. CODE §§ 171.001-.098.

for applying equitable estoppel. *Id*. at 305-06. Our decision that the signatory, WMCO, was equitably estopped from refusing to arbitrate its claims against the nonsignatories was bottomed on *Grigson*'s first prong. *Id*. at 306. However, we also addressed, without questioning its validity, the second prong of *Grigson* in refuting the court of appeals' conclusion that WMCO's claims against the nonsignatories were not intertwined with its claims against the signatory:

> Finally, the court [of appeals] concluded that WMCO's claims against Meyer and Ford were not intertwined with claims against Bullock. This is simply wrong. WMCO's claims against Meyer and Ford are not only intertwined with its claims against Bullock, they have the same tap root: WMCO's assertion that Ford lost its right of first refusal.

Id. at 307. The one dissenting justice did not argue that the second *Grigson* prong was not a valid basis under the TAA for equitably estopping a signatory from refusing to arbitrate with a nonsignatory, but disagreed that either prong was satisfied. *Id*. at 308 (O'Neill, J., dissenting). Thus less than a year ago we at least implied both prongs of *Grigson*'s equitable estoppel construct apply even in cases subject to the TAA. Just as the claims in *Meyer* had "the same tap root," to the extent the Alanizes' claims against Medina, ML Trust, and ML Life in this case are based on Medina's alleged misconduct, they have the same root system: Medina's actions.

The two-pronged equitable estoppel framework set out in *Grigson* and referenced recently in *Brown* is the Fifth Circuit's position on equitable estoppel and arbitration pursuant to the FAA. I would conform our decisions to that position in FAA cases until either the Fifth Circuit or the United States Supreme Court rejects the construct.

We have held that "[m]andamus is proper to correct a clear abuse of discretion when there is no adequate remedy by appeal, as when a party is erroneously denied its contracted-for arbitration

rights under the FAA." *In re D. Wilson Constr. Co.*, 196 S.W.3d 774, 780 (Tex. 2006). It is within the trial court's discretion whether to apply equitable estoppel in cases like this. *See Brown*, 462 F.3d at 398; *Grigson*, 210 F.3d at 528. But a trial court "has no 'discretion' in determining what the law is or applying the law to the facts." *Meyer*, 211 S.W.3d at 308 (quoting *Walker v. Packer*, 827 S.W.2d 833, 840 (Tex. 1992)). On this record I would hold that any discretion in compelling arbitration of the Alanizes' claims against ML Trust and ML Life is foreclosed as to claims based on Medina's actions. Those claims are not just arguably substantially interdependent and concerted. They are the same claims based on the same facts: Medina's actions. If those claims are tried by the Alanizes and the companies, as opposed to being arbitrated with Medina, Medina can hardly avoid being a key part of the trial. If he is, one aspect of the federal policy favoring arbitration of claims within the scope of a valid arbitration agreement will be frustrated: disputes based on Medina's actions will not be quickly and efficiently resolved. The claims in all probability will be arbitrated and then tried in the lawsuit to a significant degree.

I join parts I and II of the Court's opinion. I dissent from the Court's refusal to direct the trial court to order the Alanizes' claims against ML Trust and ML Life to arbitration to the extent the claims against the companies are based on Medina's alleged misconduct. As to claims against ML Trust and ML Life not based on Medina's actions, I agree that the trial court did not abuse its discretion in failing to order arbitration. If mandamus relief were granted to ML Trust and ML Life as well as to Medina, I would not direct the trial court to stay the remaining trial proceedings because claims remaining in the lawsuit would not involve disputes sent to arbitration. But given the Court's holding that the Alanizes are not required to arbitrate any claims with ML Trust and ML Life, I agree

that the litigation must be stayed pending completion of the arbitration between the Alanizes and Medina because both the arbitration and the litigation will encompass claims based on Medina's actions. Accordingly, I also join the Court's opinion as to part IV.

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Phil Johnson
Justice

OPINION DELIVERED: August 24, 2007