

Delaware Court of Chancery Finds Non-Signatory Subsidiary Bound by Forum Selection Provision Contained in Contract with Its Parent

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In a recent decision, the Delaware Court of Chancery held that a non-signatory subsidiary of one party to a contract could be bound by the forum selection clause in that contract where it directly benefited from the contract and it was clear from the circumstances surrounding the transaction that the parties to the contract expected the forum selection provision to apply to the non-signatory.

The Court of Chancery action was commenced by the buyer and the subject company of a stock purchase agreement asking the court, among other things, to issue an anti-suit injunction against the seller and one of its subsidiaries that had previously sued the plaintiffs in a Texas state court. The request was based on a forum selection provision contained within the stock purchase agreement entered into between the buyer and the seller. Notably, the seller's subsidiary was not a signatory to the stock purchase agreement. The dispute among the parties stemmed primarily from a supply agreement that was entered into with the seller's subsidiary along with the stock purchase agreement—hence the involvement of the subsidiary. Since the subsidiary had not signed the stock purchase agreement containing the forum selection provision at issue, the initial question the Court had to answer was whether the subsidiary, as a non-signatory, could be bound to the provision. The Court then had to determine whether both the claims brought by the seller and those brought by its subsidiary—if it was bound—fell within the forum selection provision.

The plaintiffs argued that the seller was bound to bring all claims under the stock purchase agreement and the supply agreement in Delaware under a single agreement theory, and that the subsidiary was bound under the same theory or, in the alternative, because it accepted a benefit arising from the stock purchase agreement, that should preclude it from evading the burden of the forum selection provision.

The Court started its analysis with the application of the forum selection provision to the seller's claims. It quickly determined that the forum selection provision applied to the seller as a signatory of the stock purchase agreement. As the forum selection provision designated Delaware as the proper forum for "any Proceeding arising out of or relating to" the stock purchase agreement or "any other Transaction Document or [] any agreements contemplated...thereby," with "Transaction Document" specifically including the supply agreement in its definition, the Court had no trouble finding that any claims brought in Texas that "related to" the supply agreement also fell within the ambit of the forum selection provision and should be brought in Delaware.

In so finding, the Court rejected the seller's argument that an integration clause in the supply agreement—stating that the supply agreement and other agreements referred therein made up the entirety of the agreement among the parties—precluded the application of the forum selection clause to disputes over the supply agreement. It reasoned that the integration clause contained in the stock purchase agreement, which specifically incorporated the supply agreement, precluded the seller's interpretation.

The Court then turned to the trickier analysis of whether the non-signatory subsidiary could be bound by the forum selection provision and be enjoined from bringing suit in Texas against the plaintiffs. In support of their claim that the subsidiary should be bound, the plaintiffs advanced two arguments: (1) the stock purchase agreement and the supply agreement should be read as a single contract and, therefore, as binding parties to either agreement to the forum selection provision, and (2) the subsidiary should be found to be bound to the forum selection provision under principles of estoppel.

The Court declined to bind the subsidiary under a single agreement theory. Unlike reading the agreements as one for purposes of finding that the seller was bound to bring claims under the supply agreement in Delaware under the forum selection provision contained in the contract *it signed*, the Court found that binding the subsidiary to a forum selection provision contained in a contract to which it was not a party would “conflict with Delaware’s general policy of not extending the rights and obligations of contracts to parties that did not execute them, absent special circumstances.” Accordingly, the Court declined to apply the single agreement theory to bind the subsidiary.

Turning to the plaintiffs’ second theory, the Court applied the elements announced in *Capital Group Cos., Inc. v. Armour*, 2004 WL 2521295 (Del. Ch. Nov. 3, 2004). Under the *Capital Group* authority, “a court can enforce a forum selection provision against a non-signatory if...three elements are met: (i) the agreement contains a valid forum selection provision; (ii) the non-signatory has a sufficiently close relationship to the agreement, either as an intended third-party beneficiary under the agreement or under principles of estoppel; and (iii) the claim potentially subject to the forum selection provision arises from the non-signatory’s standing relating to the agreement.” As the parties agreed that the first element was met and the plaintiffs had not argued that the subsidiary was an intended beneficiary, the Court turned straight to the estoppel analysis of the second element.

Under the principles of estoppel, the Court explained, a non-signatory can be bound if (1) it accepted a direct benefit from the agreement or (2) it had a close relationship to the agreement, a signatory controlled the non-signatory, and the circumstances establish that the signatory agreed to the provision on behalf of the controlled affiliate (the “Foreseeability Test”). The Court found both tests met with regard to the subsidiary. It explained that the subsidiary benefited directly because the stock purchase agreement led to the execution of the supply agreement. Since the subsidiary had a guaranteed purchaser for its materials post-transaction thanks to the supply agreement, it clearly benefited directly from the stock purchase agreement and should not be allowed to “avoid the burdens that accompan[y] those benefits.”

Having so found, the Court then explained that the Foreseeability Test applies when “circumstances surrounding the transaction make it clear that the parties expected the forum selection provision to bind the non-signatory.” The test extends to non-signatories controlled by a signatory where those non-signatories have “a clear and significant connection to the subject matter of the agreement.” The Court found this test met as well, because the seller controlled the wholly owned subsidiary and the subsidiary had a clear and significant relationship to the stock purchase agreement because it was the entity through which the seller carried out one of its contractual obligations, since the stock purchase agreement required the seller to cause the subsidiary to enter into the supply agreement. Thus, the Court reasoned, “the parties expected the Delaware Forum Provision to bind [the Seller].”

Turning to the final element of the *Capital Group* test, the Court declined to follow an interpretation that would limit the forum selection provision as to a non-signatory to claims arising under the agreement in which the provision was contained. The Court explained that following this interpretation would limit the application in a manner that would allow the non-signatory to reap the full benefit of the agreement but only carry half its burden. The Court instead “interpret[ed] the third element of the *Capital Group* test as asking whether the claims at issue fall within the plain language of the provision.” The Court then relied on its claim-by-claim analysis regarding the seller to answer this last question, as the claims against the seller and the subsidiary were identical.

The Court's opinion in *Florida Chemical Company, LLC v. Flotek Industries, Inc.*, reminds parties to a transaction to be careful to remember that the mere absence of a signature on one of the contracts forming part of an overall transaction does not ensure that the non-signatory party is not bound by that particular agreement. It also once again emphasizes that, particularly when litigating in the Delaware Court of Chancery, the "real world business context" matters. *Florida Chemical Company, LLC et al. v. Flotek Industries, Inc.*, C.A. No. 2021-0288-JTL (Del. Ch. Aug. 17, 2021), Laster, V.C.