Supreme Court, U.S.
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No. _____

IN THE

Supreme Court of the United States

AMERICAN HOME ASSURANCE COMPANY,
Petitioner,

v.

UMG RECORDINGS, INC. and UNIVERSAL MUSIC GROUP, INC.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

Susan Koehler Sullivan
Douglas J. Collodel
Michael M. Walsh
SEDGWICK, DETERT,
MORAN & ARNOLD LLP
801 South Figueroa St., 19th Fl.
Los Angeles, CA 90017-5556
(213) 426-6900

G. Eric Brunstad, Jr.
Counsel of Record
Collin O'Connor Udell
Matthew J. Delude
DECHERT LLP
90 State House Square
Hartford, CT 06103
(860) 524-3999
eric.brunstad@dechert.com

Counsel for Petitioner

ADDITIONAL COUNSEL LISTED ON INSIDE COVER

Dated: September 27, 2010

Lawrence Klein
Scott Greenspan
SEDGWICK, DETERT,
MORAN & ARNOLD LLP
125 Broad St., 39th Fl.
New York, NY 10004-2400
(212) 898-4054

QUESTION PRESENTED

Arbitration agreements commonly provide for the arbitration of disputes "arising out of" a particular contractual arrangement. For over twenty years, the courts of appeals have divided sharply over the proper meaning of the phrase "arising out of." Most courts of appeals construe the phrase broadly to promote arbitration. The Ninth Circuit, however, construes it narrowly, as it did in this case, denying arbitration where other courts of appeals would require it. The question presented is:

Should the Court grant certiorari to resolve an entrenched, acknowledged, and long-standing conflict among the courts of appeals over the proper construction of the phrase "arising out of" used commonly in arbitration clauses to define the scope of the parties' arbitration agreement?

CORPORATE DISCLOSURE STATEMENT

Pursuant to Supreme Court Rule 14(b), Petitioner American Home Assurance Company is a direct, wholly owned subsidiary of Chartis U.S., Inc., which is a direct, wholly owned subsidiary of Chartis Inc., which is a direct, wholly owned subsidiary of AIUH LLC, which is a direct, wholly owned subsidiary of American International Group, Inc., which is a publicly held corporation. With the exception of the AIG Credit Facility Trust, a trust established for the sole benefit of the United States Treasury, no parent entity or publicly held entity owns 10% or more of the stock of American International Group, Inc.

TABLE OF CONTENTS

Page

QUESTION PRESENTED ..... *i*

CORPORATE DISCLOSURE STATEMENT ..... *ii*

TABLE OF CONTENTS ..... *iii*

TABLE OF AUTHORITIES ..... *v*

TABLE OF APPENDICES ..... *viii*

OPINIONS BELOW 1

JURISDICTION 1

RELEVANT STATUTORY PROVISIONS 2

PRELIMINARY STATEMENT 2

STATEMENT 5

A. The Insurance Program 6

B. The National Litigation 11

C. The Course of the Proceedings Below 13

TABLE OF CONTENTS
(continued)

Page

REASONS FOR GRANTING THE WRIT 17

A. The Ninth Circuit's Narrow Construction of the Phrase "Arising Out of" Deepens an Intractable and Longstanding Circuit Split and Conflicts with this Court's Precedents 19

B. The Proper Construction of the Phrase "Arising Out Of" Used Commonly in Arbitration Agreements Is of Vital Importance, and this Case Presents an Ideal Vehicle to Resolve the Conflict Among the Courts of Appeals on this Question 30

CONCLUSION 33

TABLE OF AUTHORITIES

Page

CASES

ACE Capital Re Overseas Ltd. v. Central United Life Ins. Co., 307 F.3d 24 (2d Cir. 2002) 4-5, 21

Arthur Andersen LLP v. Carlisle, 129 S. Ct. 1896 (2009) 2

Battaglia v. McKendry, 233 F.3d 720 (3d Cir. 2000) 4, 28

Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213 (1985) 15

Genesco, Inc. v. T. Kakiuchi & Co., 815 F.2d 840 (2d Cir. 1987) 22

Gregory v. Electro-Mech. Corp., 83 F.3d 382 (11th Cir. 1996) 4, 26, 27

Highlands Wellmont Health Network, Inc. v. John Deere Health Plan, Inc., 350 F.3d 568 (6th Cir. 2003) 4, 29

In re Kinoshita & Co., 287 F.2d 951 (2d Cir. 1961) 18, 20

Louis Dreyfus Negoce v. Blystad Shipping & Trading, Inc., 252 F.3d 218 (2d Cir. 2001) 21

TABLE OF AUTHORITIES
(continued)

Page

Mar-Len of Louisiana, Inc. v. Parsons-Gilbane, 773 F.2d 633 (5th Cir. 1985) 23

Mediterranean Enters., Inc. v. Ssangyong Corp., 708 F.2d 1458 (9th Cir. 1983) 17, 20-21, 25

Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983) 22, 25

Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967) 23

S.A. Mineracao da Trindade-Samitri, 745 F.2d 190 (2d Cir. 1984) 21

Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974) 26, 27

St. Paul Fire & Marine Ins. Co. v. Employers Reinsurance Corp., 919 F. Supp. 133 (S.D.N.Y. 1996) 22

Sweet Dreams Unlimited, Inc. v. Dial-a-Mattress Int'l, Ltd., 1 F.3d 639 (7th Cir. 1993) 4, 23-25

TABLE OF AUTHORITIES
(continued)

Page

Tracer Research Corp. v. Nat'l Envtl. Servs. Co., 42 F.3d 1292 (9th Cir. 1994) ..... *passim*

STATUTES

9 U.S.C. § 2 2

9 U.S.C. § 3 2

9 U.S.C. § 4 2

9 U.S.C. § 16 2

28 U.S.C. § 1254(1) 2

28 U.S.C. § 1332 1

28 U.S.C. § 1441(d) 1

OTHER AUTHORITIES

Mark Berger, *Arbitration and Arbitrability: Toward an Expectation Model*, 56 BAYLOR L. REV. 753 (2004) 22-23

TABLE OF APPENDICES

Page

Appendix A — Opinion of the United States Court of Appeals for the Ninth Circuit Decided May 13, 2010 ..... 1a

Appendix B — Order of the United States District Court for the Central District of California Dated November 3, 2008 ..... 5a

Appendix C — Excerpts from 2001 Payment Agreement 18a

Appendix D — Excerpt from 2001 Large Risk Rating Plan Endorsement 26a

Appendix E — Statutory Appendix 27a

Appendix F — Order of the United States Court of Appeals for the Ninth Circuit Filed June 29, 2010 ..... 30a

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Ninth Circuit, Pet. App. 1a, is unpublished, although it is available at 2010 WL 1917561 (9th Cir. May 13, 2010). The opinion of the United States District Court for the District of Central California, Pet. App. 5a, is unpublished.

JURISDICTION

Respondents UMG Recordings, Inc. and Universal Music Group, Inc. (collectively "UMG")[1] are Delaware corporations with principal places of business in Los Angeles County, California. American Home Assurance Company ("American Home") is a New York corporation with its principal place of business in New York, New York. UMG commenced the underlying litigation in state court, and American Home invoked removal jurisdiction under 28 U.S.C. § 1441(d). The district court possessed diversity jurisdiction over the removed litigation pursuant to 28 U.S.C. § 1332. The district court denied American Home's motion to stay the litigation pending arbitration on November 3, 2008. Pet. App. 5a.

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[1] Both UMG entities are subsidiaries of non-party Vivendi S.A. ("Vivendi").

The Ninth Circuit possessed jurisdiction over American Home's appeal pursuant to 9 U.S.C. § 16. *See Arthur Andersen LLP v. Carlisle*, 129 S. Ct. 1896, 1900 (2009) (citing 9 U.S.C. § 16(a)(1)(A)). The court of appeals entered its judgment on May 13, 2010. Pet. App. 1a. American Home's petition for rehearing was denied on June 29, 2010. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

RELEVANT STATUTORY PROVISIONS

The provisions of 9 U.S.C. §§ 2, 3, 4 are reprinted at Pet. App. 27a-29a pursuant to Supreme Court Rule 14(f).

PRELIMINARY STATEMENT

American Home is an insurer. UMG sued American Home in the underlying litigation, claiming that American Home breached various obligations to UMG under certain policies of insurance (the "Policies"). During the course of the litigation, American Home argued that UMG could not state a claim for damages because, under a series of documents related to the Policies (the "Payment Agreements"), UMG is obligated to reimburse American Home for any damages American Home might have to pay. UMG disputed its reimbursement obligation under the Payment Agreements, and American Home

claims that this discrete reimbursement dispute is subject to arbitration.

The Payment Agreements set forth UMG's reimbursement obligation. Pet. App. 18a-21a. Specifically, the Payment Agreements provide that "the amounts that [UMG] must pay [American Home] ... include ... Deductible Loss Reimbursements," which the agreements define as UMG's share of any losses that American Home incurs in processing and defending claims under the policies (provided those losses are within certain applicable limits, as in this case). Pet. App. 19a-20a; *see also infra* note 4. The Payment Agreements also contain an arbitration clause (the "Arbitration Clause"), covering any dispute "arising out of" the Payment Agreements. Pet. App. 22a-25a.

Applying a narrow interpretation of the phrase "arising out of," the court below concluded that the dispute over UMG's reimbursement obligation is not arbitrable. The court began by observing that the "underlying dispute" in the litigation involves UMG's claim for breach of the Policies. Pet. App. 3a. Citing its own precedent construing the phrase "arising out of" restrictively, the court then reasoned that the discrete dispute over UMG's reimbursement obligation set forth in the Payment Agreements does not "arise out of" the agreements because UMG contests its reimbursement obligation in

the context of the underlying litigation over the Policies and asserts that American Home breached the Policies as a defense. Pet. App. 3a (citing *Mediterranean Enters., Inc. v. Ssangyong Corp.*, 708 F.2d 1458, 1464 (9th Cir. 1983)). In other words, the court below held that, even where a contract (here the Payment Agreements) sets forth a party's obligation (here UMG's reimbursement obligation) and contains an arbitration clause regarding disputes involving that obligation, a dispute does not "arise out of" that particular contract if resolution of the dispute involves consideration of more than just the contract itself – here, whether American Home breached the Policies, which UMG asserts as a defense to its reimbursement duty.

The Ninth Circuit's narrow interpretation of the meaning of the phrase "arising out of" conflicts irreconcilably with the decisions of at least four other courts of appeals. Other courts of appeals apply a much more generous interpretation and have specifically rejected the Ninth Circuit's approach. *E.g., Highlands Wellmont Health Network, Inc. v. John Deere Health Plan, Inc.*, 350 F.3d 568, 577-78 (6th Cir. 2003); *Battaglia v. McKendry*, 233 F.3d 720, 723-27 (3d Cir. 2000); *Gregory v. Electro-Mech. Corp.*, 83 F.3d 382, 385-86 (11th Cir. 1996); *Sweet Dreams Unlimited, Inc. v. Dial-a-Mattress Int'l, Ltd.*, 1 F.3d 639, 641 (7th Cir. 1993); *see also ACE Capital Re Overseas Ltd. v. Central United Life Ins. Co.*, 307 F.3d 24,

43-33 (2d Cir. 2002) (Sotomayor, J.). Indeed, under the approach that these other courts of appeals have taken, American Home's request for arbitration of the reimbursement dispute would have been granted. The issue is one of vital importance, and certiorari is warranted here to resolve this longstanding conflict among the courts of appeals.

STATEMENT

Prior to January 1, 2001, UMG and its corporate parent, Vivendi, sought to obtain commercial general liability, automobile, and workers' compensation insurance. Because of the size, complexity, and cost of this insurance, as well as the particular needs of Vivendi and UMG, the terms of the insurance that they ultimately purchased were carefully negotiated, structured, and tailored to suit Vivendi and UMG's unique requirements. The carefully structured insurance program ("Insurance Program") at issue here is the result of the parties' negotiation.[2]

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[2] UMG acknowledged in the district court that it is a named insured under the Insurance Program. ER-531. UMG agreed to the initial Payment Agreement and Schedule on May 4, 2001. ER-572, 591. The term "You" is defined in the Payment Agreements as not only Vivendi, but "each of its subsidiary, affiliated or associated organizations that are included as Named Insureds

A. The Insurance Program

Unlike a traditional consumer insurance policy, the Insurance Program does not involve the simple issuance of a single policy document. Rather, it consists of a series of interrelated documents that serve different functions. The master documents are the Payment Agreements, the first of which was entered into in 2001 and the second in 2004. ER-563, 572, 638, 648.[3] Each Payment Agreement establishes the general structure of the Insurance Program, cross-references and incorporates other relevant program documents, and defines and explains the basic rights and obligations of the parties. Pet. App. 18a-21a. Each Payment Agreement explains that UMG is obligated to pay American Home the costs of the Insurance Program, which is defined as "Your Payment Obligation." Pet. App. 20a-21a.

UMG's Payment Obligation is not limited to paying an up-front "premium." Like other

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under any of the *Policies*" and further provides that "[e]ach is jointly and severally liable to [American Home] for the entire amount of *Your Payment Obligation*." Pet. App. 20a. The phrase "Your Payment Obligation" includes the reimbursement obligation at issue in this case. Pet. App. 20a-21a.

[3] The term "ER" refers to certain "excerpts of record" filed in the Ninth Circuit.

policies of this type, UMG also has certain deductible reimbursement obligations that it must meet. ER-024, 026-27, 067, 168, 307, 532. Unlike a traditional consumer insurance policy (where the insured consumer pays a premium up-front and then bears the full amount of any loss until any applicable deductible limit is reached), the Insurance Program provides that American Home will advance payment for losses incurred and then seek reimbursement from UMG of certain amounts in accordance with the terms of the Payment Agreements.

Specifically, UMG's Payment Obligation is defined to include not only its liability for premiums, but also its share of American Home's losses and expenses in handling claims (*i.e.*, UMG's deductible reimbursement obligation). Pet. App. 20a-21a. To that end, the Payment Agreements define UMG's Payment Obligation as "the amounts that [UMG] must pay [American Home] for the insurance and services in accordance with the terms of the *Policies*, this Agreement, and [certain other policies]"; moreover, "[s]uch amounts shall include . . . premiums and premium surcharges [and] Deductible Loss Reimbursements." Pet. App. 20a. The Payment Agreements define UMG's "Deductible Loss Reimbursement" obligation as UMG's share of any losses incurred by American Home in processing and defending claims under the poli-

cies (provided those losses are within applicable deductible limits, as in this case).[4]

The Payment Agreements also contain the Arbitration Clause at issue in this matter. Pet. App. 22a-25a. This clause provides broadly that if UMG disputes any of its payment obligations to American Home under any Payment Agreement, including any deductible reimbursement obligation, UMG must identify and explain the contested items. Pet. App. 22a. If the matter remains unresolved between the parties after sixty days, the dispute must then "be submitted to arbitration." Pet. App. 22a. Further, each

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[4] The term "Deductible Loss Reimbursement" is defined specifically as "the portion of any *Loss* and *ALAE* [American Home] pay[s] that [UMG] must reimburse [American Home] under any 'Deductible' or 'Loss Reimbursement' provisions of a *Policy*." Pet. App. 19a. The term "Loss" is defined as "damages, benefits or indemnity that [American Home] become[s] obligated under the terms of the *Policies* to pay to claimants." Pet. App. 19a. The term "ALAE" is defined as "Allocated Loss Adjustment Expense as defined in the *Policies*." Pet. App. 19a. That term is defined in the LRRPs (*see infra,* note 5) attached to the policies to include all costs and fees, including attorneys' fees, incurred in the "defense of a loss or a claim or suit against [UMG]." Pet. App. 27a. In the proceedings in the district court, UMG admitted that it is responsible for any reimbursement obligations it owes to American Home under the Insurance Program; it simply contests the applicability of the reimbursement obligation to its claims. ER-495-97.

Payment Agreement provides expansively that "[a]ny other unresolved dispute *arising out of* this Agreement must be submitted to arbitration." Pet. App. 23a (emphasis added).

In addition to the Payment Agreements (which as noted function as the master documents in the Insurance Program), the Insurance Program also includes the Schedules attached to each Payment Agreement. These Schedules list the relevant commercial general liability, automobile, and workers' compensation policies issued to Vivendi and UMG.[5] Finally, the Insurance Program also includes the Policies themselves.[6]

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[5] The Insurance Program further includes certain Loss Risk Rating Plan endorsements ("LRRPs"), a third category of documents appended to the policies listed on the Schedules.

[6] The relevant Policies at issue are the four commercial general liability policies identified in the 2001-2004 Schedules – these are the policies UMG claims American Home breached. The LRRP attached to each policy (*see supra,* note 5) sets forth the relevant deductible limits for each policy. The LRRPs attached to the 2001 and 2002 policies establish a deductible of $500,000 per occurrence for each of those policy years. ER-067, 168. The LRRP attached to the 2003 policy sets a deductible of $1,000,000 for policy year 2003, ER-307, and the LRRP attached to the 2004 policy sets a deductible of $250,000 for policy year 2004. ER-024, 026-27. UMG acknowledged these deductible limits in the proceedings below. ER-532.

In accordance with the applicable deductible limits of the Insurance Program, if American Home must pay a judgment or settlement on a covered claim that is less than the relevant limit, UMG would be responsible for reimbursing the payment as part of UMG's deductible reimbursement obligation. For example, if the $1 million deductible limit under the 2003 policy applied, and the amount of the judgment or settlement that American Home paid was $800,000, UMG would be responsible for reimbursing American Home that amount.[7]

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[7] *See supra*, note 6. American Home's payment of defense costs works in a similar way. ER-014. For example, if the same $1 million deductible applied, and the judgment or settlement was again for $800,000, UMG would be responsible for paying all of the defense costs because the amount of the judgment or settlement was less than the deductible amount, and UMG would be responsible for all costs associated with the judgment or settlement. ER-014. On the other hand, if American Home's payment exceeded the deductible limit, UMG and American Home would be responsible for sharing responsibility for the defense costs on a pro rata basis. ER-014. For example, if the $1 million deductible applied, and the judgment or settlement was for $2 million, and, further, the defense costs were $500,000, then UMG would be responsible for one half of the defense costs ($250,000), and American Home would be responsible for the other half. ER-014-15.

B. The National Litigation

In April of 2005, a group of plaintiffs commenced the National Litigation against UMG in state court. Pet. App. 10a. Through a series of amended complaints, the plaintiffs alleged a broad assortment of claims against UMG, including racketeering, collusion, extortion, fraud, breach of contract, defamation, and libel. *See National Music Marketing, Inc. v. Universal Music Group, Inc.*, LASC Case No. SC085231. Of all these numerous allegations, American Home contends that only the defamation and libel claims were conceivably covered under American Home's Policies. Pet. App. 10a.

UMG tendered the National Litigation complaint to American Home on or about May 24, 2005. Pet. App. 10a. Following roughly two years of apparent miscommunications and contested factual circumstances, American Home contends that UMG settled the case for $360,000 without American Home's knowledge or consent. Am. Home Assur. Co.'s Reply to UMG Recordings, Inc. and Universal Music Group, Inc.'s Statement of Genuine Issues of Material Fact, at 25 (July 14, 2008). On April 3, 2008, UMG forwarded a copy of the settlement agreement to American Home after UMG had already consummated the settlement and approximately one year after UMG sued American Home. *Id.* at 26.

American Home contends that the settlement amount is less than the deductible limits of the Policies.[8] Accordingly, American Home maintains that UMG is fully responsible under its deductible reimbursement obligation for 100 percent of the settlement and 100 percent of the associated defense costs.[9]

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[8] As noted (*see supra* notes 6 & 7), the respective deductibles for the four policies at issue are $500,000 for the 2001 policy; $500,000 for the 2002 policy; $1 million for the 2003 policy; and $250,000 for the 2004 policy. The $360,000 settlement did not exceed the deductible limits for 2001, 2002, and 2003. In addition, UMG has not contended that more than $250,000 of the $360,000 settlement is attributable to the 2004 policy.

[9] Among other things, American Home also contends that the settlement agreement does not allocate the $360,000 among either (1) the various defendants (one of whom was not an insured under any of American Home's Policies and therefore not covered); (2) the various claims asserted against UMG in the National Litigation (only two of which – defamation and trade libel – were conceivably covered under the policies); or (3) the various years of coverage. *Id.* at 27-30. American Home further contends that, although it asked UMG for more information on these issues so it could determine what portion of the settlement (if any) is actually covered under the policies as a settlement by an insured of a covered claim, UMG failed to provide this information. *Id.* at 30.

C. The Course of the Proceedings Below

On April 13, 2007, UMG sued American Home in state court, alleging bad faith and breach of its duty to defend UMG in the National Litigation. American Home removed the action to the district court. American Home filed its answer in December of 2007, denying UMG's allegations and also seeking reformation to correct certain errors in the 2003 and 2004 policies (which reformation the district court granted, Pet. App. 15a). Additionally, American Home raised its right to reimbursement as a defense to UMG's claims.

On May 30, 2008, American Home moved for summary judgment in the case, arguing, *inter alia*, that UMG cannot state a claim for damages because UMG is responsible under the Payment Agreements for reimbursing American Home in full for any and all amounts American Home is obligated to pay UMG in defense and settlement costs. Specifically, American Home explained: "[u]nder the policies, American Home's contractual obligation is only to 'front' these amounts – they must be reimbursed back to American Home under the terms of the Policies." SER-057.[10]

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[10] The term "SER" refers to certain "Supplemental Excerpts of Record" filed in the Ninth Circuit.

On June 23, 2008, UMG filed its opposition to American Home's motion for summary judgment. For the first time, UMG disputed that it had any obligation to reimburse American Home for the amount of the settlement or defense costs. ER-542-43. Specifically, UMG argued that "it is Vivendi, not UMG, that would have any such duty." ER-542. As noted above, however, UMG bears the same reimbursement obligations under the Payment Agreements as Vivendi. *See supra,* note 2. In addition, UMG argued that "American's breaches have relieved UMG of its duties," including its deductible reimbursement obligation. ER-543.

As noted, American Home contends that any dispute regarding UMG's reimbursement obligation is subject to the Arbitration Clause in the Payment Agreements. Pet. App. 16a. Accordingly, on July 11, 2008, American Home served an arbitration demand on UMG with respect to this dispute. ER-671, 674. In light of American Home's position that an arbitrable dispute existed, on July 14, 2008, American Home further filed a motion to stay the litigation in the district court pending resolution of the arbitration dispute.

In the litigation in the district court, American Home did not contend that UMG's claims that American Home acted in bad faith

and breached its duty to defend are subject to arbitration. American Home argued only that the discrete dispute over UMG's reimbursement obligation is subject to arbitration. It does not matter that some disputes in a particular case are subject to arbitration while others are not. As this Court has held, even though a particular controversy as a whole may not be subject to arbitration, there may be discrete issues arising in a controversy (here, whether UMG has a reimbursement obligation under the Payment Agreements) that are subject to arbitration, and those discrete issues must be submitted to arbitration even if the entire controversy cannot be. *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 220-21 (1985).

In a brief discussion at the end of its order denying summary judgment in the litigation, the district court denied American Home's motion for a stay of the proceeding pending arbitration. Pet. App. 15a-16a. In so doing, the district court characterized the Payment Agreements as largely concerning "the mode and manner of carrying out UMG's payment obligations under the Policies and the consequences for failing to satisfy those obligations." Pet. App. 16a. The court then concluded that "[t]he mandatory arbitration provision therefore does not extend to disputes, such as the one in the present case, concerning the validity or applicability of ALAE reimbursement obligations." Pet. App. 16a.

American Home appealed the district court's ruling to the Ninth Circuit, arguing once again that the discrete dispute over UMG's reimbursement obligation set forth in the Payment Agreements is subject to mandatory arbitration. American Home also argued that the district court erred in even reaching the question of arbitrability, given that the Arbitration Clause provides expressly that the question of the arbitrability of the dispute was itself for the arbitrators to decide. Pet. App. 25a (stating that the arbitrators "will have exclusive jurisdiction over the entire matter in dispute, including any question as to its arbitrability"). On appeal, the Ninth Circuit affirmed, holding that the district court "properly reached the question of arbitrability" and that the dispute does not "arise out of" the Payment Agreements and, thus, is not arbitrable. Pet. App. 3a. The Ninth Circuit denied American Home's petition for *en banc* rehearing on June 29, 2010, and this petition followed.[11]

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[11] American Home seeks review in this Court only of the Ninth Circuit's ruling that the discrete dispute over UMG's reimbursement obligation under the Payment Agreements does not "arise out of" the Payment Agreements.

REASONS FOR GRANTING THE WRIT

The courts of appeals are intractably divided over the proper construction of the phrase "arising out of" commonly used in arbitration clauses. The Ninth Circuit interprets the phrase restrictively to include only disputes "relating to the interpretation and performance of the contract itself." *Mediterranean Enters., Inc. v. Ssangyong Corp.*, 708 F.2d 1458, 1464 (9th Cir. 1983); *see also Tracer Research Corp. v. Nat'l Envtl. Servs. Co.*, 42 F.3d 1292, 1295 (9th Cir. 1994). Citing *Mediterranean*, the court below applied its restrictive approach here, concluding that the dispute over UMG's reimbursement obligation does not "arise out of" the Payment Agreements because the underlying litigation involves the Policies, and UMG argues that it is excused from its reimbursement obligation because of American Home's alleged breach – thus requiring consideration of more than just the "interpretation and performance" of the Payment Agreements.

Other courts of appeals – specifically the Third, Sixth, Seventh, Eleventh, and, most importantly here, the Second – have expressly rejected the Ninth Circuit's narrow approach and construe the phrase "arising out of" broadly to include a variety of claims involving far more than merely the interpretation or performance of the contract at issue, including related tort

claims. Under the approach taken by other courts of appeals, the outcome in this case would be entirely different.

The Ninth Circuit traces its narrow approach to the Second Circuit's 1961 decision in *In re Kinoshita & Co.*, 287 F.2d 951, 953 (2d Cir. 1961). In the ensuing decades, however, the Second Circuit itself has repudiated *Kinoshita* and limited the decision to its facts. Other courts of appeals have followed suit, expressly rejecting both *Kinoshita* and the Ninth Circuit's adherence to it. Only the Ninth Circuit continues to follow *Kinoshita*.

The resulting conflict among the courts of appeals is acknowledged, longstanding, entrenched, and unlikely to resolve itself absent intervention by this Court. In a series of cases spanning nearly thirty years, the Ninth Circuit has steadfastly adhered to its position, in spite of the criticism of other courts of appeals. Further, the decision of the court below is wrong – among other things, it conflicts with prior precedents of this Court directing a generous reading of arbitration agreements. The issue is likewise an important one, as the phrase "arising out of" is used commonly in innumerable arbitration agreements and should not be subject to varying interpretation based on the circuit in which the question of its meaning is being adjudicated. In addition, this case presents an ideal vehicle to

resolve the conflict among the courts of appeals because the issue is presented squarely and is outcome-determinative. Accordingly, certiorari should be granted.

A. The Ninth Circuit's Narrow Construction of the Phrase "Arising Out of" Deepens an Intractable and Longstanding Circuit Split and Conflicts with this Court's Precedents.

The Ninth Circuit's decision in this case deepens an existing and longstanding conflict among the courts of appeals over the proper construction of the phrase "arising out of" used commonly in arbitration agreements. In this case, UMG's contested reimbursement obligation is set forth in the Payment Agreements, Pet. App. 18a-21a, and the Payment Agreements provide that any dispute "*arising out of* this Agreement" must be submitted to binding arbitration. Pet. App. 23a (emphasis added).

As noted, the Court below held that the dispute over UMG's reimbursement obligation does not "arise out of" the Payment Agreements because the underlying litigation involves UMG's claim that American Home breached the Policies, and UMG contests its reimbursement obligation on the theory that American Home's breach excuses its performance. Accordingly, consideration of the reimbursement dispute

would require more than simply the mere "interpretation" of the Payment Agreements – it would also require consideration of UMG's allegations concerning American Home's alleged breach. Citing its own prior precedent construing the phrase "arising out of" narrowly, the court remarked: "UMG's contention that it might not be obligated to perform in full its duties under the policies if American Home acted in bad faith does not transform those claims into disputes 'arising out of' the payment agreements." Pet. App. 3a (citing *Mediterranean Enters., Inc. v. Ssangyong Corp.*, 708 F.2d 1458, 1464 (9th Cir. 1983)).

The Ninth Circuit stands alone in its narrow construction of the phrase "arising out of," which it has held covers only disputes "relating to the interpretation and performance of the contract itself." *Mediterranean*, 708 F.2d at 1464; *see also Tracer*, 42 F.3d at 1295. The Ninth Circuit has persisted in its restrictive construction of the phrase, *see, e.g., Tracer*, 42 F.3d at 1295, in spite of the fact that other courts of appeals have adopted a far more generous view and have expressly criticized and rejected the Ninth Circuit's approach.

The Ninth Circuit's restrictive approach follows the Second Circuit's early decision in *In re Kinoshita & Co.*, 287 F.2d 951, 953 (2d Cir. 1961). *See Tracer*, 42 F.3d at 1295; *Mediterra-*

nean, 708 F.2d at 1464 (citing *Kinoshita*, 287 F.2d at 953) ("Judge Medina [in *Kinoshita*] concluded that when an arbitration clause 'refers to disputes or controversies under or arising out of the contract,' arbitration is restricted to 'disputes and controversies relating to the interpretation of the contract and matters of performance.'").

Notably, however, the Second Circuit itself has repudiated the reasoning of *Kinoshita* and has limited the decision to its facts. *E.g., ACE Capital Re Overseas Ltd. v. Central United Life Ins. Co.*, 307 F.3d 24, 32-33 (2d Cir. 2002) (Sotomayor, J.) ("*Kinoshita*, which was adopted before the Supreme Court's more recent decisions emphasizing the strong federal policy in favor of arbitration, has frequently been criticized in this Circuit, and no decision of recent vintage mentions the case without confining it to its precise facts."); *Louis Dreyfus Negoce v. Blystad Shipping & Trading, Inc.*, 252 F.3d 218, 225 (2d Cir. 2001) ("We have . . . since limited [*Kinoshita*'s] holding to its facts, declaring that absent further limitation, only the precise language in *Kinoshita* . . . would evince a narrow clause"); *S.A. Mineracao da Trindade-Samitri*, 745 F.2d 190, 194 (2d Cir. 1984) ("We decline to overrule *In re Kinoshita*, despite its inconsistency with federal policy favoring arbitration, particularly in international business disputes, because we are concerned that contracting parties may have (in theory at least) relied on that case in their for-

mulation of an arbitration provision. We see no reason, however, why we may not confine *Kinoshita* to its precise facts."); *St. Paul Fire & Marine Ins. Co. v. Employers Reinsurance Corp.*, 919 F. Supp. 133, 135 (S.D.N.Y. 1996) (noting that in *S.A. Mineracao* and *Genesco*, "the court grappled with *Kinoshita* and left it in tatters. While declining to overrule the case outright, the court confined *Kinoshita* to 'its precise facts' and noted that it was inconsistent with the federal policy favoring arbitration. As a result [of later Second Circuit cases], the authority of *Kinoshita* is highly questionable in this Circuit.") (citations omitted); *cf. Genesco, Inc. v. T. Kakiuchi & Co.*, 815 F.2d 840, 854 n.6 (2d Cir. 1987) ("we recognize . . . that *Kinoshita* is inconsistent with the federal policy favoring arbitration, nevertheless we decline the invitation [to overrule *Kinoshita*]. Because the instant clause is distinguishable from the *Kinoshita* clause, we need not discuss the continued viability of *Kinoshita*.") (citations omitted).

Likewise, other circuits have sharply criticized *Kinoshita* as being out of step with this Court's more recent precedents, particularly the Court's indications that arbitration agreements are favored and that "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." *E.g., Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983); *see also* Mark Berger, *Arbitration and*

Arbitrability: Toward an Expectation Model, 56 BAYLOR L. REV. 753, 772 (2004) ("The development of the presumption of arbitrability in cases after *Kinoshita* . . . led the Second Circuit to restrict the decision to its facts, while courts in other circuits have declined to follow the ruling's narrow approach."). This criticism is longstanding, commencing in 1985 with the Fifth Circuit holding that a district court had erred in relying on *Kinoshita* because, *inter alia*, "*Kinoshita* is inconsistent with federal policy favoring arbitration." *Mar-Len of Louisiana, Inc. v. Parsons-Gilbane*, 773 F.2d 633, 637 (5th Cir. 1985). Since then, the criticism has grown and spread.

In *Sweet Dreams Unlimited, Inc. v. Dial-a-Mattress Int'l, Ltd.*, the Seventh Circuit construed the phrase "arising out of" appearing in an arbitration clause in the context of a rescission action seeking to undo the parties' contract. *See Sweet Dreams*, 1 F.3d 639, 641 (7th Cir. 1993). The Seventh Circuit noted that in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), this Court held that the parties' similar "contractual language [was] easily broad enough to encompass Prima Paint's claim that both execution and acceleration of the . . . agreement were procured by fraud." 1 F.3d at 641 (quoting *Prima Paint*, 388 U.S. at 406) (internal quotation marks omitted). After discussing the arbitration clause at issue in *Prima Paint*, which provided that "[a]ny controversy or

claim *arising out of or relating to* this Agreement, or the breach thereof, shall be settled by arbitration . . . ," the Seventh Circuit reversed the district court's holding that "because the phrase 'relating to' appears in *Prima Paint* but not in the [*Sweet Dreams*] Agreement, the [*Sweet Dreams*] arbitration provision . . . is narrower than that at issue in *Prima Paint*." 1 F.3d at 642.

The Seventh Circuit observed that, in reaching its conclusion, the district court had "relied principally upon *Mediterranean*[], which in turn relied upon *In re Kinoshita*[] . . . ," and also noted that both *Mediterranean* and *Kinoshita* construed "arise under" clauses as encompassing "only those disputes that relate to the interpretation and performance of the contract itself." *Id.*[12] Deliberately departing from *Kinoshita*, the Seventh Circuit interpreted the phrase "arising out of" as "reach[ing] all disputes having their origin or genesis in the contract, *whether or*

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[12] The Seventh Circuit noted that the Ninth Circuit in *Mediterranean* interpreted the phrase "arising hereunder" as synonymous with "arising under," so that for purposes of its analysis, the arbitration provisions in *Mediterranean* ("arising hereunder") and *Kinoshita* ("arising under") were identical. *Sweet Dreams*, 1 F.3d at 624 n.5 (citing *Mediterranean*, 708 F.2d at 1464). As discussed *infra*, the Ninth Circuit later equated the phrase "arising under" with "arising out of." *Tracer*, 42 F.3d at 1295.

not they implicate interpretation or performance of the contract per se." *Id.* (emphasis added).

In reaching its conclusion, the Seventh Circuit explicitly declined to follow "Judge Medina's dicta in *Kinoshita* that suggests an equation between 'arising under' and 'arising out of,'" stating that "our own analysis rejects such an equation." *Id.* Citing *Moses Cone* and the principle that "any doubt concerning the scope of arbitrable issues should be resolved in favor of arbitration," 460 U.S. at 24-25, the Seventh Circuit concluded that the rescission claim was subject to arbitration. 1 F.3d at 642-43.

One year later, the Ninth Circuit reached precisely the opposite result, holding that the "'arising out of' language" in an arbitration clause "is of the same limited scope as the 'arising under' language in *Mediterranean Enterprises*. *See id.* (quoting *In re Kinoshita & Co.*), 287 F.2d 951, 953 (2d Cir. 1961))." *Tracer*, 42 F.3d at 1295. Thus, according to the Ninth Circuit, the phrases "arising out of" and "arising under" are both strictly restricted to matters involving the interpretation or performance of a contract. In contrast, the Seventh Circuit distinguishes the two phrases, concluding that "arising out of" is broader, and includes all disputes involving the contract, not simply those pertaining to enforcement or construction of the agreement itself.

Like the Seventh Circuit, the Eleventh Circuit has also vigorously rejected the Ninth Circuit's adherence to *Kinoshita*. *See H.S. Gregory v. Electro-Mech. Corp.*, 83 F.3d 382, 385-86 (11th Cir. 1996). Construing the phrase "any dispute between any of the Parties *which may arise hereunder,*" the Eleventh Circuit concluded that various tort claims (fraud, fraudulent inducement, deceit, misrepresentation, conversion, breach of good faith and fair dealing, and outrage) fell within the scope of the relevant arbitration clause at issue. *Id.* at 384, 386. The Eleventh Circuit noted that the plaintiffs in the case had relied on *Kinoshita* in drafting their agreement, but that "as early as 1967, the Supreme Court held that a claim of fraud that related to inducement of an agreement is covered by an 'arising out of or relating to the agreement' arbitration clause." *Id.* at 385 (citing *Prima Paint*, 388 U.S. 395 (1967)). Moreover, the Eleventh Circuit observed that in *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974), this Court "required no such additional language to require arbitration of the kind of claims asserted" in *Gregory*. 83 F.3d at 385 (stating that *Scherk* held that arbitration of fraudulent misrepresentation claim was required because the claim 'arose out of' the contract). The Eleventh Circuit added:

> To the extent that the cases binding on this Circuit may have left *Kinoshita* intact, we now reject it simply as not being in accord with present day notions of arbitration as a viable alternative dispute resolution procedure. The Second Circuit itself later recognized that the *Kinoshita* decision was inconsistent with federal policy favoring arbitration but, although obviously aware of the incorrectness of the decision, refused to overrule the case only because lawyers in that circuit may have "relied on the case in their formulation of an arbitration provision." Only the Ninth Circuit seems to have followed the decision in *Kinoshita*. Both the Seventh and the Fifth Circuits have more willingly followed the admonition of the Supreme Court that "[a]ny doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration."

83 F.3d at 385 (citations omitted). The Eleventh Circuit then departed from the Seventh Circuit in *Sweet Dreams* by adding that it had not drawn a distinction between the words "arising under" and "arising out of," and that in *Scherk*, 417 U.S. at 506, this Court "seemed to use 'arise out of' and 'arise under' interchangeably." *Gregory*, 83 F.3d at 386. In other words, although the Seventh Circuit may construe the phrases "arising

out of" and "arising under" differently, the Eleventh Circuit declined to do so. In any event, the Eleventh Circuit clearly construes both "arising out of" and "arising under" more broadly than the Ninth, and has specifically rejected the Ninth Circuit's narrow approach.

In *Battaglia v. McKendry*, the Third Circuit construed the phrase "arises hereunder" to encompass disputes relating to the formation of a settlement agreement, and specifically that the scope of the clause was not limited to disputes involving merely the interpretation and performance of the agreement. 233 F.3d 720, 723-27 (3d Cir. 2000). The Third Circuit rebuffed the plaintiff's reliance on *Kinoshita* and other decisions adopting its reasoning, noting that "this line of cases has been discredited both in the Second Circuit and in other jurisdictions." *Id.* at 725. The Third Circuit continued, "[i]n particular, we decline to follow the Ninth Circuit, which apparently continues to approve the teaching of *Kinoshita*." *Id.* at 727 (citing *Tracer*, 42 F.3d at 1295; *Mediterranean*, 708 F.2d at 1464). Instead, the Third Circuit followed the Eleventh Circuit's decision in *Gregory*, concluding that "when phrases such as 'arising under' and 'arising out of' appear in arbitration provisions, they are normally given broad construction, and are generally construed to encompass claims going to the formation of the underlying agreement." *Battaglia*, 233 F.3d at 727.

In *Highlands Wellmont Health Network, Inc. v. John Deere Health Plan, Inc.*, the Sixth Circuit likewise declined to follow *Kinoshita* when construing the phrase "arising out of" in an arbitration clause. 350 F.3d 568, 577-78 (6th Cir. 2003). After discussing the Second Circuit's negative treatment of *Kinoshita* as well as the Seventh Circuit's decision in *Sweet Dreams*, the Sixth Circuit held that a fraudulent inducement claim fell within the ambit of the arbitration clause at issue. *Id.* ("an arbitration clause requiring arbitration of any dispute arising out of an agreement is 'extremely broad.'") (citation omitted).

It is evident that, under the more generous approach that the Third, Sixth, Seventh, Eleventh (and, in more recent years, Second) Circuits have taken, arbitration of the discrete dispute over UMG's reimbursement obligation would be required as "arising out of" the Payment Agreements. The Payment Agreements specify UMG's obligation, and any dispute over it necessary involves the Payment Agreements directly. Although consideration of UMG's asserted defense to its reimbursement obligation (*e.g.*, whether American Home breached the Policies) requires more than just analysis of the interpretation or performance of the Payment Agreements themselves, that is not materially different from the additional analysis required in *Gregory*,

Battaglia, *Sweet Dreams*, or *Highlands* to resolve the relevant tort and breach of contract claims at issue in those matters. If a dispute involving a "conversion" or "fraud" claim properly "arises out of" a contract, then so does UMG's dispute over its contractual reimbursement obligation. The only reason for the difference in outcome here is the far more restrictive nature of the Ninth Circuit's approach in interpreting the phrase "arising out of."

As the foregoing illustrates, the conflict among the courts of appeals on the proper construction of the phrase "arising out of" is long-standing, developed, and entrenched, justifying this Court's intervention. It is likewise outcome-determinative in this case. In addition, for the reasons offered by the various courts of appeals that have rejected *Kinoshita*, the Ninth Circuit's approach is simply wrong. Certiorari is warranted.

B. The Proper Construction of the Phrase "Arising Out Of" Used Commonly in Arbitration Agreements Is of Vital Importance, and this Case Presents an Ideal Vehicle to Resolve the Conflict Among the Courts of Appeals on this Question.

Parties routinely use the phrase "arising out of" to define the scope of their arbitration

agreements, and competing interpretations of this common phrase among the several courts of appeals serves only to generate unfortunate uncertainty, needless litigation, and improvident cost. Parties rely on what they believe is a correct understanding of the phrase when they draft their arbitration agreements, and that understanding should not be subject to variance depending on the location of the court interpreting their agreement. Certiorari is warranted to establish much-needed uniformity in this area.

In addition, the Ninth Circuit's standard is affirmatively harmful precisely because it is so narrow, denying arbitration where the parties intended it. Further, the Ninth Circuit's standard is subject to abuse, as this case well illustrates. When UMG disputed its reimbursement obligation, American Home sought to have the dispute submitted to arbitration in accordance with the parties' arbitration agreement. By the simple expedient of interposing issues that stray beyond the mere interpretation of the Payment Agreements (*e.g.*, by arguing that it was excused from performance of its reimbursement obligation because of American Home's alleged breach of the Policies), UMG succeeded in defeating arbitration and, in the process, effectively gutted the Arbitration Clause. The effect, of course, is to chart a path of easy evasion for similar cases in the future. This makes no sense and serves only to frustrate arbitration and the policies of

the law that seek to promote it. In addition, the question is likely to recur, and is squarely raised in this instance. Moreover, resolution of the split of authority among the courts of appeals is not likely to be resolved absent intervention by this Court. The Ninth Circuit has reaffirmed its position several times, notably in the *Tracer* decision in 1994 and again in this case, and has denied *en banc* consideration of the matter. Accordingly, certiorari is warranted.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

Susan Koehler Sullivan
Douglas J. Collodel
Michael M. Walsh
SEDGWICK, DETERT,
MORAN & ARNOLD LLP
801 South Figueroa St.,
19th Fl.
Los Angeles, CA 90017
(213) 426-6900

G. Eric Brunstad, Jr.
Counsel of Record
Collin O'Connor Udell
Matthew J. Delude
DECHERT LLP
90 State House Square
Hartford, CT 06103
(860) 524-3999
eric.brunstad@dechert.com

Lawrence Klein
Scott Greenspan
SEDGWICK, DETERT,
MORAN & ARNOLD LLP
125 Broad St., 39th Fl.
New York, NY 10004-2400
(212) 898-4054

Counsel for Petitioner

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