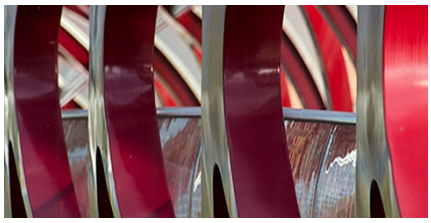
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News & Types: Commercial, Competition & Trade Update

Dilatory and Indecisive Litigant Loses Chance at Arbitration

3/18/2020

Practices: Commercial, Competition & Trade, Corporate, Finance & Acquisitions, Litigation

Executive Summary

When a party is in litigation, but feels it has a right to arbitrate, it can be a difficult decision whether to allow the litigation to continue or to force arbitration. But, as illustrated in a recent 7th Circuit case, the party should make the decision at an early stage and not waver. (*Brickstructures, Inc. v. Coaster Dynamix, Inc.*, 7th Circuit Court of Appeals, No. 19-2187, March 11, 2020)

Brickstructures is a product design firm that creates LEGO sets. Coaster Dynamix creates and sells model roller coasters. The two companies agreed to work together to design a roller coaster kit that would be compatible with LEGOs or other plastic bricks. For this purpose, they entered into a joint venture agreement which Judge Scudder, the author of the 7th Circuit opinion, characterized as "no master class in contract drafting - it was a stock, fill-in-the-blank agreement with spaces for the terms and details to be inserted. Many of those blanks went unfilled." The joint venture agreement contained an arbitration provision that Judge Scudder quoted in full (including the blank lines).

"SECTION TEN: ARBITRATION

> The assignment of specific duties and authority to _____ [C.D.] was made to avoid major differences between the parties as to conduct of the venture. The parties declare that the terms of this agreement are controlling as to each of them. Any matter in dispute, and which is not provided for in this agreement, shall be submitted to arbitration _____ [under the provisions of _____ (cite statute) or as the case may be]."

The companies successfully released an initial product called the Roller-Coaster Factory. But the second product was not successful and was never marketed. Coaster Dynamix eventually, independently, launched the Cyclone, a LEGO-compatible roller coaster kit. Of course, it gave no credit to its former joint venture partner, Brickstructures.

Brickstructures sued, claiming breach of the joint venture agreement, breach of Coaster Dynamix's fiduciary duties to Brickstructures and false advertising. Coaster Dynamix moved to dismiss for reasons other than the arbitration provision. The district court dismissed the original complaint based on a jurisdictional defect (not the arbitration provision).

Undeterred, Brickstructures amended its complaint and added an unjust enrichment claim. Coaster Dynamix again moved to dismiss, alleging there was no binding contract. As an alternative, if the court concluded there

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was a binding contract, Coaster Dynamix moved to dismiss for improper venue based on the arbitration provision.

Days later Coaster Dynamix received a letter from Brickstructures's attorneys. The letter demanded Coaster Dynamix withdraw its motion to dismiss based on personal jurisdiction and arbitration. Brickstructures's attorneys alleged Coaster Dynamix had waived the arbitration provision by not raising it in its first motion to dismiss and even called the arbitration argument "frivolous" and threatened sanctions.

Amazingly, on the same day it received the letter, Coaster Dynamix told the court that it was withdrawing the portion of its motion to dismiss based on personal jurisdiction and arbitration. As Judge Scudder noted, Coaster Dynamix's notice to the court was clear: "Since Coaster Dynamix did not explicitly move on the personal jurisdiction and venue issues in its motion to dismiss the original complaint, Coaster Dynamix withdraws the sections of its pending motion to dismiss based on lack of personal jurisdiction and improper venue." This proved a fatal mistake.

Just a month later, Coaster Dynamix again raised the arbitration when it moved to compel arbitration. Coaster Dynamix claimed there was no ruling on its second motion to dismiss based on the arbitration provision, failing to mention that it had withdrawn that motion. Brickstructures argued that Coaster Dynamix had waived its right to arbitrate.

The district court declined to compel arbitration agreeing that Coaster Dynamix had waived its right to arbitrate. Coaster Dynamix appealed. Writing on behalf of the 7th Circuit Court of Appeals, Judge Scudder affirmed.

Judge Scudder affirmed that federal law favors arbitration. But the right to arbitrate is waivable. The question is whether "based on all the circumstances, the party against whom the waiver is to be enforced has acted inconsistently with the right to arbitrate." Judge Scudder concluded the issue was primarily a factual one, so applied a standard that would affirm the district court unless the district court committed a "clear error", giving a procedural advantage to Brickstructures.

Judge Scudder held, "We find no clear error in the district court's finding that Coaster Dynamix waived its right to arbitrate." After asserting the arbitration provision in its second motion to dismiss, Coaster Dynamix withdrew this argument - "a litigation choice inconsistent with the right to arbitrate." Judge Scudder explained,

> "The withdrawal signaled to Brickstructures and the district court that Coaster Dynamix was content to leave the litigation where it was in federal court. Having put the arbitration card on the table and then taken it back, Coaster Dynamix was not permitted to play that card again later.
>
> As the district court observed, Coaster Dynamix employed a wait-and-see approach—it decided to retract the arbitration issue and roll the dice on its other dismissal arguments before seeking a ruling on the proper venue. Parties seeking to enforce their arbitration rights ought to get to it as soon as possible. Traveling too far down the judicial road before reversing course to restart in an arbitral forum wastes time and resources."

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Judge Scudder agreed with Coaster Dynamix that a party does not necessarily waive the right to arbitrate if a motion to compel arbitration is not the first motion filed. Other filings, like a motion to dismiss or requesting a transfer of venue, can be filed without waiving the right to arbitrate. But Coaster Dynamix went further.

> "By identifying the arbitration argument in its motion to dismiss, the company showed that it knew of its right to arbitrate, and by then expressly withdrawing the argument, it surrendered the right."

Coaster Dynamix had options when it was sued by Brickstructures, including asserting the right to arbitrate. Judge Scudder also said Coaster Dynamix could have conducted its own research to confirm if Brickstructures's sanctions threat was justified, rather than immediately caving. But the choice Coaster Dynamix took, withdrawing the arbitration demand, was fatal to its later demand to assert the arbitration right. By its indecision, Coaster Dynamix lost what it believed to be a valuable contractual right.

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