Kluwer Arbitration Blog

# Northern District of California Compels Arbitration Between Contractor and Non-Signatory Insurer of Subcontractor

Griffin Carlson (UCLA) · Wednesday, May 22nd, 2024

On March 11, 2024, in *Swinerton Builders, Inc. v. Argonaut Insurance Company*, a district court in the Ninth Circuit found a valid arbitration agreement between the contractor, Swinerton Builders, Inc. ("Swinerton"), and the non-signatory insurer, Argonaut Insurance Co. ("Argonaut"), of its subcontractor, Northern Services, Inc. ("Northern"). No. 23-CV-4158 (DMR), 2024 WL 1057473 (N.D. Cal. Mar. 11, 2024). Northern's projects that Argonaut insured were governed by a framework agreement between Swinerton and Northern which included an arbitration clause. The court denied Argonaut's motion to dismiss the case for lack of subject matter jurisdiction and converted it into a motion to compel arbitration under Section 4 of the Federal Arbitration Act ("FAA") which it then granted on the basis of the interconnectedness of the agreements and bonds that bound the parties to the arbitration process outlined in the framework agreement. This decision represents an extension of the reach of arbitration agreements to include parties that have not directly signed the original contract, particularly in the construction industry.

**The Contractor and Subcontractor Entered into a Framework Agreement Containing an Arbitration Clause, Covering Three Work-Orders That Were Secured by the Subcontractor's Insurer**

In December 2019, Swinerton engaged Northern as a subcontractor under a Master Subcontract Agreement ("MSA"). This MSA outlined general terms and conditions for all specific work orders that Swinerton would assign to Northern. The MSA's dispute resolution clause defined disputes broadly and mandated binding arbitration under the Construction Industry Rules of the American Arbitration Association ("AAA"). Following this agreement, Swinerton and Northern executed three specific work orders, which were explicitly stated to be part of the overarching MSA. As required by the work orders for these projects, Northern obtained performance and payment bonds from a California-licensed insurer, Argonaut.

**Project Default and Subsequent Legal Action**

However, complications arose when Northern's owner passed away, leading to Northern's failure to complete the three projects. Despite Swinerton's notifications to Argonaut about Northern's defaults, Argonaut refused to honor the claims under the performance and payment bonds. In response, Swinerton filed a lawsuit against Argonaut in August 2023, alleging breach of contract and failure to fulfill the surety obligations associated with the defaulted projects.

**The Trial Court Denies Insurer's Motion to Dismiss, Converts Into and Grants Motion to Compel Arbitration**

The central legal question was whether Argonaut, as a non-signatory, could be compelled to arbitrate based on its surety bonds for Northern's work orders with Swinerton which were incorporated by reference into the MSA. The court reasoned that the integration of the work orders with the MSA, which explicitly included an arbitration clause, suggested an intention for parties involved in executing the work orders, including the insurer, to be bound by the MSA's dispute resolution terms. This interpretation was supported by the fact that the performance bonds issued by Argonaut effectively guaranteed Northern's obligations under those work orders and brought Argonaut within the ambit of the arbitration agreement by reference.

***Boys Club v. Fidelity* and *Kramer v. Toyota*: Compelling Non-Signatories to Arbitration**

Compelling non-signatories to arbitration is not novel nor is it well settled. The question of whether non-signatories can be compelled to arbitrate has been addressed before in two cases with divergent outcomes: *Boys Club v. Fidelity* and *Kramer v. Toyota*.

In *Boys Club*, the California Court of Appeal held that "[a]n arbitration agreement in an incorporated bonded contract may be used to compel arbitration of disputes involving that incorporated bonded contract." *Boys Club*. *Boys Club of San Fernando Valley, Inc. v. Fidelity & Deposit Co.*, 6 Cal. App. 4th 1266, 1274 (1992). Swinerton sought to differentiate *Boys Club* on grounds that there was unequivocally "'no dispute that the bonded contractor was in default' and '[t]he only dispute is the failure of Argonaut to honor the bonds.'" *Swinerton Builders*, 2024 WL 1057473, at *7. The district court found this distinction immaterial since Argonaut's liability on the bonds was contingent on Northern's own contractual breaches. *Id.*

This marks a departure from the precedent set in *Kramer*, a case Swinerton used to argue against compelling arbitration. In *Kramer v. Toyota Motor Corp.*, the Ninth Circuit denied a motion to compel arbitration due to the absence of a direct arbitration agreement between the disputing parties, where the defendant, a car manufacturer, was not a signatory to the purchase agreements which contained the arbitration clauses, and the parties to the arbitration clauses were explicitly limited to the plaintiffs and their car dealerships. 705 F.3d 1124-25, 1127 (noting the lack of "clear and unmistakable evidence that Plaintiffs agreed to arbitrate arbitrability with nonsignatories"). The *Swinerton* court distinguished from *Kramer* since performance bonds issued by Argonaut effectively integrated the work orders into MSA and its arbitration provision. This highlights incorporation of the arbitration clause through the performance bonds into the contractual framework between Swinerton, Northern, and indirectly, Argonaut Insurance.

**Delegation of the Gateway Issue and Incorporation of Rules of Construction Industry Arbitration Rules of the AAA Gives Arbitrator Authority to Determine Applicability of Arbitration Agreement to Contractor's Surety Claims**

The MSA delegated to the arbitrator the gateway issue of "whether the arbitration agreement applies to [Swinerton's] claims in this litigation" since it incorporated by reference the rules of the Construction Industry Arbitration Rules of the American Arbitration Association. *Swinerton Builders*, 2024 WL 1057473, at *7; *see Portland Gen. Elec. Co. v. Liberty Mut. Ins. Co.*, 862 F.3d 981, 985 (9th Cir. 2017) (noting that "parties may delegate the adjudication of gateway issues to the arbitrator if they 'clearly and unmistakably' agree to do so" and stating, "[w]e have found such delegation when the parties have incorporated by reference the rules of the American Arbitration Association"). Here, agreement over delegation of gateway issues was clear and unmistakable

since Swinerton did "not dispute the MSA's delegation of gateway issues, including the power to determine arbitrability of a claim, to the arbitrator." *Swinerton Builders*, 2024 WL 1057473, at *7-8.

***Conclusion – the Broadening Scope and Impact of Arbitration Agreements***

The *Swinerton* ruling demonstrates the court's endorsement of the FAA's "liberal federal policy favoring arbitration agreements." *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 625 (1985). Moreover, it aligns with the Ninth Circuit's interpretation of Article II, Section 3 of the New York Convention as self-executing, and privileged in the realm of federal arbitration jurisdiction, notwithstanding opposing state laws. *See CLMS Mgmt. Servs. et al. v. Amwins Brokerage et al.*, 8 F.4th 1007, 1014 (9th Cir. 2021). The *Swinerton* decision extends the application of arbitration agreements to include non-signatories under specific conditions, reflecting the growing American preference for and power of agreements sourcing disputes to arbitration. This decision carries weight both parties to international contracts and the international arbitration community at large. Whether directly entering into an international contract, or indirectly entering into an international contract as a third party by agreeing to carry out some of the obligations detailed in the international contract, parties should note the growing potential inclusivity of arbitration clauses. Third parties should keep an eye out for contractual language that incorporates framework agreements. As highlighted in the discussion above, such framework agreements may contain arbitration clauses that are binding for third parties to the extent the framework agreement is referenced in the contract concluded between the third party and one of the primary parties.

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