IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

TODD HELLER, SUSAN HELLER, THI SMITH LANE INVESTMENTS, INC. THI PARTNERS, TODD HELLER, INC. ABRAHAM BERNSTEIN, DIANNE G. BERNSTEIN, AB RITTENHOUSE INVESTMENTS LLC, RITTENHOUSE SQUARE PARTNERS, ABD RITTENHOUSE INVESTMENTS, INC., JAMES F. NASUTI, CELESTE NASUTI, JFN WILLIAMSON INVESTMENTS LLC, WILLIAMSON PARTNERS, and JFN WILLIAMSON INVESTORS, INC.	: CIVIL ACTION : : : NO. 04-CV-3571 : : : : : : : :
vs.	:
DEUTSCHE BANK AG, DEUTSCHE BANK SECURITIES, INC., D/B/A DEUTSCHE BANK ALEX BROWN, A DIVISION OF DEUTSCHE BANK SECURITIES, INC., DAVID PARSE, BDO SEIDMAN, L.L.P. ROBERT DUDZINSKY, ELLIOTT P. FOOTER, BEARD MILLER COMPANY, LLP STEVEN D. ORNDORF, WILKINSON AND TANDY LLC, RALPH E. LOVEJOY and KPMG, LLP	: : : : : : : : : : : :

MEMORANDUM AND ORDER

JOYNER, J. **March 17, 2005**

This civil action is once again before this Court for resolution of the Motion of Deutsche Bank AG, Deutsche Bank Securities, Inc. and David Parse (the “Deutsche Bank Defendants”) to Stay the Proceedings. For the reasons discussed below, the motion shall be granted in part and denied in part and the action stayed.

Factual Background

As previously noted, this case arose out of the defendants' marketing and sale of a tax avoidance strategy or "shelter" to the Plaintiffs which was ultimately disallowed by the Internal Revenue Service. The plaintiffs instituted this suit on July 28, 2004 under the theories of civil RICO, 18 U.S.C. §§1962(c) and (d), breach of contract, unjust enrichment, breach of the duty of good faith and fair dealing, breach of fiduciary duty, fraud, negligent misrepresentation, malpractice, civil conspiracy and for declaratory judgment alleging that the defendants knowingly misrepresented and/or failed to disclose that the IRS had issued two notices in 1999 and 2000 informing accountants and tax attorneys across the country that tax strategies such as that being marketed by the defendants were illegal because they lacked a business strategy and economic substance.

The plaintiffs in this case are comprised of three groups of individual investors and the related entities which the individual investors formed for the purpose of entering into the tax strategy, known as "COBRA."[1] Pursuant to the strategy, after

[1] "COBRA" stands for "Currency Options Bring Reward Alternatives." (Plaintiffs' Complaint, ¶45). The COBRA strategy consisted of the following five steps:

First, the Individual Plaintiffs would sell a short option and purchase a long option in almost identical amounts on a foreign currency with different (but narrow) strike prices, each to expire in thirty (30) days. The cost of the long option, though large, would be largely (although not entirely) offset by the premium earned on the sale of the short option. The Individual Plaintiffs would form a single-member limited liability company ("LLC") for the purpose of purchasing the options; Second, the Individual Plaintiffs

forming their respective partnership and limited liability corporate entities, the plaintiffs[2] entered into brokerage account agreements with Deutsche Bank Alex. Brown, LLC, a predecessor of Deutsche Bank Securities, Inc. and through those accounts purchased and transferred the foreign currency options necessary to participate in the COBRA strategy.

By the motion to stay which is now before this Court, the Deutsche Bank defendants contend that, as the account agreements which the Nasuti and Bernstein plaintiffs entered into with them in 2000 contain mandatory arbitration clauses, they are entitled to compel arbitration in this matter. However, because the plaintiffs here are also members of a putative class in the case of Denney, et. al. v. Jenkens & Gilchrist, et. al., No. 03-CV-

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(through the LLCs) would contribute their options to a general partnership formed for the purpose of conducting the COBRA transactions. After 30 days, the long and short options would expire either "in or out of the money," resulting in a gain or loss, depending upon the exchange rate between the U.S. dollar and the relevant foreign currency at the time; Third, the Individual Plaintiffs would make a capital contribution consisting of cash or other capital assets to the partnership; if cash was contributed it was sometimes used to purchase capital or ordinary assets (depending on whether a capital or ordinary loss was being "created"); Fourth, the Individual Plaintiffs would contribute their interests in the partnership to an S Corporation, causing the termination of the partnership as a matter of law; and Fifth, the S Corporation would sell the capital or ordinary assets contributed by the Individual Plaintiffs. These assets would have an artificially inflated basis and their sale would lead to a substantial unrealized short-term capital loss and/or ordinary loss. (Complaint, ¶82).

[2] Specifically the three groups include the "Heller plaintiffs," the "Nasuti plaintiffs" and the "Bernstein plaintiffs." The Heller plaintiffs are Todd Heller, Susan Heller, THI Smith Lane Investments, Inc., THI Partners and Todd Heller, Inc. The Nasuti plaintiffs consist of James F. Nasuti, Celeste Nasuti, JFN Williamson Investments LLC, Williamson Partners and JFN Williamson Investors, Inc. The Bernstein plaintiffs include Abraham Bernstein, Dianne G. Bernstein, AB Rittenhouse Investments, LLC, Rittenhouse Square Partners, and ABD Rittenhouse Investors, Inc.

5460 currently pending in the United States District Court for the Southern District of New York and the arbitration agreements further provide that Deutsche Bank will not seek to compel arbitration during the pendency of a class action, this action should be stayed until such time as class certification has been denied or the plaintiffs here have opted out of the class. Moving Defendants make the same argument with regard to the Heller plaintiffs, although they premise their entitlement to arbitration not upon the account agreements which the Heller plaintiffs entered into with them[3] but upon the arbitration clauses contained in the consulting agreements which those plaintiffs entered into with BDO Seidman, one of the accountant defendants in this action. In this regard, the Deutsche Bank defendants contend that the Heller plaintiffs' claims against them are so closely intertwined with their claims against BDO, that the Heller plaintiffs should be estopped from avoiding arbitration with Deutsche Bank and that considerations of judicial economy strongly militate in favor of resolving all of the plaintiffs' claims against Deutsche Bank at once, rather than on a piecemeal basis.

Discussion

A. Arbitration Under the Federal Arbitration Act

[3] The Heller plaintiffs entered into their account agreements with the Deutsche Bank defendants in 1999, at which time an arbitration clause was not included.

Arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed to so submit. AT &T Technologies, Inc. v. Communications Workers of America, 475 U.S. 643, 648-649, 106 S.Ct. 1415, 1418, 89 L.Ed.2d 648 (1986). It follows that the question of arbitrability is undeniably an issue for judicial determination and thus, unless the parties clearly and unmistakably provide otherwise, the question of whether the parties agreed to arbitrate is to be decided by the court. Id. Principles of contract law govern the inquiry. CTF Hotel Holdings, Inc. v. Marriott International, Inc., 381 F.3d 131, 137 (3d Cir. 2004).

The Federal Arbitration Act, 9 U.S.C. §1, *et. seq.* establishes a strong federal policy favoring arbitration requiring the courts to rigorously enforce agreements to arbitrate; however, due to this strong federal policy, courts need only engage in a "limited review" to ensure that a dispute is arbitrable. Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 226, 107 S.Ct. 2332, 2337, 96 L.Ed.2d 185 (1987); Tripp v. Renaissance Advantage Charter School, Civ. A. No. 02-9366, 2003 U.S. Dist. LEXIS 19834 at *7 (E.D.Pa. Oct. 8, 2003), quoting John Hancock Mut. Life Ins. Co. v. Olick, 151 F.3d 132, 137 (3d Cir. 1998); Great Western Mortgage Corp. v. Peacock, 110 F.3d 222, 228 (3d Cir. 1997). See Also, Green Tree Financial Corp. v. Bazzle, 539 U.S. 444, 452, 123 S.Ct. 2402, 2407, 156

L.Ed.2d 414 (2003). Under the FAA, the district court must be satisfied that the parties entered into a valid arbitration agreement and that the dispute before it falls within the scope of this agreement before compelling arbitration. Great Western, supra.; McAlister v. Sentry Insurance Co., 958 F.2d 550, 553 (3d Cir. 1992). In conducting this inquiry, the district court first decides whether there was an agreement to arbitrate and if so, whether the agreement was valid. Great Western and McAlister, both supra. See Also, Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 24-25, 103 S.Ct. 927, 941, 74 L.Ed.2d 765 (1983). The FAA provides that arbitration agreements are "valid, irrevocable and enforceable save upon such grounds as exist at law or equity for the revocation of any contract." 9 U.S.C. §2; Tripp, 2003 U.S. Dist. LEXIS at *9. Thus, the FAA makes agreements to arbitrate enforceable to the same extent as other contracts. Harris v. Green Tree Financial Corp., 183 F.3d 173, 178 (3d Cir. 1999), citing Seus v. Nuveen & Co., 146 F.3d 175, 178 (3d Cir. 1998). Of course, a federal court must generally look to the relevant state law on the formation of contracts to determine whether there is a valid arbitration agreement under the FAA. Blair v. Scott Specialty Gases, 283 F.3d 595, 603 (3d Cir. 2002). Before concluding that there is a valid contract under Pennsylvania law, the court must "look to (1) whether both parties manifested an intention to be bound by

the agreement; (2) whether the terms of the agreement are sufficiently definite to be enforced and (3) whether there was consideration. Id., quoting ATACS Corp. v. Trans World Communications, Inc., 155 F.3d 659, 666 (3d Cir. 1998). At all times, the court should be mindful that agreements to arbitrate are to be generously construed and that all doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration. Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 62, n.7, 115 S.Ct. 1212, 1218, n.7, 131 L.Ed.2d 76 (1995), citing Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626, 105 S.Ct. 3346, 3353-54, 87 L.Ed.2d 444 (1985).

In applying these principles to this case, we note at the outset that the Nasuti and Bernstein plaintiffs do not dispute that they voluntarily entered into account agreements with Deutsche Bank or that those agreements included an agreement to arbitrate "any controversies which may arise..." The Heller plaintiffs, for their part, likewise do not dispute that the consulting agreement which they executed with BDO Seidman contained a clause which provided for arbitration of "any dispute, controversy or claim [that] arises in connection with the performance or breach of this agreement." Accordingly, as the validity of the arbitration agreements is essentially uncontested, we find the agreements valid.

In determining whether the instant litigation falls within the scope of these arbitration agreements, we look first to the actual language of the clauses which the Moving Defendants seek to enforce. Paragraph 19 of the 2000 account agreements between the Nasuti and Bernstein plaintiffs and Deutsche Bank states in relevant part:

> I understand that: (1) Arbitration is final and binding on the parties. (2) The parties are waiving their right to seek remedies in court, including the right to jury trial. (3) Pre-arbitration discovery is generally more limited than and different from court proceedings. (4) The arbitrators' award is not required to include factual findings or legal reasoning and any party's right to appeal or to seek modification of rulings by the arbitrators is strictly limited. (5) The panel of arbitrators would typically include a minority of arbitrators who were or are affiliated with the securities industry.
>
> I agree to arbitrate with you any controversies which may arise, whether or not based on events occurring prior to the date of this agreement, including any controversy arising out of or relating to any account with you, to the construction, performance or breach of any agreement with you, or to transactions with or through you, only before the New York Stock Exchange or the National Association of Securities Dealers Regulation, Inc., at my election. I agree that I shall make my election by registered mail to you, at P.O. Box 515, Baltimore, MD 21202, Attention Director of Compliance. If my election is not received by you within ten (10) calendar days of receipt of a written request from you that I make an election, then you may elect the forum before which the arbitration shall be held.
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> Neither you nor I waive any right to seek equitable relief pending arbitration. No person shall bring a putative class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class who has not opted out of the class with respect to any claims encompassed by the punitive (sic) class action until (1) the class certification is denied; or (2) the class is decertified; or (3) the customer is

> excluded from the class by the court. Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

Paragraph 8(d) of the Consulting Agreement which the Heller plaintiffs entered into with BDO Seidman provides in pertinent part,

> If any dispute, controversy or claim arises in connection with the performance or breach of this agreement and cannot be resolved by facilitated negotiations (or the parties agree to waive that process) then such dispute, controversy or claim shall be settled by arbitration in accordance with the laws of the State of New York, and the then current Arbitration Rules for Professional Accounting and Related Disputes of the American Arbitration Association ("AAA"), except that no pre-hearing discovery shall be permitted unless specifically authorized by the arbitration panel, and shall take place in the city in which the BDO office providing the relevant Services exists, unless the parties agree to a different locale.

In view of the breadth of both of these clauses[4] and given that agreements to arbitrate are to be generously construed and that all doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, Mastrobuono, supra., we find that the Nasuti and Bernstein plaintiffs would be obligated by paragraph 19 to immediately arbitrate the claims which they raise against the Deutsche Bank defendants here were they not putative class members in Denney v. Jenkens and Gilchrist, and that the Heller plaintiffs are obligated to arbitrate their claims against

[4] The Third Circuit has held that "when phrases such as 'arising under' and 'arising out of' appear in arbitration provisions, they are normally given broad construction." Tripp, 2003 U.S. Dist. LEXIS at *12, quoting Battaglia v. McKendry, 233 F.3d 720, 727 (3d Cir. 2000).

BDO Seidman.

B. Applicability of BDO Arbitration Clause to Hellers' Claims Against Deutsche Bank

We thus next consider whether ¶8(d) in the Heller plaintiffs' consulting agreement with BDO Seidman requires that they arbitrate their claims against Deutsche Bank. In so doing, we note that a few months ago, we were presented with the identical issue which we are asked to decide here in a case involving the same defendants and the same tax avoidance scheme. See, Miron v. BDO Seidman, et. al., 342 F.Supp.2d 324 (E.D.Pa. 2004). Although we briefly revisit the issue, we see no grounds to depart from our reasoning in that case.

There is no dispute that a non-signatory cannot be bound to arbitrate unless it is bound "under traditional principles of contract and agency law" to be akin to a signatory of the underlying agreement. E.I. Dupont de Nemours and Co. v. Rhone Poulenc Fiber and Resin Intermediates, 269 F.3d 187, 194 (3d Cir. 2001), quoting Bel-Ray Co., Inc. v. Chemrite (Pty) Ltd., 181 F.3d 435, 444 (3d Cir. 1999). The theories of third party beneficiary, agency/principal and equitable estoppel are recognized principles of contract or agency law applicable in the arbitration context and are therefore potential grounds to enforce an arbitration clause against a non-signatory. E.I. Dupont, 269 F.3d at 195. See Also, Bouriez v. Carnegie Mellon University, 359 F.3d 292, 294 (3d Cir. 2004)("Generally the

common law theories used to bind a non-signatory to an arbitration clause include third party beneficiary, agency and equitable estoppel.") Additional theories justifying an exception to this general rule include (1) incorporation by reference (2) assumption and (3) veil-piercing/alter ego. See, The Philadelphia Flyers, Inc. v. Trustmark Insurance Company, Civ. A. No. 04-2322, 2004 U.S. Dist. LEXIS 12772 at *9 (E.D.Pa. July 7, 2004); Amkor Technology, Inc. v. Alcatel Business Systems, 278 F.Supp.2d 519, 521 (E.D.Pa. 2003).

In the case at hand, the Deutsche Bank defendants again invoke the estoppel and agency theories. Specifically, they contend that the broad arbitration clause in the Hellers' BDO consulting agreement encompasses their claims against Deutsche Bank because they are "inextricably intertwined with their claims against BDO" and because they have "alleged that all of the Deutsche Bank and BDO Defendants acted in concert and as each others' agents" such that "Plaintiffs cannot separate the Defendants for purposes of avoiding arbitration."

We have previously recognized that the estoppel theory may be appropriately invoked and that a non-signatory has standing to compel arbitration against a signatory "when the issues which the non-signatory wants to resolve are intertwined with the agreement that the signatory signed." Bannett v. Hankin, 331 F.Supp.2d 354, 359 (E.D.Pa. 2004), citing Grigson v. Creative Artists

Agency, L.L.C., 210 F.3d 524 (5th Cir. 2000) and McBro Planning and Dev. Co. V. Triangle Elec. Const. Co., Inc., 741 F.2d 342 (11th Cir. 1984). Specifically, the Third Circuit noted that courts have bound a signatory to arbitrate with a non-signatory "at the non-signatory's insistence because of the close relationship between the entities involved, as well as the relationship of the alleged wrongs to the non-signatory's obligations and duties in the contract ... and the fact that the claims were intimately founded in and intertwined with the underlying contract obligations." Bannett, 331 F.Supp.2d at 360, quoting E.I. Dupont, 269 F.3d at 199-200. In such situations, the courts have considered whether Plaintiffs would have an independent right to recover against the non-signatory defendant even if the contract containing the arbitration clause was void. See, e.g., Massen v. Cliff, Civ. A. No. 02-9282, 2003 U.S. Dist. LEXIS 7392 at *14 (S.D.N.Y. April 25, 2003)(whether plaintiff has any right to commissions under the alleged agreement with [Defendant] is independent of the [agreement and] [e]ven if the [agreement] were found to be invalid or unenforceable, it would not affect plaintiff's right to recover...") In as much as there is nothing in the plaintiffs' complaint or in the record of this matter that even remotely suggests that there is any relationship between the alleged wrongs and the non-signatory's obligations and duties in the contract and as it appears that the plaintiffs

would still have an independent right to recover on their claims against the Deutsche Bank defendants even if the BDO agreement were declared invalid, we cannot find that the Heller plaintiffs' claims against Deutsche Bank are dependent upon or intertwined with the consulting agreement they made with BDO. Accordingly, estoppel under this theory is inappropriate here.

Moreover, as no court in this Circuit has ever found an agency relationship to arise solely as the result of allegations of civil conspiracy, we likewise decline to extend the BDO arbitration clause to compel arbitration against Deutsche Bank on this basis. See, Miron, 342 F.Supp. 2d at 332-333 *citing, inter alia*, Reibstein v. CEDU/Rocky Mt. Academy, Civ. A. No. 00-1781, 2000 U.S. Dist. LEXIS 18206 at *26, 2000 WL 1858718 (E.D.Pa. 2000)(outlining the four types of agency under Pennsylvania law). For these reasons, we deny the Deutsche Bank defendants' motion to compel the Heller plaintiffs to arbitrate their claims against them on the basis of the BDO arbitration clause.

C. Stay of Proceedings

We next consider whether a stay of proceedings is in order in this matter pending arbitration. Under 9 U.S.C. § 3,

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance

> with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

The plain language of §3 affords a district court no discretion to dismiss a case where one of the parties applies for a stay pending arbitration and thus once a district court decides to order arbitration, it is obligated under this section to grant a stay. See, Lloyd v. Hovensa, 369 F.3d 263, 269 (3d Cir. 2004). Stated otherwise, upon application of one of the litigators, a court must stay the trial of the action if it finds that a particular issue is arbitrable under a written agreement. The Basketball Manufacturing Company, Inc. v. Urbanworks Entertainment, Civ. A. No. 04-CV-3179, 2004 U.S. Dist. LEXIS 22966 (E.D.Pa. Nov. 10, 2004).

In this case, however, the contracts which the Nasutis and the Bernsteins signed with Deutsche Bank *precluded* enforcement of the arbitration clause against anyone who is a member of a putative class action *until* class certification was denied, the class is decertified or the customer was excluded from the class by the court. Alternatively, the customer could opt out of the class.[5] Accordingly, it appears that the decision to order a stay

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[5] Again, paragraph 19 of the Bernsteins' and Nasutis' 2000 agreements with Deutsche Bank provides in relevant part:

> Neither you nor I waive any right to seek equitable relief pending arbitration. No person shall bring a putative class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class who has not opted out of the

of proceedings until these conditions have been satisfied falls within our discretion.

In deciding whether to so exercise our discretion we note that the consulting agreement which the Hellers signed with BDO contained no such limitation on arbitration. Hence it is clear that this matter should be stayed as to those parties pending the outcome of the arbitration of the issues between them.[6] We further note that courts have typically granted stays when there are both arbitrable and non-arbitrable claims in the same action and significant overlap exists between the parties and the issues. Miron, 342 F.Supp.2d at 334. Indeed, "the power to stay proceedings is incidental to the power inherent in every court to control the disposition of the causes on its docket." Commonwealth Insurance Co. v. Underwriters, Inc., 846 F.2d 196, 199 (3d Cir. 1988), quoting Landis v. North American Co., 299 U.S. 248, 254, 57 S.Ct. 163, 166, 81 L.Ed. 153 (1936). The decision to stay litigation even among non-arbitrating parties pending the outcome of a related arbitration is one left to the

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> class with respect to any claims encompassed by the punitive (sic) class action until (1) the class certification is denied; or (2) the class is decertified; or (3) the customer is excluded from the class by the court. Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

[6] Although BDO did file a motion to compel arbitration and stay proceedings in this matter, that motion was resolved by stipulation of the parties on January 24, 2005. Thus, the parties agreed to submit the claims in dispute to arbitration and to stay these proceedings.

discretion of the district court. Id., *citing* Moses H. Cone, 460 U.S. at 20, n.23, 103 S.Ct. At 939, n. 23. As in the Miron case, "[b]ecause there is substantial overlap in the charges against these various Defendants, particularly with respect to the RICO and civil conspiracy claims, we elect to stay the entirety of the proceedings pending arbitration of the claims against the BDO Defendants" and/or until such time as the plaintiffs have opted out of the putative Denney class, class certification is denied, the class is decertified or the plaintiffs are excluded from the class by the court. Miron, 324 F.Supp.2d at 334. Accordingly, we shall stay the proceedings herein pursuant to the attached order.

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ORDER

AND NOW, this 17th day of March, 2005, upon consideration of the Motion of Defendants Deutsche Bank AG, Deutsche Bank Securities, Inc. and David Parse (“Deutsche Bank Defendants”) to Stay the Proceedings and Plaintiffs’ Response thereto, it is hereby ORDERED that the Motion is GRANTED for the reasons set forth in the preceding Memorandum Opinion and all further proceedings in this matter before this Court are STAYED

pending completion of arbitration.

BY THE COURT:

s/J. Curtis Joyner
J. CURTIS JOYNER, J.