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NOT TO BE PUBLISHED

Commonwealth of Kentucky

Court of Appeals

NO. 2009-CA-001472-MR

HOUSEHOLD FINANCE CORPORATION II AND
AMERICAN SECURITY INSURANCE COMPANY — APPELLANTS

v.

APPEAL FROM LETCHER CIRCUIT COURT
HONORABLE SAUMEL T. WRIGHT, III, JUDGE
ACTION NO. 08-CI-00420

LEVAN AND MICHELLE KING — APPELLEES

OPINION
REVERSING AND REMANDING

** ** ** ** **

BEFORE: CLAYTON AND KELLER, JUDGES; BUCKINGHAM,[1] SENIOR JUDGE.

BUCKINGHAM, SENIOR JUDGE: Household Finance Corporation II and American Security Insurance Company ("Appellants") appeal from an order of the

[1] Senior Judge David C. Buckingham sitting as Special Judge by assignment of the Chief Justice pursuant to Section 110(5)(b) of the Kentucky Constitution and Kentucky Revised Statutes (KRS) 21.580.

Letcher Circuit Court denying their separate motions to compel arbitration. We reverse and remand.

Appellees Levan and Michelle King entered into a mortgage agreement with Household Finance Corporation II ("HFC") under which HFC agreed to lend them $70,199.37 to refinance a modular home located in Letcher County. Under the provisions of the Loan Agreement, the Kings agreed to maintain property insurance in amounts sufficient to protect HFC's security interest in the home. The Loan Agreement also allowed HFC to procure hazard insurance at the Kings' cost if the Kings did not acquire coverage themselves:

> **Lender's Right to Place Hazard Insurance**
>
> You authorize us, at our option, to obtain hazard insurance coverage on the real property in an amount not greater than the outstanding balance of principal and interest on your loan or, if known to be less, the replacement value of the real property. In the event that you fail to maintain the required hazard insurance outlined above or fail to provide adequate proof of its existence, You authorize us to charge you for the costs of this insurance . . . If at any time after we have obtained this insurance, you provide adequate proof that you have subsequently purchased the required coverage, we will cancel the coverage we obtained and credit any unearned premiums to your loan.

The Kings were unable to secure insurance on the full amount of the loan, but they were able to secure $56,100 coverage through Kentucky Farm Bureau ("KFB"). The Kings claim that HFC subsequently informed them that it had purchased additional insurance to cover the loan amount through American

Security Insurance Company ("ASIC") and that it had begun billing the Kings for this insurance in May 2007.[2]

In April 2008, the Kings' property was completely destroyed in a fire. They filed claims with both KFB and ASIC. KFB offered a check in the full amount of $56,100, while ASIC denied the claim stating that the damage was not covered as there was other valid and collectible insurance. Thereafter, HFC mailed a check for $371.52 to the Kings alleging that it was a return of the premiums paid by them for insurance coverage.

The Kings thereafter filed suit in the Letcher Circuit Court against HFC and ASIC seeking a declaration that they had "valid insurance protection" as a result of their contract with HFC. They also sought a judgment from the court that they had detrimentally relied upon HFC, and they asked for an award of compensatory and "bad faith" damages against either or both HFC and ASIC.

The Loan Agreement also provided that the Kings agreed to abide by the terms of an Arbitration Rider, the terms of which were incorporated into the Loan Agreement. The Arbitration Rider stated as follows:

> [A]ny claim, dispute, or controversy (whether based upon contract; tort, intentional or otherwise; constitution; statute; common law; or equity and whether pre-existing, present or future) . . . arising from or relating to this Agreement or the relationships which result from this

[2] The Appellants claim that the lender-placed policy at issue in Kings' complaint was actually issued by Safeco, not ASIC, but because ASIC communicated the denial of coverage, the Kings mistakenly named ASIC as a defendant. ASIC specifically reserved all defenses before the trial court, including defenses relating to being improperly named as a defendant. For the purposes of seeking to compel arbitration, Appellants addressed the facts alleged by the Kings in the complaint, i.e., that ASIC allegedly issued the lender-placed coverage.

> Agreement . . . shall be resolved, upon the election of you or us by binding arbitration[.]

The Arbitration Rider further provided that "[a]ny participatory arbitration hearing that you attend will take place in the city nearest to your residence where a federal district court is located or at such other location as agreed by the parties." Finally, the Arbitration Rider gave the Kings the right to reject the Rider within 30 days of their signature by written notice. The Kings never objected to the Arbitration Rider.

This Court reviews a trial court's factual findings in an order denying enforcement of an arbitration agreement to determine if the findings are clearly erroneous, but we review a trial court's legal conclusions under a *de novo* standard. *Conseco Fin. Servicing Corp. v. Wilder*, 47 S.W.3d 335, 340 (Ky. App. 2001).

Appellants contend that the Arbitration Rider was a valid arbitration agreement under the Kentucky Uniform Arbitration Act ("KUAA"). Both the United States Congress and the Kentucky General Assembly have enacted legislation to govern certain types of arbitration agreements: the Federal Arbitration Act ("FAA") at 9 U.S.C. § 1 and the KUAA at KRS 417.045-240.[3] Both acts have been found to benefit arbitration agreements, at least to the point of ensuring that arbitration agreements are reviewed using the same criterion that is

[3] The FAA and the KUAA have been construed consistently with each other by Kentucky courts. *Louisville Peterbilt, Inc. v. Cox*, 132 S.W.3d 850, 857 (Ky. 2004) ("we have interpreted the KUAA consistent with the FAA . . ."). Therefore, citation to federal authority has been expressly approved for interpretation of the KUAA because it is "nearly identical" to the provisions of the FAA, and "the outcome is the same" under both state and federal arbitration law. *Id.*

applied to other contracts. *Southland Corp. v. Keating*, 465 U.S. 1, 10, 104 S.Ct. 852, 858, 79 L.Ed.2d 1 (1984); *Kodak Min. Co. v. Carrs Fork Corp.*, 669 S.W.2d 917, 919 (Ky. 1984).

Moreover, because an appeal at the end of the litigation will not often afford an adequate solution to the wrongful denial of a request to arbitrate, both the FAA and the KUAA provide that an appeal may be taken from an interlocutory order denying an application to compel arbitration. 9 U.S.C. § 16; KRS 417.220.

In this case, the Arbitration Rider comes within the broad provisions of the KUAA. The KUAA applies to: "[a] written agreement to submit any existing controversy to arbitration or a provision in [a] written contract to submit to arbitration any controversy thereafter arising between the parties[.]" KRS 417.050. The Arbitration Rider in this case is a written pre-dispute agreement to arbitrate.

The Kings contend that the Arbitration Rider is invalid because KRS 417.050(2) prohibits arbitration clauses in insurance contracts. KRS 417.050(2) provides that the KUAA does not apply to insurance contracts, but the statute notes that arbitration agreements between insurers are not invalid or unenforceable. The trial court agreed with the Kings' reasoning that they are ultimately seeking recovery of insurance proceeds, thus "making the issue . . . a[n] insurance contract."

The Supreme Court of Kentucky has clarified the limited meaning of the term "insurance contract" as used in KRS 417.050(2);

> An insurance policy is a contract of indemnity whereby the insurer agrees to indemnify the insured for any loss resulting from a specific event. The insurer undertakes the obligation based on an evaluation of the market's wide risks and losses. An insurer expects losses, and they are actuarially predicted. The cost of such losses are spread through the market by means of a premium.

Buck Run Baptist Church, Inc. v. Cumberland Sur. Ins., 983 S.W.2d 501, 504-05 (Ky. 1998).

In this case, the contract containing the Arbitration Rider was the Loan Agreement, which is not an "insurance contract" as described by the General Assembly in KRS 417.050(2) or as defined by the Supreme Court in *Buck Run*. The policy behind KRS 417.050(2) was to remove arbitration agreements included in a policy issued to an insured from the coverage of the KUAA. That is not the situation here. An agreement containing a provision mandating that one party obtain insurance does not transform the agreement itself into an agreement for insurance or mean that it provides insurance coverage. Accordingly, the Arbitration Rider is not included within the meaning of an "insurance contract."

Having determined that a valid arbitration agreement under the KUAA exists, the Court must now determine if the claims asserted by the Kings fall within the Arbitration Rider. The use of the phrases "any claim, dispute or controversy" "arising from or relating to this Agreement or the relationships which result from this Agreement" indicates the extensiveness of the Arbitration Rider. Moreover, courts have interpreted the phrase "arising out of or relating to" broadly, "interpreting it to encompass all claims, contractual or tort, which touch upon

matters covered by the agreement." *Hagan v. Greenpoint Credit Corp.*, 2007 WL 2258866 (E.D.Ky. August 3, 2007) (No. 07-17-KKC) at *6 (citing *Orcutt v. Kettering Radiologists, Inc.*, 199 F.Supp.2d 746, 753 (S.D.Ohio 2002)).

The Kings' claims relate to and arise out of the provisions requiring them to maintain insurance in the Loan Agreement, as they could not maintain their claims without reference to the insurance provisions in the Loan Agreement. Therefore, the language of the Arbitration Rider includes Kings' claims.

It is less clear, however, whether ASIC has the right to require arbitration, as ASIC was not a signatory on either the Loan Agreement or the Arbitration Rider. In some circumstances, a non-signatory to an arbitration agreement may both bind, or be bound by, a signatory to the agreement. *Olshan Foundation Repair and Waterproofing v. Otto*, 276 S.W.3d 827, 831 (Ky. App. 2009). In *Olshan*, this Court recognized five ways in which a non-signatory may enforce arbitration agreements: (1) incorporation by reference; (2) assumption; (3) agency; (4) veil piercing/alter ego; (5) estoppel. *Id.* (citing *Javitch v. First Union Securities, Inc.*, 315 F.3d 619, 629 (6th Cir. 2003), *Arnold v. Arnold Corp.*, 920 F.2d 1269, 1281 (6th Cir. 1990), and *Thompson-CSF v. American Arbitration Assoc.*, 64 F.3d 773, 776 (2d Cir. 1995)).

In *Olshan*, the Court upheld an arbitration provision based on an estoppel theory and compelled arbitration involving a non-signatory to the underlying arbitration agreement. The Court found that one cannot receive the

benefits of an agreement while at the same time evading the dispute resolution procedures contained in the same agreement. *Olshan*, 276 S.W.3d at 831-32.

Similarly, where a borrower sued the mortgage lender and the insurer that issued lender-placed coverage, the federal court compelled arbitration under an estoppel theory. *Hagan* at *8 . The Court in *Hagan* noted that equitable estoppel allows non-signatory enforcement of arbitration agreements when (1) "the signatory to a written agreement containing an arbitration clause 'must rely on the terms of the written agreement in asserting [its] claims'" such as when a signatory's claims "'makes reference to' or 'presumes the existence of' the written agreement" or (2) when the signatory alleges "substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract." *Hagan*, 2007 WL 2258866, *8 (quoting *MSDealer Service Corp. v. Franklin*, 177 F.3d 942, 947 (11th Cir. 1999)). "Otherwise, 'the arbitration proceedings [between the two signatories] would be rendered meaningless and the federal policy in favor of arbitration effectively thwarted." *Id.* (citing *MSDealer*, 177 F.3d at 947).

Moreover, other courts have allowed third parties to enforce similar arbitration provisions. *See Sherer v. Green Tree Servicing LLC*, 548 F.3d 379, 382-83 (5th Cir. 2008). The arbitration clause in *Sherer* contained identical language as the clause in this situation, stating that "[a]ll disputes, claims, or controversies arising from or relating to this Agreement or the relationships which

result from this Agreement. . . shall be resolved by binding arbitration." *Id.* at 380. The Court allowed a non-signatory to compel arbitration:

> According to the broad terms of the Loan Agreement, Sherer has agreed to arbitrate any claims arising from 'the relationships which result from th[e] [a]greement.' A loan servicer, such as Green Tree, is just such a "relationship." Indeed, without the Loan Agreement, there would be no loan for Green Tree to service, and no party argues to the contrary. Sherer's . . . claims arise from Green Tree's conduct as Sherer's loan servicer and, therefore, fall within the terms of the Loan Agreement's arbitration clause. Based on the Loan Agreement's language, Sherer has validly agreed to arbitrate with a nonsignatory, such as the loan servicer Green Tree, and the language is sufficiently broad to permit Green Tree to compel arbitration.

Id. at 382.

In this case, the Court's ruling in *Olshan* permits ASIC to enforce the Arbitration Rider under an estoppel theory. Just as in *Olshan*, the Kings are attempting to enforce the Loan Agreement so that HFC will provide hazard insurance coverage, but they also wish to avoid the Arbitration Rider in the same Loan Agreement.

Moreover, the equitable estoppel test set forth in *Hagan* has been met in this situation. Kings' claims arise from and are related to the provisions for lender-placed insurance in the Loan Agreement. Additionally, the Kings have alleged "substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract." *Hagan*, 2007 WL 2258866, *8 (quoting *MSDealer*, 177 F.3d at 947). For example,

The Kings alleged that they made a claim with HFC "by and through" ASIC, that HFC "and/or" ASIC "is liable for the indebtedness owed on the policy, and that "[t]he acts of the Defendants are in violation of the Kentucky Revised Statutes and the Kentucky laws promulgated and are an act of bad faith by their refusing and continuing to refuse to pay the Plaintiffs."

The Kings further argue that the Arbitration Rider was unconscionable. However, this argument was not made to the trial court. Rather, in their response to Appellants' motion to compel arbitration, the Kings simply argued that "[t]he key issue in this matter is an insurance policy." The foundation of appellate review is based on the principle that the lower court has first had a chance to deliberate and decide upon the issues. *Florman v. MEBCO Ltd. Partnership*, 207 S.W.3d 593, 607 (Ky. App. 2006). As stated by this Court:

> The Court of Appeals is one of review and is not to be approached as a second opportunity to be heard as a trial court. An issue not timely raised before the circuit court cannot be considered as a new argument before this Court.

Lawrence v. Risen, 598 S.W.2d 474, 476 (Ky. App. 1980).

Even if we could review this issue, we do not find the Arbitration Rider to be unconscionable. An unconscionable agreement is one which "no [person], not under delusion, would make, on the one hand, and which no fair and honest [person] on the other hand would accept, on the other." *Wilder*, 47 S.W.3d at 342. The doctrine of unconscionability is only used to avoid its terms when the terms are "one sided, oppressive and unfairly surprising contracts." *Id.* at 341.

There is nothing oppressive or unfairly surprising about requiring arbitration in this matter. The Arbitration Rider was clearly-worded and stated in bold face and all caps: **"THE PARTIES HEREBY KNOWINGLY AND VOLUNTARILY WAIVE THEIR RIGHTS TO LITIGATE SUCH CLAIMS IN A COURT BEFORE A JUDGE OR JURY UPON ELECTION OF ARBITRATION BY EITHER PARTY."** The Rider also stated that the Kings could opt out of the arbitration agreement within 30 days after it was signed, which they failed to do. The Kings cannot claim that the Arbitration Rider was unfairly surprising or unconscionable.

The order of the Letcher Circuit Court is reversed and remanded for further proceedings consistent with this opinion.

CLAYTON, JUDGE, CONCURS.

KELLER, JUDGE, CONCURS IN RESULT ONLY.

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