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DIVISION II
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STATE OF WASHINGTON
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No. 35308-3-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

LARRY NELSON, and the marital community composed of LARRY and BARBARA NELSON

Respondents,

v.

WESTPORT SHIPYARD, INC., a Washington corporation, J. ORIN EDSON, individually and his marital community composed of ORIN and CHARLENE EDSON; DARYL WAKEFIELD, individually, and his marital community composed of DARYL and KIM WAKEFIELD

Appellants.

RESPONDENTS' BRIEF

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I. INTRODUCTION

Larry Nelson, a long-term employee of Westport Shipyard, Inc. since 1983, who worked his way up to Vice-President and Chairman of the Board and minority shareholder, brings this action for (1) violations of Washington's Law Against Discrimination after he was told by new ownership to retire due to his health issues and was forced out, (2) breach of implied contract of employment, (3) wrongful withholding of wages, (4) breach of fiduciary duty and minority shareholder oppression, and (5) tortious interference with business expectancies. CP. 16-29. For these claims, he seeks full recovery for general and special damages, including all actual and compensatory economic damages for lost wages, salary and benefits, and future full stock benefits and fair value.

Also present in the case is a 2004 Shareholders Agreement, which deals with very limited matters under a narrow arbitration clause providing for arbitration only of disputes "arising out of" the Agreement. CP 52. Mr. Nelson also brings a claim for declaratory relief, that the Agreement does not control or limit his claims and damages; and that it is void, invalid, or otherwise unenforceable due to duress, coercion, misrepresentation, failure of consideration, and various breaches. CP 27. As to validity of the arbitration provision, Mr. Nelson filed a demand for trial pursuant to RCW 7.04.040. CP 563.

The trial court ruled here that the arbitration provision is a narrow one, to which Appellants did not assign error, and it is a verity on appeal. Judge McCauley determined that none of Mr. Nelson's claims, enumerated (1) through (5) above, fall within the scope of the Agreement or the narrow arbitration provision. This ruling was also not assigned as error and it is a verity on appeal.

The trial court denied arbitration "at this stage of the litigation" due to the limited scope of the Agreement and the narrow arbitration because, in order to preserve for trial those issues and claims which are clearly not within the scope of the narrow arbitration provision, procedurally the trial of the non-arbitrable claims must go forward first. Otherwise, Appellants could attempt to use the arbitration to restrict or destroy the non-arbitrable claims and measure of damages.[1] The trial court also ruled that enforceability of the Agreement was to be determined by the Court due to the narrow arbitration clause. CP 132, 134.

Instead of timely appealing from the substantive denial of arbitration on the issue of enforceability which was made on November 5, 2005, Appellants engaged in unrestricted, *not limited,* discovery, litigated aggressively for ten (10) months, engaged in extraordinary motions practice, and filed dispositive motions. Having failed to appeal earlier,

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[1] See, VRP (August 8, 2005) at 12:6 to 13:17.

they filed another motion to compel arbitration heard January 3, 2006, and then filed a motion for summary judgment on March 21, 2006, as to the very issue they claim should be arbitrated: enforceability of the Shareholders Agreement. CP 235. On April 10, 2006, they filed another motion to compel arbitration. CP 390. When their summary judgment motion was denied, they then filed an appeal from denial of the third motion to compel arbitration.

It is clear that, contrary to the underlying policy favoring arbitration because it is inexpensive and quick, Appellants' conduct here has greatly delayed and extended the time and increased the cost. Trial would have been held as set on January 17, 2007, but for Appellants' improper delayed notice of appeal. Further, it remains vague as to what issues Appellants seek to have arbitrated. They cannot clearly articulate or frame them so that they do not overlap into issues which are not arbitrable.[2] Arbitration of matters as sought by Appellants, prior to trial, would necessarily include facts or issues which were clearly not within the narrow provision, a problem thoroughly recognized by the trial court. By

[2] Appellants first moved to compel arbitration of all shareholder claims, CP 31, including numerous factual paragraphs of the Complaint and the Fourth and Sixth Causes of Action. Appellants then moved to clarify and compel arbitration of its claims for breach against Mr. Nelson under the 2004 Shareholders Agreement. CP 141. This was also denied because it would necessarily require advancement of defenses by Mr. Nelson which are matters clearly not within the narrow arbitration provision. VRP (Jan. 3, 2006) at 8. Third, appellants moved to compel arbitration on the issue of enforceability of the Shareholders Agreement, including Mr. Nelson's minority shareholder oppression claims or breach of fiduciary duty if advanced as a defense to enforceability. CP 393.

determining to have trial first, the trial court could preserve the non-arbitrable claims and issues that Mr. Nelson rightfully brought before the Court. Arbitration prior to trial would bring in issues, defenses or claims which are not within the narrow provision.

This is precisely what Appellants are attempting to do by way of this appeal. By asserting that this is a simple, straightforward issue – whether the Court or the arbitrator should determine enforceability of the Shareholders Agreement – Appellants are ignoring the inherent authority of the court to control the order of the proceedings before it, the law of the case that this is a *narrow* provision, and the provisions of RCW 7.04.040 requiring trial on the issue. Most significantly, appellants are attempting to untimely force arbitration on a very limited issue in order to bring into that forum many factual issues which underlie the non-arbitrable claims and are not within the narrow arbitration clause. They attempt to misuse arbitration to restrict or destroy non-arbitrable claims and the full compensatory measure of damages.

This Court should dismiss this appeal without reaching the merits because of the failure to timely appeal, and conduct constituting waiver tantamount to forum-shopping. No underlying policy favoring arbitration is present or advanced by permitting this appeal.

On the merits, this Court should uphold the procedural posture that the limited issue for arbitration, i.e. buy-back value of shares, must await the trial of Mr. Nelson's claims. This Court should uphold the determination that the validity of the Agreement is not subject to arbitration.

II. STATEMENT OF ISSUES

1. Whether the appeal is timely when the issue subject to review was determined ten (10) months prior to filing the notice of appeal.

2. Whether Appellants waived any right to seek arbitration as to validity of the Agreement, decided against them on November 5, 2005, by extensively litigating and specifically bringing a summary judgment motion on the very issue claimed to be subject to arbitration, and then filing an appeal when the ruling on summary judgment was adverse.

3. Whether the trial court's decision that it must decide the validity of the Shareholders Agreement, based on the narrow arbitration clause which does not encompass Mr. Nelson's claims, consistent with RCW 7.04.040, and in order to preserve the non-arbitrable claims for trial, should be upheld.

III. STATEMENT OF CASE

A. Factual Background.

Westport Shipyard, Inc., was started by Rick and Randy Rust in 1978 and has been in the business of manufacturing boats ever since.

CP 110. In 1983, Larry Nelson began working for Westport as a laborer on the laminator line. He stayed with Westport for his career, and worked his way up to being a key executive. CP 109. Several times, Mr. Nelson contemplated leaving for other valuable opportunities, but he was promised an ownership opportunity and just cause employment. CP 18. Mr. Edson specifically made numerous representations and promises, which Mr. Nelson later learned to be misrepresentations and deceit. CP 329-332. Based on these representations, Mr. Nelson stayed with Westport, became the Vice President and Chairman of the Board, and in 1998, he purchased shares and became a minority shareholder of this closely held, valuable company. CP 18, 19, 110.

Orin Edson was initially brought into the company by the Rust brothers in 1996 as a one-third (1/3) owner. CP 18. Gradually, Mr. Edson exerted powerful financial control over the other shareholders. CP 19. He drove wedges between the owners, manipulated them to do his will, and used his position of total financial control, as a major shareholder and the sole construction lender and financier, through his company, Pacific Marine Management, to coerce other shareholders to do his bidding. CP 333. Mr. Edson used threats to terminate and destroy their livelihood to force them to vote how he wanted, among other acts of coercion and duress. CP 333-334.

Mr. Edson wanted to make his earlier hire, Daryl Wakefield, a shareholder. CP 111-112. At this point, no one was in a position to refuse his demands. The 2004 Shareholders Agreement was put in place by Mr. Edson. After several years of turmoil and the unjustifiable termination of many key employees, the remaining Rust brother decided to sell his interests to Mr. Edson. CP 19. Despite this difficult situation and unfavorable changes, Mr. Nelson planned and intended to continue with Westport because he had many years left prior to retirement and he loved his work and employees. Mr. Edson had represented and promised that he could work until retirement, that they would grow the company as partners and it would be worth more than book value. CP 331.

On April 29, 2005, during the middle of a business seminar, Mr. Nelson experienced a medical emergency and was transported to the hospital by ambulance. CP 20. Within a few days, Mr. Edson, for the first time, approached Mr. Nelson about forced early retirement. *Id.* Two days later, Mr. Edson faxed Mr. Nelson a letter stating in relevant part that it would be "best" if he "would retire" "considering [his] health problems," "some known, some unknown." *Id.* This letter was a *per se* violation of Washington employment discrimination laws and strong evidence of his general disregard for the rights of others. Shortly thereafter, Mr. Nelson

advised that he did not intend to retire and that he had no medical work restrictions. He continued to work full-time for Westport. *Id.*

The next day, May 18, 2005, Mr. Nelson was told that his "presence is not required nor allowed at Westport Shipyard facilities." CP 20. He was told to leave the premises and that he had until June 16, 2005 to resign under their terms or else he would be fired. *Id.* On May 26, 2005, all Westport employees were informed that Mr. Nelson was no longer working at the company. *Id.*

On June 17, 2005, Mr. Nelson was notified that the Board of Directors had terminated his employment at Westport. This board meeting was not properly noticed, in violation of the corporation's by-laws. CP 21. Mr. Nelson was then informed that Westport would be purchasing his shares pursuant to the 2004 Shareholder Agreement, and advised him of the price that Westport would pay. That amount, however, was not based on the book value as reported by the last audited financial statement, as required under the Agreement. *Id.* Although Appellants claim that the purchase price was "tendered" to Mr. Nelson, there has been no such tender, no unrestricted deposit of any kind.

The 2004 Shareholder Agreement provides, in part, that "upon the termination/resignation of employment; death; or incapacity of any shareholder; the Corporation shall have the option to purchase any or all of

the shares held by the shareholder in the Corporation." CP 45. It also provides that the corporation must pay 1.5 times the book value of the stock as determined in the last audited financial statement. CP 46. The three earlier buy-sell agreements have similar provisions, except the repurchase price is book value. CP 56-66.

The 2004 Shareholder Agreement contains a narrow arbitration clause:

> 6.5 Arbitration. In the event of any disputes among any of the parties *arising out of this Agreement*, then such disputes shall be submitted to arbitration pursuant to the Commercial Arbitration Rules of the American Arbitration Association. . . . .

CP 52 (emphasis added).

B. Procedural Background.

Mr. Nelson filed suit on June 24, 2005. CP 1. An amended complaint was filed on July 15, 2005. CP 16. On August 5, 2005, Mr. Nelson filed a Demand for Jury Trial pursuant to RCW 7.07.040, on the "validity or existence of the arbitration agreement of the 2004 Shareholders Agreement or the failure to comply therewith." CP 563. In his lawsuit, Mr. Nelson brings claims for disability discrimination in violation of Washington's Law Against Discrimination, Chapter 49.60 RCW, breach of implied contract to terminate only for just cause, wrongful withholding of wages, breach of fiduciary duty, minority shareholder oppression, and tortious interference with business expectancies. He also seeks declaratory relief that the Shareholder

Agreement does not control or limit his claims or damages, and that it is void and unenforceable, based on misrepresentations, duress, coercion, failure of consideration and breaches. CP 23-27.

On August 8, 2005, Westport[3] moved to compel arbitration of all shareholder claims, including the Fourth and Sixth Causes of Action and many of the shareholder-related factual allegations in Section III of the Complaint. CP 30. In his letter opinion issued October 31, 2005, Judge McCauley denied Westport's motion to stay litigation and compel arbitration, stating:

> There is no indication that the parties agreed to arbitrate the type of claims set forth in the amended complaint. One cause of action challenges the validity of the Shareholders Agreement. I do not know if the claim has any merit, but I do conclude that such a claim is not covered by the arbitration clause in the Shareholder Agreement.

CP 132. An Order entered on November 10, 2005, states that "it is hereby ordered that at this stage of the litigation, Defendants' Motion is denied." CP 134. On December 6, 2005, Westport filed a motion for "motion for clarification," CP 141, which it acknowledged was a "second motion to compel." VRP (Jan. 3, 2006) 2:6. This motion was also denied. *Id.* at 8.

Westport elected not to appeal the November 2005, or the January 2006 determinations denying arbitration as to enforceability of the Agreement or its claims of breach. Instead, it accepted the Court's

[3] "Westport" is used for the remainder of this brief in lieu of "Appellants," and is intended to apply to all Appellants. If the name of the individual Appellant is material, the individual's name will be used.

decision without appellate challenge, and began to ferociously litigate. It requested relief from the Superior Court in the form of dispositive motions to dismiss claims, motions to compel discovery and production, CP 571, 589, commissions for out-of-state depositions, and even a motion for sanctions. Significantly, on March 3, 2006, Westport filed a motion for summary judgment to dismiss the claim for punitive damages, CP 598-606, which was granted. CP 648. Even more significantly, on March 21, 2006, Westport filed a Motion for Partial Summary Judgment Re Declaratory Relief, seeking a summary determination that the Shareholders Agreement is valid and enforceable, the very claim Westport argues is subject to arbitration. CP 235. This motion was denied on August 9, 2006. CP 501.

On July 7, 2006, Westport filed a motion to Enforce Protective Order and for Sanctions, CP 650-651, which was denied on August 10, 2006. CP 655. In June, 2006, Westport requested and received commissions for four out-of-state depositions, CP 622-637; and took the depositions of David Jones, Richard Holiber, Rick Rust, part of Randy Rust, and full and lengthy depositions of both Mr. and Mrs. Nelson. CP 343. Westport also filed a response to plaintiff's note for trial, CP 614, requesting trial as soon as possible, which resulted in an early setting by the court for January 17, 2007. CP 621.

Westport filed yet another motion to compel arbitration on April 10, 2006. CP 390. This motion as well was denied through a memorandum opinion issued July 21, 2006. CP 498. The trial court simply reiterated "[i]n the present case, I ruled that the arbitration clause is narrow, and the parties did not agree to arbitrate the validity of the Shareholders Agreement." *Id.* An Order, again denying Westport's motion to compel arbitration was entered on August 10, 2006. CP 503. Westport then filed a notice of appeal from the denial of arbitration on September 1, 2006 – over ten (10) months after the trial court's October 31, 2005 ruling and seven (7) months after the trial court's January 3, 2006 ruling. CP 506.

IV. ARGUMENT AND AUTHORITY

By way of summary of argument, Westport failed to timely appeal the Superior Court's determination denying arbitration within thirty (30) days; and instead elected to avail itself of the benefits and protections afforded by the judicial system, proceeding to fully and aggressively litigate, engage in discovery, and filing discovery and substantive, dispositive motions. Because Westport waived any right of appeal as to whether arbitration should await trial, this Court should dismiss this appeal before reaching the merits.

If this Court does reach the merits, the decisions of the Honorable Mark McCauley denying Westport's motion to compel arbitration should

be affirmed. The determination by the trial court that the arbitration clause is *narrow* has not been assigned as error on appeal. The *narrow* arbitration clause, even if valid, does not cover the multitude of claims asserted by Mr. Nelson, or the underlying facts upon which those claims are based. Moreover, the validity of the Shareholders Agreement is for the court to determine due to the narrow arbitration clause, and RCW 7.07.040. Last, the trial court's control of the order of proceedings, determining that trial should be held first so as to preserve the non-arbitrable claims and issues for trial, should be upheld. For these reasons, the decision below should be affirmed and this matter remanded for trial.

A. Westport Failed To File A Timely Notice Of Appeal.

This appeal should be dismissed as untimely because Westport forfeited any right of appeal from the denial of its motion to compel arbitration as to enforceability of the Agreement when it failed to timely appeal from either the November, 2005, or the January 3, 2006, orders denying arbitration. Instead, it engaged in extensive discovery, motion practice, and submitted two motions for partial summary judgment, including a partial summary judgment motion addressing the issues it claims are subject to arbitration. CP 235. Westport waited until the trial court rejected its partial summary judgment motion to file this appeal. Thus, it has forfeited the right of immediate appeal on the issue of arbitration of the validity of the Shareholders Agreement.

The time for filing a Notice of Appeal is a jurisdictional step. *Mallot v. Randall,* 8 Wn. App. 418, 506 P.2d 1296 (1973). The appeal must be perfected in the manner and time required by this rule for the appellate court to have jurisdiction. The deadlines for filing an appeal are strictly construed. RAP 18.8. While Washington's appellate courts are generally permitted to adjust most deadlines to decide cases on their merits, the deadline for filing a notice of appeal is not subject to adjustment unless there are "extraordinary circumstances." RAP 18.8. Specifically, RAP 18.8(b) provides:

> (b) Restriction on Extension of Time. The appellate court will only in extraordinary circumstances and to prevent a gross miscarriage of justice extend the time within which a party must file a notice of appeal, a notice for discretionary review, a motion for discretionary review of a decision of the Court of Appeals, a petition for review, or a motion for reconsideration. The appellate court will ordinarily hold that the desirability of finality of decisions outweighs the privilege of a litigant to obtain an extension of time under this section.

(Emphasis added). In *Beckman v. DSHS*, 102 Wn. App. 687, 690, 11 P.3d 313 (2000), the defendant filed its notice of appeal from a 17.76 million dollar jury verdict 10 days late, and the plaintiff moved to dismiss because the notice of appeal was not timely. This Court dismissed, reasoning, "[i]n contrast to the liberal application we generally give the Rules of Appellate Procedure (RAP), RAP 18.8 expressly requires a narrow application[.]" 102 Wn. App. at 693.

Here, Westport's right of immediate appeal is lost by expiration of the time prescribed in the rule. After the expiration of the time to appeal from either the November, 2005, or the January 3, 2006, orders, Westport hired new counsel. The third motion to compel arbitration appears to be a strategy to try to create a new right of immediate appeal devised once the new attorneys were retained – an attempt to go through the back door to correct the prior failure to timely appeal.

This Court must look at when the trial court made its ruling on the *substantive* issue that enforceability of the Agreement is not subject as to arbitration. This substantive issue was decided when the Court denied the July, 2005, motion to compel arbitration, by order in November, 2005, and not when the third, later motion as to the same issue was filed and denied almost a year later.

To allow Westport to circumvent the deadline for filing its appeal would render the 30-day filing deadline meaningless. This is not what the case law permitting immediate appeal of a denial of arbitration contemplates. Moreover, this would permit a party to essentially forum shop, which Westport has done here, to litigate until the proceedings head in a negative direction.

In Washington, an order denying arbitration must be immediately appealed, because the denial of such motion terminates the action for arbitration, and the benefits of arbitration are irretrievably lost without an

immediate appeal. *Herzog v. Foster & Marshall,* 56 Wn.2d 437, 440, 443, 783 P.2d 1124 (1989); *Stein v. Geonerco, Inc.,* 105 Wn. App. 41, 44, 17 P.3d 1266 (2001). The reason for the immediate appeal is to prevent the delays, costs and expenses of extended judicial proceedings from defeating the savings associated with arbitration. Indeed, the policy behind arbitration is to avoid the formalities, expenses and delays inherent in the court system. *Mendez v. Palm Harbor Homes,* 111 Wn. App. 446, 455, 45 P.3d 594 (2002); *Perez v. Mid-Century Ins. Co.,* 85 Wn. App. 760, 765-66, 934 P.2d 731 (1997).

Here, however, Westport did not immediately appeal and instead, fully engaged in extensive discovery, discovery motions, and substantive motions to dismiss claims and to seek sanctions. The principal reason for the rule permitting immediate appeal simply does not exist here, and is rendered meaningless if such repeated motions and open-ended appeal rights throughout the litigation were allowed.

1. The language, "at this stage of the litigation," does not support or excuse the substantial delay in filing for immediate appellate review.

In response to Westport's first motion to compel arbitration on July 27, 2005, Judge McCauley's opinion letter and Order stated that "at this stage of the litigation," the motion to compel is denied. CP 134. This language was included because the court recognized that arbitration may become appropriate after trial of the non-arbitrable claims and issues; and

if the non-arbitrable claims and issues were decided at trial against Mr. Nelson, at that point, then the limited issue of book value and buy-back of the shares would be ripe and subject to arbitration.

The transcripts from both the August 8, 2005, and the January 3, 2006 hearings make this clear. Judge McCauley was exercising the court's proper authority to control the order of proceedings before it, to preserve the non-arbitrable claims of Mr. Nelson for trial. The court was well aware of the potential that arbitration on the limited issue of buy-back and share value would necessarily bring in some underlying factual issues which were not subject to arbitration, and that Westport would or could use arbitration to try to restrict or destroy Mr. Nelson's other claims and damages measures. VRP (Aug. 8, 2005) 12:6 to 13:17. This point was also made clear during the January 3, 2006 hearing on the motion for "clarification" that it was not proper to have certain issues before an arbitrator which would necessarily require evidence and decisions on the non-arbitrable claims. VRP (Jan. 3, 2006) at 8:14-9:20.

Judge McCauley was only indicating with the language, "at this stage in the litigation," that if it is determined, by the court or jury, that the Shareholder Agreement is enforceable, and/or that Mr. Nelson was lawfully terminated, then the provision in the Shareholder Agreement regarding the value of the stock and buy-back would be ripe for arbitration, and the motion could be renewed at that point.

This is clearly what was intended by the language, "at this stage of the litigation" in the letter decision, which was hand-written in the Order to be consistent with the opinion, not to give it undue emphasis. There was no change in *the stage of the litigation* between the first order denying arbitration in November, 2005, and the third motion to compel filed April 10, 2006, because not even one of the non-arbitrable issues had been decided. To hold that Judge McCauley intended Westport to be able to file motions to compel arbitration at any time, as Westport now argues, would be ludicrous. There had to be a change in the stage of the litigation, which under the circumstances and in the context of the trial court's remarks on the record, can only mean after decision or trial on the underlying non-arbitrable issues. Nothing substantive had changed as of April, 2006 – the underlying claims and issues which were not arbitrable had not been decided in whole or in part. There was no change so as to justify the renewed request for arbitration or that it was procedurally permissible in accordance with Judge McCauley's earlier orders denying arbitration.

Westport cannot claim that the *stage of the litigation* had changed which would permit yet another motion to compel arbitration on the same basis. All of the non-arbitrable issues were still in the case at the time the third motion to compel was filed and decided. At the same time that Westport asked the Court to make a decision on the merits as to the

validity of the Agreement, it was also asking the Court to order arbitration of that issue. Had Westport won dismissal of the claim challenging the validity of the agreement on its summary judgment motion, it follows that Westport would not have appealed the denial of its April, 2006, arbitration motion. This conduct by Westport is strategic misuse of the judicial system and forum-shopping. This must not be permitted by this Court, and would be directly contrary to the underlying policy and purpose of arbitration.

2. The decision of *Buckeye Check Cashing Inc. v. Cardegna* does not justify a renewed motion, or the delay in filing the notice of appeal.

In an effort to come up with an explanation to justify its third motion to compel arbitration, which was designed to re-create a right of immediate appeal, Westport also claims that the decision of *Buckeye Check Cashing Inc. v. Cardegna*, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d. 1038 (Feb. 21, 2006), altered the legal landscape regarding the enforceability of arbitration agreements. However, Westport's argument overstates the significance of the *Buckeye* decision and ignores its inapplicability to the facts of this case. As noted by Judge McCauley, the *Buckeye* decision did not alter the law, and is not pertinent to the arbitration clause at issue in this case.

Unlike this case, the *Buckeye* case, a class action, involved very broad arbitration clauses not like the narrow one here, and specifically

provided that disputes as to the validity, enforceability or scope of the arbitration clause shall be resolved by binding arbitration. There, the arbitration clause provided, in relevant part, that:

> 1. *Arbitration Disclosure.* By signing this Agreement, you agree that if a dispute **of any kind** arises out of this Agreement or your application therefore or any instrument **relating thereto**, then either you or we or third-parties involved can choose to have that dispute resolved by binding arbitration as set forth in Paragraph 2 below . . . .
>
> 2. *Arbitration Provisions.* **Any claim, dispute, or controversy . . . arising from or relating to this Agreement . . . or the validity, enforceability, or scope of this Arbitration Provision or the entire Agreement** (collectively 'Claim'), shall be resolved, upon the election of you or us or said third-parties, by binding arbitration . . . . This arbitration Agreement is made pursuant to a transaction involving interstate commerce, and shall be governed by the Federal Arbitration Act ('FAA'), 9 U.S.C. Sections 1-16. The arbitrator shall apply applicable substantive law constraint *[sic]* with the FAA and applicable statutes of limitations and shall honor claims of privilege recognized by law . . . .

Buckeye, 126 S. Ct. at 1207 (emphasis added in bold).

The contract in *Buckeye* is much different than the arbitration clause in this case. The *Buckeye* agreement specifically required that the arbitrator decide questions about the scope, validity and enforceability of the agreement. The arbitration agreement in this case does not include such broad language. Thus, Judge McCauley's decision correctly distinguished *Buckeye,* and the case did not provide a basis for filing yet another motion to compel arbitration.

Westport's argument that *Buckeye* justified the third motion to compel arbitration or rendered it an independent motion from which it could appeal is unfounded. And, the notion advanced in *Buckeye* was already made by Westport in its first and second motions, and was supported by prior case law. The basis of the trial court's denials to compel arbitration was the very limited scope of the arbitration clause and its determination that the issue of validity had to be first decided by the court or jury due to the narrow scope of the arbitration clause and the limited matters covered in the Agreement.

Because the law on this issue is firmly established, *Davis v. Chevy Chase Financial*, 667 F.2d 160 (D.C. Cir. 1981),[4] and *Buckeye* does not even address the question here, the *Buckeye* decision was not a change in the "stage of the litigation" in order to supply the grounds for Westport to file yet a third motion to compel arbitration.

Generally, it is improper for a party to re-submit the same motion that has already been decided. *See Raymond v. Ingram*, 47 Wn. App. 781, 784, 737 P.2d 314 (1987). Likewise, it should be improper for a party to engage in gamesmanship by filing the same motion on a substantive issue decided ten (10) months earlier in order to manufacture an order from which it could then argue it filed a timely appeal from. For these reasons, this appeal should be dismissed.

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[4] This factually similar case is discussed in detail below.

B. Westport Waived Arbitration By Seeking Relief From The Superior Court Before Appealing The Question Of Arbitration.

In addition to forfeiting the right of immediate appeal as argued above, Westport's conduct in the litigation subsequent to entry of the November, 2005, order denying arbitration, *without filing an appeal,* constitutes a waiver of any claimed right to arbitrate the substantive issues which were ruled upon by the Court. If Westport wanted to preserve its right to seek arbitration of the enforceability of the Agreement or its claims against Mr. Nelson, it had to file an appeal following the November 2005, Order, when these decision were made. At the very least, it had to file an appeal following the January 3, 2006, Order, denying the motion to compel again, specifically addressing and denying arbitration of Westport's potential claims against Mr. Nelson.

Instead of preserving its right to seek arbitration, Westport participated in the litigation through extensive discovery and even brought an affirmative motion for partial summary judgment on the very issue that it claimed was subject to arbitration. CP 235. Under such circumstances, Westport has engaged in conduct in the litigation, without filing a timely appeal from the outset, which is inconsistent with any claimed right to arbitration on that issue.[5] A party waives the right to seek arbitration by

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[5] Under the restrictive language of the 2004 Shareholders Agreement, even if valid and enforceable, the only issue an arbitrator could decide under the agreement would be the value of the shares; and the arbitrator could not determine any of the other multitude of underlying facts or issues in the litigation. Westport has engaged in discovery and a substantive motion for summary judgment on the issue of enforceability of the agreement

participating in legal action involving the substance of the issue. *Naches Valley School District v. Cruzen,* 54 Wn. App 388, 775 P.2d 960 (1989) (motion for summary judgment on liability indicated intent to proceed with the action rather than seek arbitration); *Kinsey v. Bradley,* 53 Wn. App. 167, 765 P.2d 1329 (1989) (party engaged in extensive motion practice to dismiss claims without seeking arbitration).

By proceeding extensively in the litigation without filing a notice of appeal, and then specifically filing a motion for partial summary judgment on the very claim it asserts is subject to arbitration, Westport indicated its intent to proceed with the action, and waived its right to claim arbitration as to the enforceability of the Agreement or the issue that the clause was *narrow* and did not encompass the claims asserted by Mr. Nelson. *Lake Washington School Dist. v. Mobile Modules,* 28 Wn. App. 59, 61, 621 P.2d 791 (1980). The reasons our courts permit immediate appeal from a denial of a motion to compel arbitration were succinctly stated by the *Herzog* Court as follows:

> If a court refuses to stay litigation pending arbitration, the party seeking to enforce arbitration will suffer the serious, irreparable consequence of being forced to resolve the dispute by costly and lengthy litigation rather than by arbitration. The benefits of arbitration will thus be irretrievably lost. Such a result not only runs counter to the parties' agreement to arbitrate, but, more importantly, it frustrates the strong public policy in this state favoring arbitration of disputes.

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without filing an appeal of the initial denial of arbitration, and thus, Westport waived any arbitration as to that issue.

Herzog v. Foster & Marshall, 56 Wn. App. 437, 443, 783 P.2d 1124 (1989). Thus, a party has the right to an immediate appeal if the motion for arbitration is denied *provided* the party appeals with thirty days. RAP 5.2(a). On the other hand, if a party, as here, elects to forgo filing an appeal and instead litigates the dispute in a judicial forum, none of the reasons which support the policy for an immediate appeal exist.

Westport cannot voluntarily avail itself of the judicial forum and then seek arbitration only when the litigation goes in an unfavorable path. These tactics should not be condoned by the court, and this appeal should be dismissed as waived.

C. The Superior Court Correctly Denied Westport's Motion To Compel Arbitration.

The scope of the arbitration clause, even if valid and enforceable, is limited and narrow, as ruled by the trial court. Westport has not challenged this ruling in its assignments of error. It only challenges and assigns error to the trial court's decision that whether the Agreement is valid or enforceable is for the court to determine.

Contrary to the assertions made by Westport, Mr. Nelson's claims arise from events which occurred beginning in 1998, his long-term employment, his long-term purchasing of company stock, the statements, actions and conduct which started in 1998 and continued up to and through the time of the December 2004 Shareholders Agreement, the representations and promises made to him, his purchase of stock and

investment of time, money and resources in the company, the misrepresentations and omissions toward him as a minority shareholder, the threats and breaches of fiduciary duty owing to him, and the like – many of which even occurred prior to the Agreement and none of which are dependent upon it or arise from it. CP 16-29. Because Mr. Nelson did not waive his inviolate right to jury trial by virtue of such a narrow, limited arbitration clause, he cannot be required to submit to arbitration on the claims asserted in this lawsuit. The Superior Court agreed, reasoning:

> There is no indication that the parties agreed to arbitrate the type of claims set forth in the amended complaint. One cause of action challenges the validity of the Shareholders Agreement. I do not know if the claim has any merit, but I do conclude that such a claim is not covered by the arbitration clause in the Shareholder Agreement.

CP 132.

The decision of the trial court is correct for multiple reasons. First, even assuming that the 2004 Shareholders Agreement is enforceable, which Mr. Nelson disputes, the scope of the arbitration clause is narrow and does not encompass the claims asserted by Mr. Nelson. The scope of the clause must first be decided by the Court, as Appellants acknowledge and concede. The arbitration provision here is a narrow clause, restricted to the limited matters in the Agreement which cannot be expanded as a matter of contract law. The claims asserted by Mr. Nelson exist independently of the Agreement, and do not *arise* from it – rather they are

claims for minority shareholder oppression, misrepresentation, tortious interference, breach of fiduciary duty and other tort, common law or statutory shareholder claims. None of these claims are dependent upon the Agreement, and are not controlled by it or the arbitration clause in it.

Second, a court must determine whether the Shareholders Agreement, including the arbitration agreement, is void or unenforceable, applying contract principles of formation and enforceability of contracts, unless the arbitration clause indicates that these decisions are for the arbitrator. Such declaratory relief has been pleaded and requested by Mr. Nelson in the Complaint and Amended Complaint, and must be determined by the Court. CP 1-29. And, Mr. Nelson filed a demand for jury trial and complied with the Washington Arbitration Act which requires that the issue of validity of the arbitration provision be submitted for trial. RCW 7.04.040. This issue is discussed separately below in Section D.

As explained in more detail below, Judge McCauley correctly concluded that the arbitration clause is narrow, and that the claims asserted are not within the scope of the narrow arbitration clause. The trial court also correctly concluded that the court must first determine whether the Shareholder Agreement controls the claims, issues and damage claims of Mr. Nelson, or if it is otherwise void, invalid or unenforceable, because these were not issues that the parties agreed to arbitrate in the arbitration

clause. For those multiple reasons, this Court should affirm the trial court's decision.

1. The arbitration clause found in the 2004 Shareholder Agreement does not cover these claims.

The arbitration clause states: "In the event of any disputes among any of the parties *arising out of this Agreement*, then such disputes shall be submitted to arbitration . . . ." CP 52 (emphasis added). Contrary to Westport's assertion, this is construed to be a *narrow* clause under the case law, not a broad one, and is restricted and limited to claims or disputes which actually arise from the Agreement. That the clause here is narrow has not been assigned as error, and is a verity on appeal. *State v. Luther*, 157 Wn.2d 63, 78, 134 P.3d 205 (2006); *Robel v. Roundup Corp.*, 148 Wn.2d 35, 42, 59 P.3d 611 (2002). Because the scope of the arbitration clause is *narrow*, the collateral matters, which Westport seeks to force into arbitration, are far beyond its purview.

Arbitration is a contractual remedy, freely bargained for,[6] that provides extrajudicial means for resolving disputes. *Thorgaard Plumbing & Heating Co. v. County of King,* 71 Wn.2d 126, 131, 426 P.2d 828 (1967). The "first task of a court asked to compel arbitration of a dispute is to determine whether the parties agreed to arbitrate that dispute."

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[6] Mr. Nelson contends that the arbitration clause of the Shareholders Agreement, and the Agreement itself, were not freely bargained for, and that they are both void and unenforceable. But for purposes of this analysis as to scope of the arbitration clause, it is assumed that the Agreement and clause are valid.

Kamaya v. American Property Consultants, 91 Wn. App. 703, 712 (1998); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985). The scope or arbitrability of a dispute is controlled by the language of the contract and is to be determined by the Court.[7] Where the parties dispute whether an arbitration clause applies to a particular type of controversy, the question is for the Court. *Howsam v. Dean Witter Reynolds, Inc.,* 537 U.S. 79, 83 (2002). In *Howsam*, the Supreme Court held:

> This Court has determined that "arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit." *Steelworkers v. Warrior & Gulf Nav. Co.*, 363 U.S. 574, 582, 4 L. Ed. 2d 1409, 80 S. Ct. 1347 (1960); see also *First Options*, 514 U.S. at 942-943. Although the Court has also long recognized and enforced a "liberal federal policy favoring arbitration agreements," *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25, 74 L. Ed. 2d 765, 103 S. Ct. 927 (1983), it has made clear that there is an exception to this policy: The question whether the parties have submitted a particular dispute to arbitration, i.e., the "question of arbitrability," is "an issue for judicial determination unless the parties clearly and unmistakably provide otherwise." *AT&T Technologies, Inc. v. Communications Workers*, 475 U.S. 643, 649, 89 L. Ed. 2d 648, 106 S. Ct. 1415 (1986) (emphasis added).

Id. Decisions issued after *Buckeye* affirm this black letter law. *Goodrich Cargo Sys. v. Aero Union Corp.*, 2006 U.S. Dist. LEXIS 93680 (D. Cal.

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[7]Under both state and federal case law, when determining whether the parties have agreed to arbitrate a particular issue, the Court must apply ordinary state-law principles that govern the formation and validity of contracts. *First Options of Chicago Inc. v. Kaplan,* 514 U.S. 938, 944 (1995). In Washington, this includes the application of the context rule. *Tjart v. Smith Barney, Inc.,* 107 Wn. App. 885, 895, 28 P.3d 823 (2001) *rev. denied*, 145 Wn.2d 1027 (2002).

December 14, 2006) (holding "a federal court must review the contract at issue to determine whether the parties have each agreed to submit a particular dispute to arbitration."); *Slatnick v. Deutsche Bank AG,* 2006 U.S. Dist. LEXIS 94836 (D. Cal. March 15, 2006) (holding that courts are only to "compel arbitration if the court is satisfied the claim at issue falls within the scope of a valid, enforceable agreement among the parties to arbitrate the claim.").

Contract law principles control over the broad public policy preference for upholding alternative dispute resolution. Despite the public policy of state and federal courts favoring arbitration, "it will not be invoked to resolve disputes that the parties have not agreed to arbitrate." *King County v. Boeing Co.,* 18 Wn. App. 595, 602-03, 570 P.2d 713 (1977). Indeed, the Court must first look to the language of the contract to determine whether the parties actually agreed to arbitrate a particular dispute, and not to general policy preferences. *EEOC v. Waffle House, Inc.,* 534 U.S. 279, 294 (2002). "Arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit." *AT & T Techs., Inc. v. Communications Workers of America,* 475 U.S. 643, 648 (1986); *United Steelworkers v. Warrior & Gulf Navigation Co.,* 363 U.S. 574, 582 (1960).

Likewise, under state law, in *Godfrey v. Hartford Cas. Ins. Co.,* 142 Wn.2d 885, 894, 16 P.3d 617 (2001), the Court emphasized that the

"parties are free to decide if they want to arbitrate" and by "their agreement to arbitrate, the parties may control the issues to be arbitrated."

As we noted in *Price*, the reasons for this rule are as follows:

> "(a) that parties are free to decide whether they wish to use arbitration in lieu of the judicial process, (b) that they may agree on what matters they wish to submit to an arbitrator, (c) that a party is only required to arbitrate those matters which are the subject of such an arbitration agreement, . . ."
>
> While the parties are free to decide by contract whether to arbitrate, and which issues are submitted to arbitration, once an issue is submitted to arbitration, however, Washington's Act applies.

Id. (emphasis added.).

In determining whether parties intended to submit a particular dispute to arbitration, the Court must consider four guiding principles:

> (1) the duty to submit to arbitration must arise from the contract itself; (2) the question whether the parties agreed to arbitrate a particular dispute is for the court, unless the parties clearly provide otherwise; (3) the court should not determine the underlying merits of a dispute in determining the arbitrability of an issue; and (4) the courts favor arbitration of disputes.

W.A. Botting Plumbing & Heating Co. v. Constructors-Pamco, 47 Wn. App. 681, 683, 736 P.2d 1100 (1987) (emphasis added); *Mendez v. Palm Harbor Homes, Inc.*, 111 Wn. App. 446, 455-56, 45 P.3d 594 (2002).

Here, Westport erroneously asserts that the claims raised in this action *arise* under the 2004 Shareholder Agreement or to the extent they may not, they are nevertheless related or so intertwined that they should be

sent to arbitration due to the public policy favoring arbitration of disputes. However, as a matter of contract and case law, Westport is wrong.

a. The arbitration clause at issue is "narrow."

The arbitration clause on its face here only applies to disputes "arising out of this Agreement." CP at 52. This is a narrow clause, and it is restricted to only those disputes which are included or "arise out" of "this" Agreement. The courts have recognized that there is a wide range in the language and breadth of arbitration clauses, and therefore, the reviewing court must first look to the clause itself to determine whether it is *broad* or *narrow*. To properly consider the scope of a clause, the court must distinguish between "narrow" and "broad" arbitration clauses, because the type of clause will determine the extent of matters which can be held to be arbitrable. *Tracer Research Corp. v. National Envtl. Svcs. Co.*, 42 F.3d 1292, 1295 (9th Cir. 1994); *Louis Dreyfus Negoce S.A. v. Blystad Shipping & Trading Inc.*, 252 F.3d 218, 224 (2d Cir. 2001).

When an arbitration clause requires arbitration of disputes "arising out of" the agreement, the clause is deemed to be *narrow* and arbitration is restricted to those disputes what literally arise from the contract. When the arbitration clause includes such phrases as "in connection with" or "relating to", the clause is characterized as *broad*. *Vetco Sales, Inc. v. Vinar*, 2003 U.S. Dist. LEXIS 6925 (N.D. Tex. 2003)

The language, "arising" out of or arising under this agreement, was also directly addressed in *Mediterranean Enterprises Inc., v. Ssangyong Corp,* 708 F.2d 1458, 1464 (9th Cir. 1983) ("Any disputes arising hereunder or following the formation of joint venture shall be settled through binding arbitration. . . ."). The Ninth Circuit held that "arising under" was a *narrow* clause, and limited the scope of the arbitration clause accordingly. It distinguished other clauses which were *broad* (such as "any controversy or claim arising out of or relating to this agreement," or "any dispute arising out of or relating to this contract or the breach thereof").

The Ninth Circuit found that it was a "significant" matter whether the clause applies to disputes "arising out of this Agreement" compared to one that applies to disputes "relating to the agreement." The Court held that the language, "arising hereunder," is intended to cover a much narrower scope of disputes. *Ssangyong,* 807 F.2d at 1464. There, the court distinguished other cases where the arbitration provision was broad stating "[m]ost cited cases involve arbitration clauses which were drafted in broader terms and intended to cover a broader spectrum of disputes than the clause involved here." *Id.* at 1463, n.5. It also noted that those matters which were determined to be outside the scope of the arbitration clause and not arbitrable could have occurred even if the Agreement did not

exist. Thus, they are also independent events and claims and do not *arise* out of the agreement.

Westport supports its position by citing the *Kamaya* decision where it quotes select language from the case in an attempt to convince this Court that in determining the scope of a contract, the court should error on the side of compelling arbitration. Br. at 28. This, however, is not the law and is completely inconsistent with the legal rule of contracts that a party is not bound to things he or she did not agree. Westport's selected language cited from *Kamaya* is easily explained by the fact that the Court was reviewing an agreement that "contains a *broad and inclusive* internal dispute provision that ultimately requires arbitration *of all unresolvable disputes* and differences between partners . . . ." 91 Wn. App. at 714 (emphasis added).

While a *broad* clause may bring collateral or related matters into arbitration, a *narrow* one will not. In *Blythe v. Deutsche Bank AG*, 2005 U.S. Dist. LEXIS 292, 16-17 (S.D.N.Y. 2005), the court recognized these principles stating:

> if the clause is narrow, "the court must determine whether the dispute is over an issue that 'is on its face within the purview of the clause,' or over a collateral issue that is somehow connected to the main agreement that contains the arbitration clause." "Where the arbitration clause is narrow, a collateral matter will generally be ruled beyond its purview." Third, if the arbitration clause is broad, "'there arises a presumption of arbitrability' and arbitration of even a collateral matter will be ordered if the claim alleged 'implicates issues of contract construction or the parties' rights and obligations under it.'"

Id. (footnotes omitted).

Likewise, in *Vetco Sales,* 2003 U.S.Dist. LEXIS 6925, a Shareholder Buy-Sell Agreement mandated arbitration of "each dispute, claim and controversy . . . *arising out of* this Agreement or breach thereof." Disagreements arose and the parties entered into a second agreement, a Buy-Out Agreement, which did not include an arbitration clause. Plaintiffs sued for breach of the Buy-Out Agreement and defendants moved to compel arbitration. The Court held that because the arbitration clause employed only the language "arising out of" without the broader terms "in connection with" or "relating to", that the clause was a *narrow* one and applied only to those disputes that literally arise from that Buy-Sell Shareholder Agreement. *Id.* at 10 (citing *United Offshore Co. v. Southern Deepwater Pipeline Co.,* 899 F.2d 405, 409-410 (5th Cir. 1990)).

The Court in *Vetco* rejected the defendants' argument that the buy-out agreement or disputes arose out of the Shareholder Agreement and should be viewed as intertwined with the Shareholders Agreement, because contract principles would not permit expansion of the parties' actual contract. The Court reviewed the Buy-Sell Agreement and found that on its face it was clear that it delineated the restrictions governing acquisition and transfer of Vetco stock, but did not include any of Vetco's present causes of action. None of Vetco's causes of action implicated the restrictions on stock transfer or those obligations imposed by the

Shareholder Agreement. The Court noted that an arbitration clause is a "creature of contract and may not be stretched beyond the scope intended by the parties" – the claims fell outside the scope of the clause and were not subject to arbitration. *Id.* at 11.

Similar to *Vetco*, the 2004 Shareholders Agreement only deals with very specific matters between the shareholders: (1) granting of an option to Daryl Wakefield to purchase 360 shares from Westport, (2) restricting the transferability of shares to the corporation or other shareholders to protect the closely-held corporation status, (3) obligating shareholder distributions for tax purposes, and other specific distributions at the written request of then-shareholder, Rick Rust, and (4) confidentiality of business operations. CP 44-54. The Agreement does <u>not</u> in any way include or encompass any of the conduct, duties, rights and obligations imposed by common law or statute which form Mr. Nelson's claims and causes of action.

Mr. Nelson's Fourth Cause of Action, entitled Breach of Fiduciary Duty and Minority Shareholder Oppression, alleges that Mr. Edson owes a fiduciary duty to him as a minority shareholder, a duty not to frustrate or impeded his rights or benefits of share ownership including his employment and compensation from employment; that Mr. Edson breached this fiduciary duty, that Mr. Wakefield acted in concert to breach the fiduciary duties, and that as a result, Mr. Nelson is entitled to all

damages flowing from such breaches, including profits, salary, benefits, bonuses, financial benefits of share ownership, increased value of ownership, etc. This cause of action arises from the acts and omissions of Mr. Edson over a long period of time and are based on common law torts and statutory rights. CP 21-22. *None* of these claims and supporting evidence arise from the 2004 Shareholders Agreement. They exist independent of it, and in fact, many of the events and acts occurred prior to its execution.

Mr. Nelson's Sixth Cause of Action for Declaratory Relief alleges duress, coercion, misrepresentation, failure of consideration, and violations of fair dealing and good faith, and seeks a declaration by the Court that the Shareholders Agreement does not control or restrict the claims or damages sought in the case, and that it is otherwise void and unenforceable. CP 27. Such relief is not a matter which is arbitrable under the narrow arbitration clause or the limited matters covered by the Agreement.

Where the arbitration clause is narrow, as here, whether the Agreement is valid is dependent upon the principles of contract law and is a matter reserved to the Court. And, the validity of the arbitration provision under the Washington Arbitration Act is for the court, and subject to a jury trial. RCW 7.04.040.

Westport has conceded that Mr. Nelson's employment claims and breach of implied contract of employment under Causes of Action I and II are not included in the arbitration clause, are not arbitrable, and stand alone independent of the Shareholder Agreement. CP 483. Yet, Westport argues that the damages from these claims must be decided by an arbitrator as those damages include the increased share value in future years if Mr. Nelson had not been wrongfully terminated, and the reasonable expectation of the increase in share value and distributions had he not been wrongfully terminated. Br. at 11, n. 4. Despite Westport's concession that no employment-based claims are arbitrable, it still seeks to bring many of these factual allegations into arbitration, and to foreclose those issues from being tried to the jury and to restrict Mr. Nelson's damages claims.

Under the narrow arbitration clause at issue, an arbitrator would not be empowered to decide whether the termination of Mr. Nelson was wrongful, legal or operative, i.e. whether it triggered any obligation to sell shares back to the company or the company's option to repurchase those shares, or at what price. And an arbitrator would not be empowered to determine the value of the shares that Mr. Nelson should have received were he not wrongfully terminated, or his other compensatory and statutory damages. The arbitrator would not be empowered to eliminate

Mr. Nelson's common law and statutory claims for full compensatory economic damages.

After Mr. Nelson rejected Mr. Edson's demand that he retire due to health, and after he rejected Mr. Edson's demand to then resign or be terminated, and after rejecting the demand that he transfer his shares at the inaccurate price they offered, Mr. Nelson was immediately advised that Westport would "proceed under Section 6.5 [of the 2004 Shareholders Agreement] . . . to require the sale of your 460 shares to Westport at a price per share of $2,362.11 for a total of $1,086,570." CP 386. The letter from Mr. Wakefield, Westport's President, further indicated that the issue for arbitration was the value of the stock and the correct accounting method. CP 386-387. Simply put, an arbitrator is not entitled to determine if Mr. Nelson was lawfully terminated, or whether the "termination" triggered the buy-back provision.[8] But this is now what Westport is attempting to force into arbitration.

[8] Even assuming *arguendo* that the Shareholder Agreement and arbitration clause is enforceable, Westport has not validly commenced any arbitration or served a valid notice of arbitration pursuant to the arbitration clause. It incorporates the Commercial Arbitration Rules of the American Arbitration Association. Those rules require at R-4 that the notice of intention to arbitrate include a "statement setting forth the nature of the dispute, the names and addresses of the parties, the amount involved, the remedy sought, and the hearing locale requested." The rules also provide that the description of the claim should be in sufficient detail to make the circumstances of the dispute clear to the arbitrator. Westport has requested arbitration, yet it has not taken the mandatory first step to commence arbitration, and has not set forth in such a notice the specific issues for arbitration. Both attempted notices of arbitration are insufficient under the AAA rules. These deficiencies leave Mr. Nelson and the Court completely in the dark. It suggests that Westport is attempting to wrongfully force into arbitration, broadly, all the common law and statutory claims which are far beyond the scope of the arbitration clause, as well as trying to force into arbitration many of the factual allegations which support employment and other tort claims asserted. It suggests that Westport is attempting to create collateral estoppel claims, and increase the time, cost and resources to adjudicate Mr. Nelson's claims.

Westport seeks to use a very narrow arbitration clause, applicable to disputes arising from an Agreement which includes only limited matters, as the vehicle to bring into arbitration the underlying factual issues which arise and support Mr. Nelson's claims under common law or statutory law. As such, Westport seeks to restrict or destroy the non-arbitrable claims and deny Mr. Nelson his right to trial of those non-arbitrable issues and claims. Mr. Nelson's statutory and common law claims provide for full compensatory and economic damages. This is what Westport attempts to eliminate in arbitration, and this is precisely why Westport has been so adamant and has repeatedly filed motions to compel arbitration – in order to underhandedly destroy or restrict Mr. Nelson's non-arbitrable claims by forcing arbitration first. This strategy was clearly revealed and known to the trial court, which is why it determined that trial should occur first. See VRP (August 5, 2005) 12:6 to 13:17.

b. Cases interpreting analogous agreements support the decision of the Superior Court.

In addition to the similar case of *Vetco,* discussed above, the fact situation and holding in *Davis v. Chevy Chase Financial,* 667 F.2d 160 (D.C. Cir. 1981), is remarkably similar to the present case. During his employment, Davis executed a Stock Purchase Agreement whereby he purchased 4,960 shares of stock. The Agreement contained provisions restricting his right to alienate his minority interest, and obligated the

company to purchase them if he wanted to sell them or upon his termination of employment. Davis terminated employment and the company demanded that Davis tender his shares back and when he refused, the company invoked the arbitration clause to submit the dispute to arbitration. Davis denied that the matter was subject to arbitration, participated under protest, and denied that an arbitrable dispute existed because he did not wish to sell his shares and contended he was under no obligation to transfer them back. He maintained that there were oral representations made to him that he would not have to transfer the shares back if he was terminated more than 5 years after employment.

Over Davis' protests, the arbitrator rejected Davis' claim that he was under no contractual obligation to sell the shares back, and ordered their conveyance at a certain price. The arbitrator determined that his termination *triggered* the contractual obligation to tender the shares back. Davis then filed suit claiming excessive authority of the arbitrator under the arbitration clause and that the arbitrator did not have authority to rule on the issue whether Davis was obligated to tender his shares back to the company. Davis argued that the arbitrator only had jurisdiction to determine the value of shares that Davis might actually transfer back, and that the condition precedent to obligate a transfer back had not occurred. Davis also sued claiming that there were oral misrepresentations as to the stock purchase and that the company's attempt to enforce the Agreement

in a manner contrary to those representations, through arbitration, was in violation of the anti-fraud provisions of the federal securities laws.

The *Davis* court held that the arbitrator did not have the power to determine whether Davis was contractually obliged to sell his shares to the company, whether the condition precedent occurred, because that issue was not within the scope of the arbitration agreement. The Court noted that neither arbitrators nor courts have the prerogative to redraft an arbitration clause to require parties to arbitrate matters that they did not initially agree to arbitrate. It stated that to hold otherwise would run the unacceptable risk of denying a party's right to a judicial forum to resolve disputes.

The Court found that the arbitration clause related to the means of valuing the stock *in the event* it was to be transferred back to the company. It ruled that the arbitration clause did not encompass whether the events occurred which would then trigger a right of the company to repurchase the shares. In addition, as here, the company had given notice of the nature of the dispute for arbitration, asserting that it was entitled to repurchase the shares at a value as determined under the Agreement, that it had exercised its right to repurchase, and the parties were unable to agree on the value under the agreement. Such notice indicated the restricted scope of the arbitration clause, acknowledged by the company.

Here, the arbitration clause does not encompass the issue of whether the events giving rise to a repurchase of shares has occurred, i.e. whether the "termination" is lawful or operative, or whether there were oral representations and misrepresentations made to Mr. Nelson surrounding his purchase of shares over the years. As in *Davis,* Mr. Nelson asserts that the events which supposedly would *trigger* Westport's right to repurchase his shares under the Agreement, i.e. the conditions precedent of termination/resignation, are not within the scope of the arbitration clause. Indeed, as discussed above, Westport has conceded that point, by acknowledging that none of Mr. Nelson's employment or employment-related claims are included in the Shareholders Agreement or are otherwise subject to arbitration.[9] CP 389; Br. 11, n. 4.

Because the Superior Court correctly determined that the narrow arbitration clause did not cover the claim asserted in this lawsuit, the decision below should be affirmed.

2. Under the 2004 Shareholder Agreement, whether it is void and unenforceable under common law contract principles is for the Court to decide.

Mr. Nelson properly requested that the Superior Court issue a declaratory judgment that the 2004 Shareholders Agreement does not control or restrict the claims in the case. Mr. Nelson also seeks declaratory

[9] Westport moved for arbitration pursuant to Chapter 7.04 RCW, which expressly does not apply to employment, RCW 7.04.010.

relief that the Agreement is otherwise invalid, void or unenforceable, which is to be determined by state contract principles of formation and enforceability of contracts, and must be determined prior to any attempt to enforce any arbitration clause within such an Agreement. In fact, Westport itself moved for summary judgment on this claim.

A party may assert general contract defenses to a putative agreement to arbitrate. *Southland Corp. v. Keating,* 465 U.S. 1, at 16 n. 11 (1984). Traditional state law contract principles as to formation include adequate consideration, mutual assent, mutuality of obligation, breach excusing performance, duress, coercion, misrepresentation or fraud. Here, Mr. Nelson has pleaded coercion, duress, misrepresentations, failure of consideration, violations of the covenants of good faith and fair dealing, and such breaches as to excuse any claimed performance. Based on the evidence submitted by Mr. Nelson, the Superior Court determined that "there are genuine issues of material fact that must be decided at trial . . . ." CP 501.

Mr. Nelson was aware of the existence of the Buy-Sell agreements under which he purchased shares of stock of the company, and he understood that in this closely-held corporation, only limited numbers of persons would be permitted to be shareholders and that he could not transfer the shares to anyone other than shareholders or the company. CP 379-384. He also understood, under the prior Buy-Sell agreements,

that only the limited matters included in the agreements, i.e. the question of the book value of the shares and prohibition against transferring stock to someone other than the company or shareholders, would be subject to arbitration. *Id.* The Agreement on its face does not apply to the claims asserted by Mr. Nelson in this case.

The 2004 Shareholders Agreement was not requested, negotiated, or bargained for in any way by Mr. Nelson. *Id.* It was presented as a take-it-or-leave-it matter from Mr. Edson, the majority shareholder. *Id.* Mr. Edson had stated at a meeting in late 2004 that a shareholder agreement was needed to make everything the same for everyone. No one could or would question or refuse him, including Mr. Nelson. CP 383. Mr. Edson had made threats in the past toward shareholders to the effect that they would be fired if they did not go along with something he wanted, and he had caused the firing or termination of several shareholders and management executives without apparent reason. *Id.* Mr. Nelson had no choice but to agree to anything Mr. Edson wanted. Mr. Nelson knew that the document was written by Mary Welk, who at that time was not an Officer, shareholder or employee of Westport Shipyards, Inc., but was an officer and employee of Pacific Marine Management, a company owned by Mr. Edson. *Id.* Mary Welk frequently would "represent" Mr. Edson in dealings with the shareholders and executive employees of Westport, including Mr. Nelson. *Id.*

Mr. Nelson observed in the 2004 Shareholder Agreement presented to him to sign that it had the same type of arbitration provision as his prior Buy-Sell agreements, requiring arbitration only of matters arising from the agreement. It was his understanding and intention in signing that document, although it did not represent his free will, that the arbitration clause was limited just to the specific matters in the agreement, and that he was not subjecting to arbitration any other possible claims he might have in the future or under law or that he was waiving his right to a jury trial on any common law or statutory shareholder claims, employment claims or tort claims which might exist or arise in the future. CP 383.

In summary, the *narrow* scope of the arbitration clause in the 2004 Shareholders Agreement limits arbitration to only those matters arising from the Agreement itself. The scope is determined by the court, and here, the court ruled that the scope was narrow, which was not assigned as error. Neither the validity, enforceability, or scope of the agreement has been given to an arbitrator to determine under the language of the Agreement itself. Nothing in this lawsuit involves any dispute over the matters of substance covered in the Agreement: the Wakefield option, confidentiality of business operations, the duty to distribute monies for tax payments or at Rick Rust's request or enforcing any obligation to buy back his shares, or non-transferability of shares. The disputes in this lawsuit arise from common law and statutory rights of action, and exist

independently from the Shareholder Agreement. Mr. Nelson simply seeks a declaration from the Court that the Shareholder Agreement does not apply to this controversy, and that if it does that, it is void and unenforceable.

3. The prior Agreements are inapplicable, void and unenforceable for the same reasons.

Westport asserts that if the 2004 Shareholder Agreement is held to be void or invalid, the prior agreements would be resurrected, and that because each of those agreements include arbitration clauses, the claims would have to be sent to arbitration. This argument is misplaced. Each of the prior buy-sell agreements do contain an arbitration clause, but the clause is even more limited and narrow than the clause in the 2004 Shareholders Agreement. The scope of arbitration under the prior agreements would be limited just as the scope under the 2004 agreement is limited. Therefore, Westport's argument in this regard should be rejected.

D. Respondents Have A Right To Jury Trial On The Issue Of Arbitration.

Pursuant to the Washington Arbitration Act, Mr. Nelson has raised a substantial issue "as to the existence or validity of the arbitration agreement or the failure to comply therewith," and has complied with the statutory procedures and demanded trial by jury. CP 563. Thus, at a minimum, the Superior Court must proceed to trial on such issues.

As a matter of contract law, a party cannot be forced to arbitrate an issue or dispute which is not within the arbitration agreement. But more

significantly, the right to trial by jury is inviolate. *Washington State Constitution,* Art. I Sec. 21. Any alleged waiver of the right to jury trial, by virtue of an arbitration clause, "must be voluntary, knowing and intelligent." *City of Bellevue v. Acrey,* 103 Wn.2d 203, 207, 691 P.2d 957 (1984). Waivers are narrowly construed. *Wilson v. Horsley,* 137 Wn.2d 500, 511, 974 P.2d 316 (1999). A party who consents to a contract which includes a limited arbitration clause does not thereby waive his right to a judicial hearing on the merits of a dispute not encompassed within the clause. *Davis v. Chevy Chase Financial Ltd.,* 667 F.2d 160 (D.C. Cir. 1981).

Not only has Mr. Nelson not waived his right to trial by jury of his common law and statutory shareholder claims (misrepresentation, breach of fiduciary duty, oppression, tortious interference, etc.) by virtue of the narrow arbitration clause in the 2004 Shareholders Agreement, but he has also not waived his right to jury trial on the issue of validity or existence of the arbitration agreement. That right to jury trial is specifically afforded under the Washington Arbitration Act, RCW 7.04.040.

The procedures for a determination of whether to order the parties to arbitration and what to order to arbitration, if anything, is set forth in RCW 7.04.040, which provides:

> (1) A party to a written agreement for arbitration claiming the neglect of another to proceed with an arbitration there under may make application to the court for an order directing the parties to proceed with the arbitration in accordance with their agreement. .

> . . If the court is satisfied after hear-ing the parties that no substantial issue exists as to the existence or validity of the agreement to arbitrate or the failure to comply therewith, the court shall make an order directing the parties to proceed to arbitrate in accordance with the terms of the agreement.
>
> (2) If the court shall find that a substantial issue is raised as to the existence or validity of the arbitration agreement or the failure to comply therewith, the court shall proceed immediately to the trial of such issue. If upon such trial the court finds that no written agreement providing for arbitration was made or that there is no default in proceeding thereunder, the motion to compel arbitration shall be denied.
>
> (3) Either party shall have the right to demand the immediate trial by jury of any such issue concerning the validity or existence of the arbitration agreement or the failure to comply therewith. Such demand shall be made before the return day of the motion to compel arbitration under this section. . . .
>
> (4) In order to raise an issue as to the existence or validity of the arbitration agreement or the failure to comply therewith, a party must set forth evidentiary facts raising such issue . . . (b) by contesting a motion to compel arbitration as provided under subsection (1) of this section.

As noted above, Mr. Nelson has raised a substantial issue as to the validity or existence of the arbitration agreement or the failure to comply therewith. Therefore, at a minimum, a jury trial must be held on the issues.

Mr. Nelson has not failed to comply with any arbitration clause in the 2004 Shareholders Agreement, or any prior Buy-Sell Agreement, because any obligation to transfer shares back has not arisen – that issue has not been determined because it is a part of the claims and factual allegations in this suit – none of which are arbitrable issues or claims. He was not under any contractual obligation to transfer shares back to the

company or the other shareholders because the conditions precedent to any obligation to so transfer shares under any of the agreements are still undecided. They are part of the issues and claims in the lawsuit, which are not subject to arbitration.

To submit the narrow issue of share value for a buy-back by Westport to arbitration prior to trial of the multitude of underlying, non-arbitrable issues (discrimination, wrongful termination, breach of implied employment contract, minority shareholder oppression, breach of fiduciary duty) would erase Mr. Nelson's right to jury trial under the Washington Arbitration Act, and would place his clearly non-arbitrable claims before an arbitrator for potential decision. Simply said, the scope of the arbitration clause does not encompass Mr. Nelson's wrongful termination of employment claims or his shareholder claims for which is he entitled to recover full, compensatory damages, not limited by the Shareholders Agreement which does not control these claims. The arbitration agreement is, therefore, not applicable and the decision below should be affirmed.

V. CONCLUSION

For the reasons stated above, Respondents respectfully request that this Court dismiss this appeal as untimely, or in the alternative, affirm the Superior Court below and remand this matter for trial. Affirming the trial court's decision and Order of November 10, 2005, protects the rights of Mr. Nelson to have his non-arbitrable claims decided by the court and a

jury, prior to implementation of any option by Westport to have the shares transferred to it or the value of the buy-back. Because the clause is narrow, Mr. Nelson is entitled to first have a trial on his non-arbitrable claims, and in the event he is not successful on those and it is determined that he was lawfully terminated triggering the buy-back, then the dispute is ripe for arbitration under this narrow clause and limited terms of the Agreement.

Dated this 28th day of February, 2007.

Respectfully submitted,

GORDON, THOMAS, HONEYWELL,
MALANCA, PETERSON & DAHEIM LLP

By _____
Victoria L. Vreeland
WSBA No. 08046
James W. Beck
WSBA No. 34208
Attorneys for Respondents

EXHIBIT A

LEXSEE 2006 U.S. DIST. LEXIS 93680

GOODRICH CARGO SYSTEMS, Plaintiff, v. AERO UNION CORP., Defendant.

No. C 06-06226 CRB

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA

2006 U.S. Dist. LEXIS 93680

December 14, 2006, Decided
December 14, 2006, Filed

COUNSEL: [*1] For Goodrich Cargo Systems, LLC, a Delaware corporation, Plaintiff: Mark Jay Linderman, LEAD ATTORNEY, SONNENSCHEIN NATH & ROSENTHAL LLP, San Francisco, CA.; Matt Merril Marostica, Attorney at Law, Sonnenschein Nath & Rosenthal LLP, San Francisco, CA.

For Aero Union Corporation, a California corporation, Defendant: M. Taylor Florence, LEAD ATTORNEY, Bullivant Houser Bailey, SACRAMENTO, CA.; Darcy L. Muilenburg, Gaurav Kalra, Bullivant Houser Bailey PC, Sacramento, CA.

JUDGES: CHARLES R. BREYER, UNITED STATES DISTRICT JUDGE.

OPINION BY: CHARLES R. BREYER

OPINION:

ORDER

Goodrich Cargo Systems ("Plaintiff") sued Aero Union Corporation ("Defendant") in connection with the acquisition of a business unit ("the APS Business") that manufactures, among other things, systems for loading cargo onto aircraft. Now pending before the Court is Defendant's motion to compel arbitration. For the reasons set forth below, that motion is hereby GRANTED in part and DENIED in part.

BACKGROUND

On June 29, 2004, Plaintiff agreed to buy the APS Business from Defendant. To consummate this deal, the parties executed an Asset Purchase. Agreement ("APA"). The APA is an umbrella contract that sets forth the [*2] structure of the entire transaction. Its primary purpose is to transfer all assets of the APS Business from Defendant to Plaintiff. Significantly, the APA contains no comprehensive arbitration clause. It does, however, provide that "[t]he Exhibits and Schedules hereto are an integral part of this Agreement and are incorporated by reference herein." APA P 9.12. Similarly, it notes that "[e]ffective on the Closing, Seller and Buyer will enter into a Manufacturing License Agreement ... on the terms and conditions as further set forth in Schedule 7." APA P 7.1.

Thus, as an attachment to the APA, the parties appended a Manufacturing License Agreement ("MLA"). The purpose of the MLA was to create a licensing arrangement such that Defendant would continue to operate a portion of the APS Business called the Cargo Transfer System. In other words, under the MLA, the parties agreed that Defendant would continue to manufacture, price, and sell Cargo Transfer Systems and would pay to Plaintiff a "royalty" of fifteen percent of revenue generated by such sales. The MLA contains a binding arbitration clause. See MLA P 15.

In this lawsuit, Plaintiff asserts five causes of action. Three of [*3] these claims arise under the APA, one arises under the MLA, and one involves a claim for conversion that, at least on the face of the complaint, does not clearly arise under either agreement. Defendant filed a motion to compel arbitration, arguing that all of Plaintiff's claims arise out "one integrated business transaction." Defendant contends that the case therefore must be dismissed and the entire matter submitted to binding arbitration under the arbitration clause contained in the MLA.

DISCUSSION

The Federal Arbitration Act provides that an agreement to submit commercial disputes to arbitration shall be "valid, irrevocable, and enforceable." *9 U.S.C. § 2.* Congress's purpose in passing the Act was to put arbitration agreements 'upon the same footing as other contracts,'" thereby "reversing centuries of judicial hostility to arbitration agreements" and allowing the parties to avoid 'the costliness and delays of litigation.'" *Scherk v.*

Alberto-Culver Co., 417 U.S. 506, 510-11, 94 S. Ct. 2449, 41 L. Ed. 2d 270 (1974) (quoting H. R. Rep. No. 96, 68th Cong., 1st Sess., 1, 2 (1924)). Thus, in applying the Act, courts have developed a "liberal federal policy favoring arbitration [*4] agreements," *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Co., 460 U.S. 1, 24-25, 103 S. Ct. 927, 74 L. Ed. 2d 765 (1983)*, and doubts about the applicability of an arbitration clause are "resolved in favor of arbitration," *United Steelworkers of Am. v. Warrior & Gulf Navigation Co., 363 U.S. 574, 582-83, 80 S. Ct. 1347, 4 L. Ed. 2d 1409 (1960)*.

At the same time, however, "arbitration is simply a matter of contract between the parties; it is a way to resolve those disputes--but only those disputes--that the parties have agreed to submit to arbitration." *First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 943, 115 S. Ct. 1920, 131 L. Ed. 2d 985 (1995)*. Indeed, the Supreme Court has emphasized that "'arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.'" *AT&T Tech., Inc. v. Communications Workers of Am., 475 U.S. 643, 648, 106 S. Ct. 1415, 89 L. Ed. 2d 648 (1986)* (quoting *Warrior & Gulf, 363 U.S. at 582*). Thus, a federal court must review the contract at issue to determine whether the parties have each agreed to submit a particular dispute to arbitration. See *Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79, 83, 123 S. Ct. 588, 154 L. Ed. 2d 491 (2002)* ("The question [*5] whether the parties have submitted a particular dispute to arbitration, i.e., the question of arbitrability,' is an issue for judicial determination ...."); *John Wiley & Sons, Inc. v. Livingston, 376 U.S. 543, 547, 84 S. Ct. 909, 11 L. Ed. 2d 898 (1964)* ("The duty to arbitrate being of contractual origin, a compulsory submission to arbitration cannot precede judicial determination that the ... agreement does fact create such a duty.")

Here, Defendant contends that the MLA requires arbitration of all claims set forth in Plaintiff's complaint. Defendant argues that the APA and the MLA were executed together as part of an integrated business transaction and that the MLA's binding arbitration clause therefore encompasses any disputes related to that business transaction. See, e.g., *Pers. Sec. & Safety Sys., Inc. v. Motorola, Inc., 297 F.3d 388, 393 (5th Cir. 2002)*.

This Court disagrees. Just because the parties enacted multiple agreements in connection with the acquisition of the APS Business does not mean that this Court may ignore the fact that there are discrete agreements pertaining to different facets of the transaction. Here, the parties executed two distinct agreements. The [*6] first agreement, the APA, governs Plaintiff's acquisition of certain assets owned by Defendant. The second agreement, the MLA, governs a smaller aspect of the transaction--namely, a licensing arrangement whereby Defendant agreed to continue operating a portion of the business unit it sold. Only the latter agreement contains an arbitration clause, and it follows that the arbitration clause only applies to disputes as to those aspects of the transaction that are actually covered by the latter agreement. See *Int'l Ambassador Programs v. Archexpo, 68 F.3d 337 (9th Cir. 1995)* (holding that an arbitration award did not preempt or preclude a judgment obtained in another lawsuit between the same parties and involving the same business relationship where "the Moscow arbitration and the Ambassador litigation [were] two distinct disputes arising under two separate agreements, one providing for arbitration and one not"); *Rosenblum v. Travelbyus.com Ltd., 299 F.3d 657 (7th Cir. 2002)* (holding that a purchase agreement and an employment contract enacted simultaneously by the parties pertained to different subject matter, and that the compulsory arbitration clause [*7] contained in the latter did not require the court to dismiss claims arising under the former).

This conclusion is dictated by the manner in which the parties themselves structured the transaction. Here, Plaintiff and Defendant executed an umbrella contract that incorporated as "schedules" or "attachments" several other discrete agreements. If the parties, who are not unsophisticated legal actors, had wanted to arbitrate any dispute arising out of their integrated economic transaction, they should have placed an arbitration clause in the umbrella agreement. The only logical inference to draw from the fact that the arbitration clause appears only in one of the attachments to the APA is that the parties intended the arbitration clause to apply to part of the transaction, and not to all of it. To hold otherwise would not only permit the tail to wag the dog, it would effectively mean that an arbitration clause included anywhere in a transaction must apply everywhere. The Court declines to interpret the MLA's arbitration clause in such an all-consuming fashion, notwithstanding Defendant's observation that the two agreements refer to one another and that the APA explicitly incorporates the [*8] terms of the MLA. That the whole constitutes the sum of its interrelated parts it obvious, but that does not mean a particular provision contained in and confined to one part is applicable to the whole.

Furthermore, the plain language of the arbitration clause requires that this Court confine it to the context of the MLA. The clause states that the parties must submit to arbitration "all disputes, claims and controversies that arise under or relate in any way *to this Agreement.*" MLA P 15 (emphasis added). The term "this Agreement" is unambiguously defined as the MLA itself, and not any other part of the larger business transaction between Plaintiff and Defendant. See MLA pmbl. Thus, consistent with the most plausible view of the language and structure of the parties' agreement, the Court concludes

that only disputes arising under the MLA must be submitted to arbitration. n1

> n1 Plaintiff has argued that the MLA's arbitration clause is inconsistent with the APA. The Court finds that argument unpersuasive. There is nothing inconsistent in the APA with the application of an arbitration clause, even one that prohibits an award of attorneys' fees, as the clause in the MLA does. A clause requiring arbitration and prohibiting an award of attorney's fees *in disputes between Plaintiff and Defendant* would be perfectly consistent with, for example, the APA's indeminification clause, which requires Defendant to pay attorneys' fees that Plaintiff might incur *in suits brought by third parties.* In short, the Court finds nothing in the APA that is inconsistent, as a matter of logic, with the MLA's arbitration clause. The problem is not that the APA is incompatible with an arbitration clause, but rather that it just does not contain one.

[*9]

Defendant observes that requiring arbitration of only a portion of Plaintiff's claims "would result in significant waste of judicial resources, unnecessary expense, and the specter of inconsistent adjudication of common questions of law and fact." To be sure, it does. Conducting multiple proceedings in different tribunals about similar subject matter will indeed produce spectacular inefficiency. Nonetheless, this Court is not entitled to rewrite a contract merely because it commands an inefficient result. A federal court may not compel a party to submit to arbitration unless the party has consented to it, and here, Plaintiff has not consented to arbitrate all disputes arising under the APA. Of course, if Defendant's chief concern is the efficiency of dispute resolution, it remains free to repudiate the arbitration clause it now seeks to enforce and submit the entire controversy to this Court's jurisdiction.

CONCLUSION

The Court holds that the arbitration clause contained in the MLA applies only to disputes arising under that particular agreement. Therefore, as to Count I, Count II, and Count III, which all arise out of provisions in the APA, Defendant's motion to compel arbitration [*10] is DENIED. As to Count IV, which arises under the MLA, Defendant's motion to compel, arbitration is GRANTED. As to Count V, which involves the alleged conversion of a payment made to Defendant rather than to Plaintiff, the motion to compel arbitration is DENIED. If, however, it ultimately appears that the converted payment relates to the post-MLA sale of a Cargo Transfer System, and therefore falls within the scope of the MLA, see MLA P 7, Defendant may renew its motion to compel arbitration as to Count V.

In sum, Defendant's motion to compel arbitration is GRANTED as to Count IV and DENIED as to Counts I, II, III, and V. The parties shall appear before the Court for a status conference at 8:30 a.m. on Friday, January 5, 2007.

IT IS SO ORDERED.

Dated: December 14, 2006

CHARLES R. BREYER

UNITED STATES DISTRICT JUDGE

EXHIBIT B

LEXSEE 2006 U.S. DIST. LEXIS 94836

KEVIN SLATNICK and JOHN SONNENBERG, Plaintiffs, vs. DEUTSCHE BANK AG; DEUTSCHE BANK SECURITIES INC. d/b/a DEUTSCHE BANK ALEX. BROWN; CORNERSTONE STRATEGIC, ADVISORS, LLC; ROGER FULLER; D. MICHAEL BISHOP; CANTLEY & SEDACCA, LLP; EDWARD SEDACCA, ESQ.; CLARION CAPITAL LLC; CF ADVISORS, LLC; DAN BROOKS; and DOES 1-50, inclusive, Defendants.

CASE NO. 04CV2288-LAB (JMA)

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF CALIFORNIA

2006 U.S. Dist. LEXIS 94836

March 14, 2006, Decided
March 15, 2006, Filed

COUNSEL: [*1] For Kevin Slatnick, John Sonnenberg, Plaintiffs: Robert Scott Dreher, LEAD ATTORNEY, Dreher Law Firm, San Diego, CA.

For Deutsche Bank AG, Deutsche Bank Securities, Inc., doing business as Deutsche Bank Alex Brown, a Division of Deutsche Bank Securities, Inc., Defendants: Benjamin Sokoly, Lawrence M Hill, Seth C Farber, LEAD ATTORNEYS, Dewey Ballantine, New York, NY.; David S McLeod, LEAD ATTORNEY, Dewey Ballantine, Los Angeles, CA.

For Cornerstone Strategic Advisors, LLC, Defendant: Kirk C Lusty, LEAD ATTORNEY, Cornerstone Fuller and Bishop, Salt Lake City, UT.; Scott Mitchell Rand, LEAD ATTORNEY, Law Offices of Scott M Rand, San Diego, CA.

For Roger Fuller, D Michael Bishop, Defendants: Kirk C Lusty, LEAD ATTORNEY, Cornerstone Fuller and Bishop, Salt Lake City, UT.

JUDGES: HONORABLE LARRY ALAN BURNS, United States District Judge.

OPINION BY: HONORABLE LARRY ALAN BURNS

OPINION:

ORDER GRANTING DEUTSCHE BANK DEFENDANTS' MOTION TO COMPEL ARBITRATION

[Dkt No. 61]

This matter is before the Court on the motion of defendants Deutsche Bank AG and Deutsche Bank Securities, Inc. d/b/a/ Deutsche Bank Alex Brown (collectively "Deutsche Bank" or "Defendants") to compel arbitration of [*2] plaintiffs' claims against them in this breach of contract action arising out of a failed tax shelter arrangement Plaintiffs allege defendants designed, marketed, and sold while knowing it to be fraudulent and illegal. Plaintiffs Kevin Slatnick and John Sonnenberg (collectively "Plaintiffs") filed Opposition, and Defendants filed a Reply. Pursuant to Civil Local Rule 7.1(d)(1), the Court finds the issues appropriate for decision on the papers and without oral argument. For the reasons discussed below, the Motion is **GRANTED** and this action is stayed as to the Deutsche Bank Defendants (only), pursuant to the Federal Arbitration Act, *9 U.S.C. § 3.* n1

n1 The other remaining defendants in this action are Cornerstone Strategic Advisors, LLC, Roger Fuller, and D. Michael Bishop. The docket indicates all the other defendants originally named have been termed from the case, although Plaintiffs are pursuing an appeal of this court's dismissal of "the Clarion Defendants" for lack of personal jurisdiction. Dkt Nos. 52, 63.

[*3]

I. BACKGROUND

As summarized in the court's August 10, 2005 Order denying Defendants' Motion To Stay, Plaintiffs are two

San Diego County residents who allege they are electrical engineers who came into a large amount of cash in 2000 and 2001 from the sale of their business. They allege they were misled into paying more than $ 100,000 into a failed tax shelter scheme operated by the defendants, then tens of thousands more to undo the damage that unwitting investment cost them. Plaintiffs originally filed this action in San Diego County Superior Court, alleging three causes of action against the Deutsche Bank Defendants: negligence; unfair business practice; and aiding and abetting breach of fiduciary duty. Defendants removed the action to federal court based on diversity jurisdiction.

The challenged arrangement was a tax-oriented investment referred to as a "market-linked deposit" strategy ("MLD") intended to minimize liability on taxes from over $ 1.1 million each plaintiff realized from the sale of their technology business. Plaintiffs allege they implemented the MLD strategy by opening brokerage accounts, creating an S-Corporation and a limited liability corporation, [*4] contributing funds to the limited liability corporation which were used by the Deutsche Bank Defendants to engage in foreign currency trades, and utilized on their personal tax returns losses generated from the MLD strategy to offset their gains from the sale of their business. Mot. 21:6-21; Compl. PP 4, 38, 53, 55, 58, 59, 61, 65, 66. Plaintiffs allege the IRS informed them in October 2003 that it considered the MLD strategy to be "an abusive tax shelter," and that Plaintiffs should immediately file amended tax returns for the year 2001. This lawsuit followed, with Plaintiffs contending they were misled by the defendant financial institutions, attorneys, accountants, and advisors regarding the MLD strategy and execution of the underlying investment. Mot. 2:25-3:2.

In Deutsche Bank Defendants' unsuccessful Motion To Stay this action, they represented the mandatory arbitration provisions in the parties' Account Agreements would control resolution of Plaintiffs' claims, but expressly stated they were not invoking the arbitration clause at that time. They were constrained from moving to compel arbitration because the arbitration provision contains language restricting its enforcement [*5] in circumstances where certain class actions are pending, such as was the case at the time Defendants moved to stay this action. *See* Dkt No. 51. Plaintiffs qualified as members of a putative class in *Ling et al.* v. Deutsche Bank AG, *et al.*, No. 04cv4566 (S.D.N.Y.), an action then pending in the Southern District of New York on behalf of other individuals with purportedly similar claims to those asserted by Plaintiffs in this case.

Defendants substantiate in their Motion To Compel Arbitration that after the Motion To Stay was fully briefed, the Ling court dismissed all of the claims asserted in the Second Amended Class Action Complaint without prejudice. Counsel for the Ling plaintiffs informed that court they would not be filing a third amended class action complaint in federal court, and certain of the Ling plaintiffs subsequently filed an individual lawsuit in a Texas state court. Mot. P&A 2:5-20. Defendants assert "there is no longer a putative class action that would encompass any of the claims asserted by Plaintiffs here," removing the obstacle to enforcing the parties' arbitration agreement. Mot. P&A 2:20-21.

The Deutsche Bank Defendants argue Plaintiffs' [*6] claims against them are now properly referable to arbitration "pursuant to the broad, mandatory arbitration provision contained in the Account Agreements Plaintiffs entered into with Deutsche Bank Securities upon engaging in the MLD Strategy, and they must therefore pursue their claims, if at all, in arbitration." Mot. P&A 4:27-52. Defendants rely on *sections 3* and *4* of the Federal Arbitration Act ("FAA"), *9 U.S.C. §§ 1-16*, mandating that district courts direct parties to proceed to arbitration in instances where they have entered a written arbitration agreement and the controversy falls within the scope of their agreement, and that the court proceedings be stayed pending such arbitration.

Plaintiffs oppose the Motion on grounds: there is no valid agreement to arbitrate because the contract containing the arbitration provision is purportedly unconscionable; the contract is void because it was purportedly drafted for an illegal purpose; the arbitration agreement was purportedly induced by fraud; and their claims are purportedly beyond the scope of the arbitration agreement. n2 Defendants reply the arbitration agreement is valid, binding, and enforceable, [*7] Plaintiffs' claims fall within the scope of the arbitration agreement, and the FAA requires that this court refer the parties to their selected arbitration forum to resolve these disputes.

n2 Plaintiffs also opposed on grounds a new putative class action complaint was filed in New York in October 2005, Stearns, *et al.* v. Deutsche Bank, AG, *et al,* 05cv8739 (S.D.N.Y.). They acknowledged the Ling class action was dismissed, but argued the pendency of the Stearns case creates the same preclusive effect as had Ling to invocation of the arbitration agreement. However, while this Motion was under submission, Defendants applied *ex parte* and were granted leave to file in this case a Notice of Voluntary Dismissal of the Stearns putative class action, entered January 26, 2006, an event of which this court takes judicial notice. Dkt Nos. 80-83. The *ex parte* application was unopposed. The issue whether the Stearns case would have prevented arbitration of Plaintiffs' claims is accordingly moot, and the

court addresses only Plaintiffs' other grounds to oppose the Motion To Compel Arbitration.

[*8]

II. DISCUSSION

A. Legal Standards

The issue of arbitrability "is to be determined by the contract entered into by the parties." *Drake Bakeries, Inc. v. Local 50, 370 U.S. 254, 256, 82 S. Ct. 1346, 8 L. Ed. 2d 474 (1962)*. A party cannot be compelled to arbitrate a dispute that party has not agreed to arbitrate. *Howsam v. Dean Witter Reynolds. Inc., 537 U.S. 79, 83, 123 S. Ct. 588, 154 L. Ed. 2d 491 (2002)*; *see First Options Of Chicago v. Kaplan, 514 U.S. 938, 943, 115 S. Ct. 1920, 131 L. Ed. 2d 985 (1995)* ("arbitration is simply a matter of contract between the parties; it is a way to resolve those disputes -- but only those disputes -- that the parties have agreed to submit to arbitration"). However, the FAA embodies a policy favoring arbitration and requiring courts to compel arbitration if the court is satisfied the claim at issue falls within the scope of a valid, enforceable agreement among the parties to arbitrate the claim. *Moses H. Cone Memorial Hosp. v. Mercury Const. Corp., 460 U.S. 1, 24-25, 103 S. Ct. 927, 74 L. Ed. 2d 765 (1983)*; *see Kuehner v. Dickinson & Co., 84 F.3d 316, 319 (9th Cir. 1996)* (the FAA "created a rule of contract construction favoring arbitration").

> **A written provision** [*9] **in any ... contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction,** or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, ***shall be*** **valid, irrevocable,** and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 2.

When the court in which the suit is pending is satisfied an issue is referable to arbitration under an arbitration agreement between the parties, the court must stay the trial of the matter:

> 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 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 [*10] with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 3 (emphasis added); *see Wilmot v. McNabb, 269 F.Supp.2d 1203, 1206 (N.D.Cal. 2003)* ("If a district court determines that a party has failed to comply with a valid agreement to arbitrate, it must order the parties 'to proceed to arbitration in accordance with the terms of the agreement,' *9 U.S.C. § 4*, and it may stay the litigation until the arbitration process is complete. *9 U.S.C. § 3*"); *see 9 U.S.C. § 4* (court's role under the FAA is limited to (1) determining whether a valid agreement to arbitrate exists and, if so, (2) deciding whether the agreement encompasses the dispute at issue); *see also United Steelworkers of America v. Warrior & Gulf Navigation Co., 363 U.S. 574, 582, 80 S. Ct. 1347, 4 L. Ed. 2d 1409 (1960)*; *Simula, Inc. v. Autoliv, Inc., 175 F.3d 716, 719-20, 721 (9th Cir. 1999)* ("the language 'arising in connection with' reaches every dispute between the parties having a significant relationship to the contract and all disputes [*11] having their genesis in the contract").

The court reviewing a party's request to compel arbitration must decide whether an arbitration agreement has been executed by the parties, is a valid agreement, and covers the claims sued upon. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626, 105 S. Ct. 3346, 87 L. Ed. 2d 444 (1985)*. Even if enforcement of a mandatory arbitration agreement results in disputes that must be resolved in separate fora -- one under the FAA involving the parties bound by the Account Agreement provision and another involving parties not so bound -- "the relevant federal law *requires* piecemeal resolution when necessary to give effect to an arbitration agreement." *Moses H. Cone Memorial Hosp., 460 U.S. at 20*.

B. The Arbitration Agreement

Plaintiffs Slatnick and Sonnenberg each executed a four page Account Agreement, containing at its section 19, captioned **"Arbitration,"** the following three paragraphs of text:

> **I understand that: (1) Arbitration is final and binding on the parties. (2) The parties are waiving their right to seek recourse in court, including the right to jury trial.** (3) Pre-arbitration discovery [*12] is generally more limited than and different from court proceedings. (4) The arbitrator's award is not required to include factual findings or legal reasoning and any party's right to appeal or to seek modifications of rulings by the arbitrator is strictly limited. (5) The panel of arbitrators would typically include a [illegible] of arbitrators who were or are [illegible] with the [illegible] 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 [illegible] Regulation, Inc., at my election. I agree that I shall make my selection by registered mail to you..., 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. [*13]
>
> Neither you nor I waive any right to seek equitable relief pending arbitration. **No person shall** bring a putative or certified 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 putative class action until (I) 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.

McLeod Decl. Exhs. 2, 3, P 19 (emphasis added).

The Account Agreement defines the terms "I," "me," "my," "we," and "us," and "the undersigned" as referring to "the person(s) whose signatures appear(s) below and all others who are legally obligated on the account." McLeod Decl. Exhs 2, 3, preamble paragraph at p. 1. "'My Accounts' shall mean each and every account in the name of the undersigned and each and every account in which the undersigned may have [*14] an interest." Id. "'You,' and 'your' refer to DB Alex Brown LLC, its subsidiaries, affiliates, officers, directors, agents and employees. DB Alex Brown LLC is a subsidiary of Deutsche Bank AG." Id. One of the Account Agreement exhibits is signed by plaintiff Slatnick and the other by plaintiff Sonnenberg.

The concluding paragraph of the Account Agreement is headed: "22a. Certification" and contains, in pertinent part, the following language (capital letters in original): "BY SIGNING BELOW I ACKNOWLEDGE THAT I HAVE RECEIVED, READ AND AGREE TO THE TERMS OF THIS AGREEMENT," and the notation above the signature line: "THIS AGREEMENT CONTAINS A PRE-DISPUTE ARBITRATION CLAUSE AT PARAGRAPH 19." McLeod Decl. Exhs. 2, 3.

C. The Arbitration Agreement Is Valid, Enforceable For Purposes Of Referral To An Arbitrator, And Encompasses Plaintiffs' Dispute With The Deutsche Bank Defendants

With the pending class action impediment to enforcement of the arbitration agreement removed by dismissal of both the Ling and the Stearns putative class actions, the FAA requires the court to examine the validity of the arbitration agreement and the applicability of the arbitration [*15] agreement to the claims in this controversy.

1. Validity And Enforceability Of Arbitration Agreement

Federal courts generally apply state law principles governing the formation of contracts in determining whether the parties agreed to arbitrate a particular dispute. *See, e.g., First Options, 514 U.S. 938, 115 S. Ct. 1920, 131 L. Ed. 2d 985.* An agreement to arbitrate, like any other contact, must be construed to give effect to the intent of the parties. *See Victoria v. Superior Court, 40 Cal.3d 734, 739, 222 Cal. Rptr. 1, 710 P.2d 833 (1985); see also Lopez v. Charles Schwab & Co., Inc., 118 Cal.App.4th 1224, 1229, 13 Cal. Rptr. 3d 544 (2004)*

("While it is true that under the FAA, 'any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration,' ... that policy does not come into effect until a court has concluded that under state contract law, the parties entered into an agreement to arbitrate") (citation omitted). A motion to compel arbitration "is simply a suit in equity seeking specific performance of that contract." *Lopez, 118 Cal.App.4th at 1229.*

Nevertheless, the FAA creates a body of federal substantive law governing arbitrability. *Moses H. Cone Memorial Hosp., 460 U.S. at 22-24* [*16] (all questions as to the interpretation and enforceability of arbitration agreements subject to the FAA are determined by federal standards). The "parties' inclusion of a choice of law clause in the arbitration agreement does not incorporate state decisional law pertaining to the allocation of power between courts and arbitrators." *Chiron Corp. v. Ortho Diagnostic Systems. Inc., 207 F.3d 1126, 1130 (9th Cir. 2000).*

Plaintiffs argue "there is no valid agreement to arbitrate." Opp. 5:5. They attack the validity of the entire Account Agreement as procedurally unconscionable, substantively unconscionable, and void because it was purportedly drafted for an illegal purpose and was induced by fraud, rendering the arbitration clause "unenforceable." Opp. pp. 5-13; Opp. 6:14-18.

> "If a contract includes an arbitration agreement, and grounds exist to revoke the entire contract, such grounds vitiate the arbitration agreement. Thus if an otherwise enforceable arbitration provision is **contained in an illegal contract,** a party may avoid arbitration altogether."

Opp. 10:2-6 (emphasis added), *quoting Moncharsh v. Heily Blase, 3 Cal.4th 1, 5, 10 Cal. Rptr. 2d 183, 832 P.2d 899 (1992).* [*17]

Relying on California law, Plaintiffs further contend: "Allegations in a complaint regarding the illegality of the underlying contract are sufficient to defeat a motion to compel arbitration.'" n3 Opp. 10:9-10, *citing Bianco v. Superior Court, 265 Cal.App.2d 126, 130-31, 71 Cal. Rptr. 322 (1968).* They rely on *Green v. Mt. Diablo Hosp. Dist., 207 Cal.App.3d 63, 66, 254 Cal. Rptr. 689 (1989)* for the proposition:

> A petition to compel arbitration is properly denied where there are sufficient grounds alleging illegality of the underlying agreement. The allegations, if proven, would render the entire contract void.

Opp. 10:11-16.

> n3 Despite the choice of law provision in the Account Agreements at paragraph 20 selecting New York slate law, Plaintiffs rely on California cases to support their contentions. A generic choice-of-law clause does not by itself displace the FAA rules. *See Sovak v. Chugai Pharm. Co., 280 F.3d 1266, 1269 (9th Cir. 2002).* As a threshold matter, the FAA applies if, among other things, the contract requires dispute resolution"by arbitration." *Portland Gen. Elec. Co. v. United States Bank Trust Nat'l Ass'n as Trustee for Trust No. 1, 218 F.3d 1085, 1089 (9th Cir. 2000).*

Plaintiffs assert "the Complaint alleges detailed facts regarding the illegality of Deutsche Bank's tax shelters" sufficient to show illegal purpose. Opp. 10:8-20. They insist "the underlying contact [was] a sham agreement to open a securities account solely for the purpose of generating 'paper losses' as part of an abusive tax shelter." Opp. 11:14-16. "'[A] well founded claim that an arbitration agreement resulted from ... fraud' that would provide grounds for the revocation of any contract may prevent enforcement of an arbitration agreement. [*18] " Opp. 11:7-9 (citation omitted).

The United States Supreme Court recently clarified that an arbitrator rather than a court should decide the claim that a contract containing an arbitration provision is void for illegality. In *Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362 (U.S. Fla. Feb. 21, 2006)*, the Supreme Court held an arbitrator should make that determination in cases such as this, where Plaintiffs challenge not merely the validity of the agreement to arbitrate (*see, e.g., Southland Corp. v. Keating, 465 U.S. 1, 4-5, 104 S. Ct. 852, 79 L. Ed. 2d 1 (1984)*), but the contact as a whole. *Buckeye Check, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362 at *3.* A challenge to the contract as a whole, warranting referral to an arbitrator, may be made "either on a [*19] ground that directly affects the entire agreement (*e.g.*, the agreement was fraudulently induced), or on the ground that the illegality of the contract's provisions renders the whole contract invalid." Id. In *Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 87 S. Ct. 1801, 18 L. Ed. 2d 1270 (1967)*, the high Court addressed "the question of who -- court or arbitrator -- decides these two types of challenges." *Buckeye Check, 549 U.S. 440, 2006 WL 386362 at *3* (Prima Paint presented the issue

"'whether a claim of fraud in the inducement of the entire contract is to be resolved by the federal court, or whether the matter is to be referred to the arbitrators"), *quoting Prima Paint, 388 U.S. at 403-04.* "[I]f the claim is fraud in the inducement of the arbitration clause itself an -- issue which goes to the making of the agreement to arbitrate -- the federal court may proceed to adjudicate it. But the [FAA] statutory language does not permit the federal [*20] court to consider claims of fraud in the inducement of the contract generally." *Prima Paint, 388 U.S. at 403-04.*

> Subsequently, in Southland Corp., we held the FAA "create[d] a body of federal substantive law," which was "applicable in state and federal court." ... We rejected the view that state law could bar enforcement of *§ 2*, even in the context of state-law claims brought in state court.

*Buckeye Check, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362 at *3, quoting Southland Corp., 465 U.S. at 12.*

> Prima Paint and Southland answer the question presented here by establishing three propositions. First, as a matter of substantive federal arbitration law, an arbitration provision is severable from the remainder of the contract. Second, unless the challenge is to the arbitration clause itself, the issue of the contract's validity is considered by the arbitrator in the first instance. Third, this arbitration law applies in state as well as federal courts.

*Buckeye Check, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362 at *4* (concluding "that because respondents challenge the Agreement, but not specifically its arbitration provisions, those provisions [*21] are enforceable apart from the remainder of the contract, [and] [t]he challenge should therefore be considered by an arbitrator, not a court").

Plaintiffs in this case attempt to cover all bases. The court finds the gist of the Complaint is that the transactions and business relationship embodied in the Account Agreements are illegal. Their primary arguments are that "the contract containing the arbitration provision is unconscionable" and "*the contract* is void because it was drafted for an illegal purpose." Opp. pp. 6, 10 (emphasis added). Under *Buckeye Check* and the cases cited therein, those challenges render the matter properly referable to an arbitrator for resolution. Plaintiffs also argue the "arbitration provision" is "procedurally unconscionable" because they were purportedly given "no opportunity to negotiate the terms of the provision," they were "not provided a copy of the rules of the NASD or the NYSE," and because "it is buried in a pre-printed form drafted by Deutsche Bank," as well as "substantively unconscionable" because the arbitrator choices are purportedly too narrow. Opp. pp. 6-9. They further summarily argue the arbitration provision, like the contract [*22] as a whole, resulted from fraud, without elaborating with any specificity how they were wrongfully induced to agree to arbitrate claims arising out of their Account Agreements. They attempt to avoid personal responsibility for the contract formation by alleging they were "never told the documents" they signed were anything but "mere formalities." Opp. p. 11. Despite their signatures on the Account Agreements, they contend they had "no notice of their contents, no opportunity to negotiate their terms, nor any ability to choose a different broker...." Opp. pp. 11- 12. They argue "it is impossible for Defendants to attempt to enforce the terms of the account agreements" under these circumstances (Opp. 12:4-7 (emphasis added)), presumably referring to the arbitration provision as well as any other of Plaintiffs' Account Agreement obligations. Plaintiffs' challenge that the arbitration provision is fraudulent and unenforceable is thus inextricably intertwined with their attack on the validity of the entire Account Agreement.

To the extent the court can adjudicate the arbitration clause as "severable from the rest of the contract" (*Buckeye Check,. 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362 at *4),* [*23] the court finds the arbitration agreement terms are prominent, are elaborated in three separate paragraphs, describe expressly the significant differences between arbitration and litigation in a court of law, identify the choice of rules Plaintiffs have the right to select from, and should be held unenforceable only if the entire contract is void for illegality, a determination left to the arbitrator. The court rejects Plaintiffs' characterization the clause is "buried in a pre-printed form," particularly because just above the signature line, in capital letters, the signatories are reminded the Account Agreement contains an "ARBITRATION CLAUSE AT PARAGRAPH 19." The court must give effect to the FAA policy favoring arbitration. *See Three Valleys Municipal Water Dist. v. E.F. Hutton, 925 F.2d 1136, 1140-41 (9th Cir. 1991)* (courts decide the existence of an agreement to arbitrate). The validity of the Account Agreements must be decided by an arbitrator in the first instance. *See Buckeye Check, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038, 2006 WL 386362.*

2. Scope Of Arbitration Agreement

When there is a dispute as to the scope of the arbitration agreement, the court makes the [*24] factual determinations whether the arbitration provision in a contract is to be construed under the FAA and whether the scope of the arbitration agreement encompasses the particular dispute. "[A]mbiguities as to the scope of the arbi-

tration clause itself [must be] resolved in favor of arbitration." *Volt Information Sciences v. Board of Trustees of the Leland Stanford Jr. Univ., 489 U.S.468, 475-76, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989).*

Plaintiffs contend, even were the court to give effect to the arbitration provision, their claims in the controversy with the Deutsche Bank Defendants are beyond the scope of that provision, relieving them of any obligation to resolve their disputes through arbitration. They narrowly construe their claims as unrelated to the "paper transactions" that took place through DB Alex Brown (*i.e.,* the foreign currency trades) under the Account Agreements, and argue "Deutsche Bank [are] non signatories to the 'Account Agreements' between DB Alex Brown and Plaintiffs." Opp. 12:11-23. However, the Account Agreements expressly identify DB Alex Brown as "a subsidiary of Deutsche Bank AG." McLeod Decl. Exhs. 2, 3 p. 1. In addition, the language of the arbitration clauses in this [*25] case (*i.e.,* manifesting an agreement to arbitrate "**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**" (Account Agreement P19 (emphasis added)) is much broader in scope than Plaintiffs' "paper transaction" characterization suggests. In an action to compel arbitration, the court's function in determining scope is confined to ascertaining whether the claim, on its face, is governed by an enforceable selection of arbitration as the forum for dispute resolution. *See Prima Paint Corp., 388 U.S. 395, 87 S. Ct. 1801, 18 L. Ed. 2d 1270.*

Applying the FAA's liberal construction of arbitration agreements, the court finds this agreement on its face encompasses any claim arising from the parties' transactions and contractual relationship, the Plaintiffs' allegations arise from their contractual relationship with the Deutsche Bank Defendants, and an adequate foundation exists to compel the parties to arbitrate their disputes. The court's findings [*26] on its limited inquiry into whether there is an agreement to arbitrate and whether there are arbitrable claims, and absent any evidence the moving parties waived their right to arbitrate conferred by the Account Agreements, dictate the Motion should be granted. *See Chiron Corp., 207 F.3d at 1130.*

III. CONCLUSION AND ORDER

For the foregoing reasons, **THE COURT HEREBY ENFORCES AND ORDERS COMPLIANCE WITH** the arbitration agreement pursuant to the FAA, and **GRANTS** the Deutsche Bank Defendants' Motion To Compel Arbitration. Plaintiffs and the moving defendants shall proceed to arbitration under the terms of their agreement, and the action is stayed as to the Deutsche Bank Defendants until such arbitration has been had, as required under *FAA § 3.*

IT IS SO ORDERED.

DATED: 3-14-06

HONORABLE LARRY ALAN BURNS

United States District Judge

EXHIBIT C

LEXSEE 2003 U.S. DIST. LEXIS 6925

VETCO SALES, INC., Plaintiff and Counter-Defendant, VS. VANCE VINAR, SR., ET AL., Defendants, Counter-Plaintiffs, and Third-Party Plaintiffs, VS. TROY MURPHY, Third-Party Defendant.

CIVIL ACTION NO. 3:02-CV-1767-K

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION

2003 U.S. Dist. LEXIS 6925

April 23, 2003, Decided
April 23, 2003, Filed

SUBSEQUENT HISTORY: Affirmed in part and remanded in part by *Vetco Sales, Inc. v. Vinar, 2004 U.S. App. LEXIS 1248 (5th Cir. Tex., Jan. 28, 2004)*

DISPOSITION: [*1] Motion of the defendants for a plea in abatement pending arbitration denied. Plaintiff's and third-part defendant Murphy's motions to dismiss for failure to state a claim denied, and their motions for a more definite statement granted. Murphy's motion to dismiss pursuant to *Federal Rule of Civil Procedure 9(b)* denied as moot.

COUNSEL: For Vetco Sales Inc, PLAINTIFF: Braden W Sparks, Law Office of Braden W Sparks, Craig Buck Florence, Robert T Slovak, Gardere Wynne Sewell, Dallas, TX USA.

For Vance Vinar, Barbara A Vinar, Cable Connection & Supply Co, Inc, DEFENDANTS: Gary E Smith, Graham Bright & Smith, Dallas, TX USA.

For Vance Vinar, Barbara A Vinar, Cable Connection & Supply Co, Inc, Thirdparty PLAINTIFFS: Gary E Smith, Graham Bright & Smith, Dallas, TX USA.

For Troy Murphy, Thirdparty DEFENDANT: Braden W Sparks, Law Office of Braden W Sparks, Craig Buck Florence, Robert T Slovak, Gardere Wynne Sewell, Dallas, TX USA.

For Vance Vinar, Barbara A Vinar, Cable Connection & Supply Co, Inc, Counter CLAIMANTS: Gary E Smith, Graham Bright & Smith, Dallas, TX USA.

For Vetco Sales Inc, Counter DEFENDANT: Braden W Sparks, Law Office of Braden W Sparks, Craig Buck Florence, Robert T Slovak, Gardere Wynne [*2] Sewell, Dallas, TX USA.

JUDGES: ED KINKEADE, UNITED STATES DISTRICT JUDGE.

OPINION BY: ED KINKEADE

OPINION:

MEMORANDUM ORDER

Before the court are the following motions: (1) the motion of the defendants Vance Vinar, Sr. ("Vinar"), Barbara A. Vinar ("Barbara"), and Cable Connection & Supply Company, Inc. ("Cable Connection") (collectively, "the defendants") for a plea in abatement pending arbitration; (2) the motions of the plaintiff Vetco Sales, Inc. ("Vetco") and the third-party defendant Troy Murphy ("Murphy") to dismiss the defendants' counterclaims for failure to state a claim or, in the alternative, for a more definite statement; and (3) the motion of Murphy to dismiss for failure to plead fraud with particularity. For the reasons discussed below, the motion of the defendants is DENIED. The motions of Vetco and Murphy to dismiss for failure to state a claim are also DENIED but their motions for a more definite statement are GRANTED. Murphy's remaining motion is DENIED as moot.

Factual Background

Vetco and Cable Connection sell telecommunication products. Vetco is owned by Murphy and Cable Connection is owned by Vinar and Barbara. On October 18, 1999, Murphy -- hoping to secure [*3] additional capital -- sold Vinar a 49% ownership interest in Vetco and gave Vinar a seat on the board of directors. According to Vetco, following the execution of the Shareholder

Agreement, disputes arose among Vetco, Cable Connection, Vinar, and Murphy regarding the management, bookkeeping, and administration of Vetco.

Unable to resolve these disputes, Vetco, Murphy, Vinar, and Cable Connection agreed to end their business relationship. On April 26, 2002, Vinar sold his Vetco ownership interest back to Murphy and relinquished his seat on Vetco's board of directors. According to the plaintiffs, the defendants materially breached the Buyout Agreement by failing to provide adequate administrative services during a contractually defined transition period and by refusing to deliver certain records and other property. On July 19, 2002, Vetco sued in a Texas state court. On August 16, 2002, the defendants filed a counterclaim, removed this case to this Court, and moved to compel arbitration.

Defendants' Motion for Plea in Abatement Pending Arbitration

Applicable Law

In considering whether a dispute is subject to binding arbitration, the first step a court must take "is to determine [*4] whether the parties agreed to arbitrate that dispute." *Mitsubishi Motors Corporation v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626, 87 L. Ed. 2d 444, 105 S. Ct. 3346 (1985)*. In general, this determination is made by "applying the federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the [Federal Arbitration] Act." *Id.* (quoting *Moses H. Cone Memorial Hospital v. Mercury Construction Corporation, 460 U.S. 1, 24, 74 L. Ed. 2d 765, 103 S. Ct. 927 (1983))* (internal citations omitted). Here, the court sees no reason not to apply federal law in its analysis of whether this case is subject to arbitration. Neither party has argued that the *Federal Arbitration Act* ("FAA") does not apply to this dispute and the case appears to come within the FAA's purview. *See 9 U.S.C. § 1 et seq.*

Legal Standard

Federal law strongly favors arbitration. *Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 56, 131 L. Ed. 2d 76, 115 S. Ct. 1212 (1995)* (the FAA "declared a national policy favoring arbitration.") (quoting *Southland Corporation v. Keating, 465 U.S. 1, 10, 79 L. Ed. 2d 1, 104 S. Ct. 852 (1984))*; [*5] *Moses H. Cone Memorial Hospital, 460 U.S. at 24-25* ("*The Arbitration Act* establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability."). Consequently, the FAA, by its terms, "leaves no place for the exercise of discretion by a district court, but instead mandates that district courts shall direct the parties to proceed to arbitration on issues as to which an arbitration agreement has been signed." *Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213, 218, 84 L. Ed. 2d 158, 105 S. Ct. 1238 (1985)*.

To decide whether parties should be compelled to arbitrate their dispute, the Fifth Circuit has developed a two-prong inquiry. *OPE International LP. v. Chet Morrison Contractors, Inc., 258 F.3d 443, 445-46 (5th Cir. 2001)*. The first prong requires the court to determine whether "the parties agreed to arbitrate their dispute." *Id. at 445*. Two considerations guide the court in resolving this determination: [*6] (1) whether a valid agreement to arbitrate exists between the parties; and (2) whether the dispute is within the scope of the arbitration agreement.*Id.* Under the second prong, the court must ensure that no legal restraints external to the agreement have foreclosed arbitration. *Id.* If the court finds this two-prong inquiry is satisfied, arbitration is mandatory. *Mitsubishi Motors, 473 U.S. at 628*. Here, the court's analysis need only reach the first prong.

Agreement to Arbitrate their Dispute?

The determinative issue in the defendants' motion to compel arbitration is whether the arbitration clause contained in the Shareholder Agreement applies to Vetco's claims. Arguing in the affirmative, the defendants' motion to compel arbitration boldly quotes, without further support, the entire arbitration clause contained in the Shareholder Agreement. Vetco counters that its claims fall outside the scope of the arbitration clause and, moreover, that the arbitration clause was rendered inoperative by the Buyout Agreement, which itself does not contain an arbitration clause. Resolving this dispute is a matter of contract interpretation.

The court must interpret [*7] whether a contract's arbitration clause applies to a given dispute. *AT&T Technologies, Inc. v. Communications Workers of America, 475 U.S. 643, 649, 89 L. Ed. 2d 648, 106 S. Ct. 1415 (1986)*. The court's interpretative function must be carried out with appropriate deference to the federal policy that favors arbitration over litigation and requires arbitration clauses to be construed generously, in favor of arbitration. *Southland Corporation v. Keating, 465 U.S. 1, 10-11, 79 L. Ed. 2d 1, 104 S. Ct. 852 (1984)*; *ASW Allstate Painting & Construction Company, Inc. v. Lexington Insurance Company, 188 F.3d 307, 311 (5th Cir. 1999)* ("The party opposing arbitration bears the burden of proving that no valid arbitration agreement exists as to the dispute.") (construing Texas law). However, despite judicial deference to arbitration, a party may not be required to arbitrate a dispute it did not agree to arbitrate, *Neal v. Hardee's Food Systems, Inc., 918 F.2d 34, 37 (5th Cir. 1990)*, and the controversy must come within

the contract's arbitration provision before the court can order arbitration. *Explo, Inc. v. Southern Natural Gas Compnay, 788 F.2d 1096, 1098 (5th Cir. 1986).* [*8]

The defendants point to the arbitration clause in the Shareholder Agreement, which mandates arbitration of "each dispute, claim and controversy (whether arising during or after the term hereof) *arising out of* this Agreement or breach thereof (including but not limited to the validity of the agreement to arbitrate and the arbitrability of any matter) shall be settled, upon demand and written notice by an arbitrator agreed upon by the parties." Shareholder Agreement P 8.1 (emphasis added). To assist in determining the scope of an arbitration clause, courts have distinguished between "narrow" and "broad" arbitration clauses. *Pennzoil Exploration and Production Company v. Ramco Energy Limited, 139 F.3d 1061, 1067 (5th Cir. 1998)* (citing *Tracer Research Corp. v. National Envtl. Svcs. Co., 42 F.3d 1292, 1295 (9th Cir. 1994), cert, dismissed, 515 U.S. 1187, 132 L. Ed. 2d 917, 116 S. Ct. 37 (1995)).* When an arbitration clause requires arbitration of disputes "arising out of" the agreement, the arbitration clause is deemed narrow and correspondingly restricts arbitration to those disputes that literally arise from the contract. *Pennozil Exploration, 139 F.3d at 1067*; [*9] *see, e.g., Coffman v. Provost * Umphrey Law Firm, LLP, 161 F. Supp. 2d 720, 725 (E.D. Tex. 2001)* (holding that phrase "arising out of," absent broader language, requires arbitration of only those claims that literally arise under the contract); *Beckham v. William Bayley Company, 655 F. Supp. 288, 291 (N.D. Tex. 1987)* (ruling the absence of a standard broad arbitration clause demonstrates the parties' intent to limit arbitration to a narrow scope). Conversely, when an arbitration clause contains the language "in connection with" or "relating to," the arbitration clause is characterized as broad. *Pennozil Exploration, 139 F.3d at 1067.* A broad arbitration clause encompasses "all disputes between the parties having a significant relationship to the contract regardless of the label attached to the dispute."*Id.* (footnote omitted); *see, e.g., Bloxom v. Landmark Publishing Corporation, 184 F. Supp. 2d 578, 583-84 (E.D. Tex. 2002).*

Here, because the arbitration clause of the Shareholder Agreement employs only the language "arising out of" without the broader terms "in connection with" or "relating to," the arbitration [*10] clause is a narrow clause, applying only to those disputes that literally arise from the Shareholder Agreement. *See United Offshore Company v. Southern Deepwater Pipeline Company, 899 F.2d 405, 409-410 (5th Cir. 1990).* Because the parties intended the Shareholder Agreement's arbitration clause to have a narrow scope that applies only to those disputes related to the Shareholder Agreement's subject matter, the court must now determine whether Vetco's claims relate to that subject matter.

The Shareholder Agreement's arbitration clause is interpreted according to contract principles and enforced according to its plain meaning. *See Neal, 918 F.2d at 37.* The defendants assert that the Buyout Agreement arose out of the Shareholder Agreement and thus should be viewed as "inexorably intertwined with the Shareholders' Agreement. After a careful analysis of the entire Shareholder Agreement, however, the Court finds this agreement was executed solely to delineate the restrictions governing Vetco stock. *See Neal, 918 F.2d at 37.* Indeed, the Shareholder Agreement's preamble states, "Vinar and Murphy desire to enter into an agreement providing [*11] for the restrictions on [the] transfer of the shares of [Vetco] on the death of or sale by a shareholder, and to provide for the management and control of [Vetco]." This specific purpose, coupled with the narrow scope of the Shareholder Agreement's arbitration clause, limits the arbitration clause's applicability to only those disputes arising from restrictions governing Vetco stock. And a review of Vetco's claims in this case demonstrates that none of Vetco's causes of action implicate the restrictions imposed by the Shareholder Agreement. *Compare* Complaint PP 74-108, *with* Shareholder Agreement P 8.1. Therefore, because the Shareholder Agreement's arbitration clause is a creature of contract and may not be stretched beyond the scope intended by the parties, *see E.E.O.C. v. Waffle House, Inc., 534 U.S. 279, 294, 151 L. Ed. 2d 755, 122 S. Ct. 754 (2002),* this Court concludes that Vetco's claims fall outside the scope of the arbitration clause and are accordingly not subject to arbitration.

Vetco's and Murphy's Motion to Dismiss the Defendants' Counterclaims for Failure to State a Claim or, Alternatively, for a More Definite Statement

Standard for [*12] *Dismissal Under Rule 12(b)(6)*

Federal Rule of Civil Procedure 12(b)(6) authorizes dismissal of a complaint for "failure to state a claim upon which relief can be granted." *FED. R. CIV. P. 12(b)(6).* However, a motion under *Rule 12(b)(6)* should be granted only if it appears beyond doubt that the plaintiffs could prove no set of facts in support of their claims that would entitle them to relief. *Conley v. Gibson, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957); Leffall v. Dallas Independent School District, 28 F.3d 521, 524 (5th Cir. 1994); see also Kaiser Aluminum & Chemical Sales, Inc. v. Avondale Shipyards, Inc., 677 F.2d 1045, 1050 (5th Cir. 1982)* (citing WRIGHT & MILLER, Federal Practice and Procedure: Civil § 1357 at 598 (1969), for proposition that "the motion to dismiss for failure to state a claim is viewed with disfavor and is rarely granted"), *cert. denied, 459 U.S. 1105, 74 L. Ed. 2d 953, 103 S. Ct. 729 (1983).* In determining whether dismissal

should be granted, the court must accept all well-pleaded facts as true and view them in the light most favorable to the plaintiffs. *See Capital Parks, Inc. v. Southeastern Advertising and Sales System, Inc., 30 F.3d 627, 629 (5th Cir. 1994)*; [*13] *Norman v. Apache Corporation, 19 F.3d 1017, 1021 (5th Cir. 1994)*; *Chrissy F. by Medley v. Mississippi Department of Public Welfare, 925 F.2d 844, 846 (5th Cir. 1991)*. Yet, if it appears that a more carefully drafted complaint might state a claim upon which relief could be granted, the court should give the plaintiff an opportunity to amend the complaint rather than dismiss it. *Friedlander v. Nims, 755 F.2d 810, 813 (11th Cir. 1985)*; *see also Dussouy v. Gulf Coast Investment Corporation, 660 F.2d 594, 597-99 (5th Cir. 1981)*.

Murphy and Vetco's Grounds for Dismissal

Although a pleading need only contain a "short and plain statement of the claim showing that the pleader is entitled to relief," *FED. R. CIV. P. 8(a)(2)*, the defendants' counterclaim stretches the limits of even this liberal standard. The defendants' eighteen count counterclaim is supported by only four sentences. *See* Defendants' Original Answer and Counterclaim ("Counterclaim"), *attached to* Notice of Removal. The first two sentences set forth the closing dates for both the Shareholder Agreement and the Buyout Agreement. The third sentence recites [*14] Murphy's fiduciary duty as an officer of Vetco. The fourth and final sentence, in model conclusory language, asserts that "Murphy has mismanaged the affairs of Vetco and misallocated funds belonging to Vetco by various means including, without limitation, padding expense accounts, diverting funds and the like." *Id. P 7.*

Even the most generous reading of this skeletal complaint cannot overcome the complete lack of any facts supporting the defendants' causes of action. See S&W Enterprises, LLC. v. Southtrust Bank of Alabama, NA., 2001 U.S. Dist. LEXIS 25195, 2001 WL 238095, at *4 (2001) (Lindsay, J.); *see also Balistreri v. Pacifica Police Department, 901 F.2d 696, 699 (9th Cir. 1990)* ("Dismissal can be based on the lack of a cognizable legal theory or the absence of sufficient facts alleged under a cognizable legal theory."). Accordingly, the Court finds the defendants have failed to state a claim upon which relief may be granted. However, the Court appreciates that dismissal should be avoided until the defendants have been afforded an opportunity to file an amended complaint. *Hitt v. City of Pasadena, 561 F.2d 606, 608 (5th Cir. 1977)*; [*15] *cf. DeLoach v. Woodley, 405 F.2d 496, 497 (5th Cir. 1968)*. Therefore, the motions of Vetco and Murphy to dismiss for failure to state a claim must be denied and the motions for a more definite statement granted. The defendants shall have leave to replead their counterclaims -- if they can -- to satisfy the pleading requirements of *Rule 8(a)(2)*.

Conclusion

For the reasons discussed above, the motion of the defendants for a plea in abatement pending arbitration is **DENIED.** Vetco's and Murphy's motions to dismiss for failure to state a claim are **DENIED** but their motions for a more definite statement are **GRANTED.** The defendants shall have leave to file and serve, not later than May 23, 2003, an amended complaint to remedy the *Rule 8(a)(2)* deficiencies in their counterclaims against Vetco and Murphy; otherwise, those counterclaims will be deemed dismissed without further notice. If the defendants duly amend their counterclaim complaint, Vetco and Murphy may reassert their motions to dismiss if they believe the amended counterclaim complaint fails to cure the defects in the defendants' original counterclaim complaint. Murphy's motion to dismiss [*16] pursuant to *Federal Rule of Civil Procedure 9(b)* is **DENIED** as moot.

SO ORDERED.

April 23nd, 2003.

ED KINKEADE

UNITED STATES DISTRICT JUDGE

FILED
COURT OF APPEALS
DIVISION II

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STATE OF WASHINGTON
BY_____
DEPUTY

COURT OF APPEALS, DIVISION II
OF STATE OF WASHINGTON

LARRY NELSON, and the marital community composed of LARRY NELSON and BARBARA NELSON,

Respondents,

v.

WESTPORT SHIPYARD, INC., a Washington corporation, J. ORIN EDSON, individually and his marital community composed of ORIN and CHARLENE EDSON; DARYL WAKEFIELD, individually, and his marital community composed of DARYL and KIM WAKEFIELD,

Appellants.

NO. 35308-3-II

CERTIFICATE OF SERVICE

ORIGINAL

I certify that on the 28 day of February, 2007, I caused the following document(s):

RESPONDENTS' BRIEF

to be delivered to the following person in the manner described:

Gail E. Mautner
D. Michael Reilly
Sarah E. Haushild
Lane Powell PC
1420 Fifth Avenue, Suite 4100
Seattle, WA 98101-2338

By ABC Legal Messenger

I declare under penalty of perjury of the laws of the state of Washington that the foregoing is true and correct.

Dated this 28th day of February, 2007, at Tacoma, Washington.

Becky J. Niesen