EFiled: Mar 28 2013 04:18PM EDT
Transaction ID 51375122
Case No. 8191-VCN

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

ANSHAN (ANDY) LI,	:	
	:	
Plaintiff,	:	
	:	
v.	:	**C.A. No. 8191-VCN**
	:	
STANDARD FIBER, LLC,	:	
	:	
Defendant.	:	

MEMORANDUM OPINION

Date Submitted: March 8, 2013
Date Decided: March 28, 2013

A. Thompson Bayliss, Esquire and Adam K. Schulman, Esquire of Abrams & Bayliss LLP, Wilmington, Delaware, Attorneys for Plaintiff.

Daniel B. Rath, Esquire, James S. Green, Jr., Esquire, K. Tyler O'Connell, Esquire, and Joseph D. Wright, Esquire of Landis Rath & Cobb LLP, Wilmington, Delaware, and Howard O. Godnick, Esquire and Justin Mendelsohn, Esquire of Schulte Roth & Zabel LLP, New York, New York, Attorneys for Defendant.

NOBLE, Vice Chancellor

Plaintiff Anshan (Andy) Li ("Li") brought this action against Defendant Standard Fiber, LLC ("Standard Fiber" or the "Company") to enforce his right to advancement of legal fees and expenses arising under an indemnification agreement between Standard Fiber and Li (the "Indemnification Agreement"). Li requests that the Court order Standard Fiber to advance expenses and fees incurred in an arbitration proceeding in California between the two parties (the "California Arbitration"). Li also seeks an order that "Standard Fiber indemnify Li for all legal fees and expenses incurred in [prosecuting] this action."[1] Standard Fiber has moved to dismiss the complaint for lack of subject matter jurisdiction, or alternatively, to stay the action in favor of arbitration.

The Court examines the threshold question of who decides arbitrability—the Court or an arbitrator. Because the test set forth in *Willie Gary*[2] is satisfied, the Court holds that an arbitrator must determine whether Li's claims are subject to arbitration. For that reason, the Court does not delve deeply into the parties' contentions as to whether Li's advancement and indemnification claims are subject to arbitration, and declines to resolve a dispute over ripeness—a dispute which, if not already easily resolvable, will likely be essentially moot in a matter of days. Accordingly, the Court will grant Standard Fiber's motion to stay.

[1] Verified Compl. ("Compl.") ¶ 3.
[2] *James & Jackson, LLC v. Willie Gary, LLC*, 906 A.2d 76 (Del. 2006).

I. BACKGROUND

A. *The Parties*

Li is the founder of Standard Fiber, Inc. ("SFI"), the predecessor to Standard Fiber, of which he is a 25% owner. In June 2006, SFI sold substantially all of its assets to the Company pursuant to an asset purchase agreement (the "APA"). From that time, Li served as the chief executive officer (CEO) of Standard Fiber until June 1, 2012.[3] Standard Fiber is a Delaware limited liability company which produces an assortment of bedding products, including sheets, pillow sets, and mattress pads.[4]

B. *The Parties' Agreements*

Non-party Standard Fiber Investors, LLC ("SF Investors") was formed by two private equity firms, RidgeView Capital LLC ("RidgeView") and WindRiver Group Companies, Ltd. ("WindRiver"), to pursue the acquisition of all of the assets of SFI.[5] Standard Fiber was expected to be both the purchasing entity in that transaction and the operating entity. Under the terms of the APA, which was executed on June 1, 2006, Li sold all of the assets of SFI to Standard Fiber in exchange for $44.5 million and a 25% interest in the Company.[6] Together,

[3] Compl. ¶ 4.
[4] *Id*. at ¶ 5.
[5] *Id*. at ¶¶ 6-7.
[6] Transmittal Aff. of Adam K. Schulman ("Schulman Aff.") Ex. 1 (Asset Purchase Agreement).

RidgeView and WindRiver own roughly 70.4% of Standard Fiber through their investment vehicle, SF Investors (the "controlling shareholders").[7]

The complaint focuses almost exclusively on the Indemnification Agreement and its relevant provisions. However, that agreement, which was executed on May 13, 2010, is the latest in a series of contracts executed between or among the parties.[8] The members of Standard Fiber (including Li) entered into a limited liability company agreement (the "LLC Agreement") on the same day that the APA was executed. Later, the parties entered into an employment agreement, dated October 28, 2008, that addressed Li's role as the CEO of Standard Fiber (the "Employment Agreement").[9] A brief overview of the four agreements between or among the parties is necessary for resolving Standard Fiber's motion. For convenience, the APA, LLC Agreement, and the Employment Agreement are collectively referred to as the "prior agreements."

First, the APA governs the terms of the Company's purchase of substantially all of the assets of SFI. Notably, it contains a broad arbitration provision:

> Any controversy or claim arising out of or relating to this Agreement, or the breach thereof, shall be settled by arbitration in San Francisco, California, by one (1) arbitrator . . . in accordance with the applicable arbitration rules and procedures of the Judicial Arbitration and Mediation Services . . . .[10]

[7] Compl. ¶ 6.
[8] Compl. Ex. A (Indemnification Agreement).
[9] Schulman Aff. Ex. 3 (Employment Agreement).
[10] Schulman Aff. Ex. 1 § 11.13. The arbitration clause's scope is cut back only slightly by Section 10.4, which permits the parties to seek injunctive or other equitable relief in "any court

It also contains an integration clause, which provides: "This Agreement . . . is complete, and all promises, representations, understandings, warranties and agreements with reference to the subject matter hereof, and all inducements to the making of this Agreement relied upon by all the parties hereto, have been expressed herein . . . ."[11]

Second, the LLC Agreement provides indemnification and advancement rights to the Company's managers, including Li, subject to certain limitations. Section 5.8(e) states, "Expenses, including attorneys' fees, or some part of such expenses, incurred by an Indemnified Party in defending any Action shall be paid by the Company in advance of the final disposition of such Action if a determination to make such payment is made on behalf of the Company . . . ."[12] Section 5.8(f) contains a non-exclusivity clause: "indemnification and advancement of expenses provided by this Section 5.8 shall not be construed to be exclusive of or limit any other rights to which any Indemnified Party or other person may be entitled under the Act, the Certificate, this Agreement or any other agreement . . . ."[13] Importantly, the LLC Agreement also contains an integration clause, which states that the LLC Agreement and the Certificate "comprise the

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of competent jurisdiction" if Section 10—which imposes various restrictive covenants upon Li—is breached. *See id*. at Ex. 1 §10.

[11] *Id.* at Ex. 1 § 11.12.

[12] *Id*. at Ex. 2 (the LLC Agreement) § 5.8(e).

[13] *Id*. at Ex. 2 § 5.8(f). The "Certificate" refers to the Certificate of Formation filed to organize the Company as a Limited Liability Company. *Id.* at Ex. 2 § 1.2(i).

entire agreement among the parties with respect to Membership Interest in, and the governance of, the Company" and "supersede any prior agreements or understandings with respect to the subject matter thereof."[14] The LLC Agreement also contains a mandatory arbitration provision, almost identical to the one set forth in the APA.[15]

Third, the Employment Agreement provides the terms of Li's employment as CEO of Standard Fiber. It contains an indemnification provision:

> During the term of this Agreement and thereafter, Standard Fiber shall defend and indemnify you for all your acts and failures to act while you were an officer or director of Standard Fiber and acting within the scope of your employment to the full extent permitted by law and subject to the terms of Standard Fiber's charter and by-laws . . . .[16]

The Employment Agreement also includes an integration clause, which states: "This agreement . . . represents the entire agreement between [the parties] concerning the subject matter of [Li's] employment by Standard Fiber."[17] The Employment Agreement also contains a mandatory arbitration agreement similar to the arbitration clauses in the APA and LLC Agreement:

> The parties agree that any dispute regarding the interpretation or enforcement of this agreement shall be decided by confidential, final and binding arbitration conducted by Judicial Arbitration and

[14] *Id*. at Ex. 2 § 9.8.
[15] *Id*. at Ex. 2 § 9.12. Importantly, the arbitration clause includes the broad language "Any controversy or claim arising out of or relating to this Agreement, or the breach thereof . . . ." and a specific reference to the "applicable arbitration rules and procedures of the Judicial Arbitration and Mediation Services ('*JAMS*') . . . ." *Id.*
[16] *Id*. at Ex. 3 § 9.
[17] *Id*. at Ex. 3 § 11(b).

> Mediation Services ("JAMS") in San Francisco, California under the then existing JAMS rules rather than by litigation in court, trial by jury, administrative proceeding or in any other forum.[18]

Fourth, the Indemnification Agreement provides Li a separate right to indemnification: the Company "shall indemnify [Li], if [he] is made a party . . . in any Derivative Action, against expenses, including attorney's fees . . . ."[19] Indeed, Li's right to indemnification is entitled to a strong presumption—the "Company shall have the burden of proof to overcome that presumption with clear and convincing evidence to the contrary."[20] The Indemnification Agreement also provides for a right to advancement: "the Company shall pay or advance all fees and related attorney expenses actually incurred by [Li] in connection with such Action within thirty (30) days after receipt by the Company of a statement requesting such advances . . . ."[21]

Like the prior agreements, the Indemnification Agreement contains an integration clause, which provides:

> Without limiting any of the rights of Indemnitee described in Section 3(b), this Agreement sets forth the entire agreement and understanding of the parties relating to the subject matter herein and merges all prior discussions and supersedes any and all previous agreements between them covering the subject matter herein.[22]

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[18] *Id*. at Ex. 3 § 10.
[19] Compl. Ex. A § 1(b).
[20] *Id*. at Ex. A § 2(c).
[21] *Id*. at Ex. A § 2(a).
[22] *Id*. at Ex. A § 13(b).

Section 3(b), titled "Nonexclusivity," makes clear that Li's rights conferred by any other agreement are preserved under the Indemnification Agreement. It provides: "The indemnification provided by this Agreement shall not be deemed exclusive of any rights to which [Li] may be entitled under the Company's Certificate, the LLC Agreement, any agreement . . . ."[23]

Unlike the prior agreements, however, the Indemnification Agreement does not contain an arbitration provision. Li argues that Section 2(c) contains a forum selection clause in favor of the Delaware Court of Chancery, but Standard Fiber strongly contests that characterization. The relevant portion of Section 2(c) follows:

> Upon final disposition of the Action and if it is determined that Indemnitee is successful on the merits [of] the claims, issues or matters in such Action, the Company shall pay any claims made under this Agreement within thirty (30) days after a written request for payment thereof has first been received by the Company, and if such claim is not paid in full within such thirty (30) day-period, Indemnitee may . . . bring an action against the Company in the Delaware Court of Chancery to recover the unpaid amount of the claim . . . . It shall be a defense to any such action (other than an action brought to enforce a claim for advancement of legal fees under Section 2(a)) that Indemnitee has not met the standards of conduct which make it permissible under applicable law for the Company to indemnify Indemnitee for the amount claimed.[24]

Indeed, the only reference to arbitration in the Indemnification Agreement is in Section 2(c), which in part states that "if the Company contests Indemnitee's right

[23] *Id*. at Ex. A § 3(b).
[24] *Id*. at Ex. A § 2(c).

to indemnification, the question of Indemnitee's right to indemnification shall be for an arbitrator or the court to decide . . . ."[25]

C. *The California Arbitration*

On behalf of Standard Fiber, the controlling shareholders of the Company initiated an arbitration proceeding against Li on August 20, 2012. The California Arbitration involves various claims by Standard Fiber against Li for breaching his fiduciary duties to the Company. Among the fifteen causes of action alleged, Standard Fiber charges Li with "engaging in improper self-dealing transactions with the factories in which he is alleged to have ownership interests, usurping corporate opportunities for his benefit, and wrongly converting and misappropriating Company funds."[26] Standard Fiber also alleges that Li failed to disclose his interests in certain Chinese manufacturers and suppliers when he sold SFI to Standard Fiber.[27] It seeks damages in excess of $100 million. Li has asserted various cross claims against the controlling shareholders, accusing them, among other things, of breaching the LLC and Employment Agreements.[28]

D. *Current Litigation*

Li's counsel made a formal demand for advancement and indemnification to counsel for Standard Fiber on October 1, 2012. After the parties conferred, a

[25] *Id*.
[26] Compl. ¶ 22.
[27] Compl. ¶ 29.
[28] *Id*. at ¶¶ 36-41.

second demand was made on October 18, 2012.[29] On November 19, 2012, Li also executed a good faith affirmation and undertaking in accordance with Section 2(a) of the Indemnification Agreement.[30] The parties continued to discuss Standard Fiber's obligation to advance litigation expenses to Li. Although no deal was reached, Li's counsel avers that counsel for Standard Fiber stated that Li did not need to submit invoices to Standard Fiber.[31] Counsel for Standard Fiber strongly disputes that statement. Li also argues that Standard Fiber was seemingly engaged in a "rope-a-dope strategy" as Standard Fiber never followed through with its alleged commitment to send a response to Li's most recent advancement proposal.[32]

Li filed his Verified Complaint on January 8, 2013. On February 7, Li submitted invoices for *all* of his expenses and fees incurred in the California Arbitration. Standard Fiber maintains that those invoices are not sufficient under Section 2(a) of the Indemnification Agreement to trigger the 30-day-waiting-period before it is obligated to advance Li his fees and expenses. It reasons that Li has not

[29] *See id*. at Ex. C.
[30] *See id*. at Ex. D. In his affirmation and undertaking, Li states that he believes that he has met the applicable standard of care in the Indemnification Agreement and promises that he will repay the monies advanced if it is ultimately determined that he is not entitled to indemnification.
[31] Affidavit of Stephen M. Knaster ("Knaster Aff.") ¶ 7.
[32] Pl.'s Answering Br. in Opp'n to Def.'s Mot. to Dismiss or Stay ("Pl.'s Br.") 11.

specified which invoices he seeks advancement for.[33] For that reason, Standard Fiber contends that the parties' dispute is not ripe.

II. ANALYSIS

A. *Applicable Standards*

Standard Fiber seeks dismissal of the complaint based on an arbitration clause which it contends mandates arbitration. "In considering a motion to dismiss for lack of subject matter jurisdiction, the court must address the nature of the wrong alleged and the remedy sought to determine whether a legal, as opposed to an equitable, remedy is available and adequate."[34] A Delaware court lacks "subject matter jurisdiction to resolve disputes that litigants have contractually agreed to arbitrate[,]"[35] because arbitration provides an adequate remedy. In light of Delaware's public policy favoring arbitration, and in recognition that "contractual arbitration clauses are generally interpreted broadly in furtherance of that

[33] Def. Standard Fiber, LLC's Reply Br. in Supp. of its Mot. to Dismiss or Stay ("Def.'s Reply Br.") 27.
[34] *Carder v. Carl M. Freeman Cmtys., LLC*, 2009 WL 106510, at *3 (Del. Ch. Jan. 5, 2009).
[35] *NAMA Hldgs., LLC v. Related World Mkt. Ctr., LLC*, 922 A.2d 417, 429 (Del. Ch. 2007) (citing *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 295 (Del. 1999)); *see also Julian v. Julian*, 2009 WL 2937121, at *3 (Del. Ch. Sept. 9. 2009) ("If a claim is arbitrable, *i.e.*, properly committed to arbitration, this Court lacks subject matter jurisdiction because arbitration provides an adequate legal remedy.").

policy[,]"[36] a Rule 12(b)(1) motion will be granted if the parties contracted to arbitrate the claims asserted in the complaint.[37]

In the alternative, and for the same reasons, Standard Fiber seeks a stay of this action in favor of arbitration. "This Court . . . possesses the inherent power to manage its own docket and may, on the basis of comity, efficiency, or common sense, issue a stay pending the resolution of an arbitration, even for those claims that are not arbitrable."[38]

Where, as here, a party's objective is to compel arbitration, a court must first consider the threshold issue of "whether . . . arbitrability should be decided by the court or the arbitrator . . . ."[39] If a court determines that it is entitled to decide, then it may consider "whether the claims should be resolved in arbitration . . . ."[40]

The Delaware Supreme Court affirmed in *Willie Gary*[41] that Delaware arbitration law parallels federal law, which presumes that the question of substantive arbitrability, *i.e.*, "whether the parties agreed to arbitrate[,] is generally

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[36] *Majkowski v. Am. Imaging Mgmt. Servs., LLC*, 913 A.2d 572, 581-82 (Del. Ch. 2006).

[37] The Delaware Supreme Court explained: "arbitration is a mechanism of dispute resolution created by contract. An arbitration clause, no matter how broadly construed, can extend only so far as the series of obligations set forth in the underlying agreement. Thus, arbitration clauses should be applied only to claims that bear on the duties and obligations under the Agreement. The policy that favors alternate dispute resolution mechanisms, such as arbitration, does not trump basic principles of contract interpretation." *Parfi Hldg. AB v. Mirror Image Internet, Inc.*, 817 A.2d 149, 156 (Del. 2002) (footnotes omitted).

[38] *Legend Natural Gas II Hldgs., LP v. Hargis*, 2012 WL 4481303, at *4 (Del. Ch. Sept. 28, 2012).

[39] *Id*.

[40] *Id*.

[41] *Willie Gary, LLC*, 906 A.2d at 79.

one for the courts to decide and not for the arbitrators."[42] That presumption is only overcome when there is "clear and unmistakable" evidence that the parties agreed to arbitrate.[43] The court held in *Willie Gary* that such clear evidence is present when an arbitration clause (1) "generally provides for arbitration of all disputes" and (2) "incorporates a set of arbitration rules that empower arbitrators to decide arbitrability."[44]

In an effort to avoid a senseless result, *Willie Gary*'s progeny has since modified the "clear and unmistakable" test in one important respect. Delaware courts have held that, even if the *Willie Gary* test is satisfied, a court must still "make a preliminary evaluation of whether the party seeking to avoid arbitration of arbitrability has made a clear showing that its adversary has made 'essentially no non-frivolous argument about substantive arbitrability.'"[45] As mentioned, this step

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[42] *Id.* (quoting *DMS Props.-First, Inc. v. P.W. Scott Assocs., Inc.*, 748 A.2d 389, 392 (Del. 2000)). In *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 945 (1995), the United States Supreme Court characterized the question of who should decide arbitrability as "arcane." It noted that a "party often might not focus upon that question or upon the significance of having arbitrators decide the scope of their own powers." *Id.* For that reason, the presumption is reversed in that situation. The "law treats silence or ambiguity about the question '*who* (primarily) should decide arbitrability' differently from the way it treats silence or ambiguity about the question '*whether* a particular merits-related dispute is arbitrable because it is within the scope of a valid arbitration agreement' . . . ." *Id.* at 944-45. Among other things, the term substantive arbitrability encompasses "the applicability of an arbitration clause" and "whether an arbitration clause is valid and enforceable." *Legend*, 2012 WL 4481303 at *4.

[43] *Willie Gary*, 906 A.2d at 79; *see also DMS Props.-First, Inc.*, 748 A.2d at 392 ("The question of whether the parties agreed to arbitrate is generally one for the courts to decide and not for the arbitrators.").

[44] *Willie Gary*, 906 A.2d at 80.

[45] *Legend*, 2012 WL 4481303, at *6. As the Court observed in *McLaughlin v. McCann*, 942 A.2d 616, 626-27 (Del. Ch. 2008), a party that seeks to avoid having an arbitrator decide the

was added to avoid situations in which the *Willie Gary* test is technically satisfied but there is no non-frivolous argument that the arbitration clause covers the underlying dispute. The Court summed up the problem in *Julian*:

> [I]f Company A and Company B entered an emergency-vehicle purchase agreement containing a broad arbitration clause that referenced the AAA Rules, it stands to reason that in a later suit between the companies over an obviously unrelated issue, such as a business tort claim stemming from a different nucleus of operative facts, neither company should be forced to submit the question of who decides substantive arbitrability as to that issue to an arbitrator, even though the arbitral clause meets both prongs of the *Willie Gary* test.[46]

At the same time, Delaware courts have necessarily limited the preliminary evaluation step to determining whether there is no non-frivolous argument; otherwise a court would be deciding the first-order question of substantive arbitrability before deciding the second-order question of who decides substantive arbitrability.[47] For that reason, a court must not "delve into the scope of the arbitration clause and the details of the contract and pending lawsuit . . . ."[48] This limited inquiry avoids the anomalous outcome described above while preserving the efficiency gains contemplated by *Willie Gary*.

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threshold question of substantive arbitrability may do so by making a "clear showing that the party desiring arbitration has essentially no non-frivolous argument about substantive arbitrability to make before the arbitrator . . . ."

[46] *Julian*, 2009 WL 2937121, at *7.

[47] Courts have distinguished between questions of procedural arbitrability and substantive arbitrability, the former referring to questions such as "whether the parties have complied with the terms of the arbitration clause." *Id.* at *4.

[48] *McLaughlin*, 942 A.2d at 623.

B. *Do the Parties' Agreements Satisfy the Willie Gary Test?*

The arbitration clauses in the parties' prior agreements satisfy the two prongs of the *Willie Gary* test. Li does not dispute that conclusion. Instead, he argues that the *Willie Gary* test should only be applied to the Indemnification Agreement because its integration clause shows conclusively that the parties intended it to be the entire agreement between the parties with respect to the subject matter therein. Because the Court ultimately rejects that argument, the Court will first analyze the parties' prior agreements under the *Willie Gary* test before addressing Li's argument.

As to the first prong, the LLC Agreement and the APA each provide that "any claim or controversy arising out of or relating to this agreement, or the breach thereof" shall be settled by arbitration.[49] That broad language "generally refers all disputes to arbitration."[50] Similar arbitration clauses in other agreements have been found to satisfy the first prong of the *Willie Gray* test,[51] including ones that are arguably not as broad. In *McLaughlin*, for instance, a clause requiring

[49] Schulman Aff. Ex. 1 §11.13, Ex. 2 § 9.12. Although not as broad as the arbitration provisions in the APA and the LLC Agreement, the arbitration clause in the Employment Agreement states: [t]he parties agree that any dispute regarding the interpretation or enforcement of this agreement shall be decided by confidential, final and binding arbitration . . . ." Schulman Aff. Ex. 3 § 10.

[50] *Legend*, 2012 WL 4481303, at *5. The arbitration clause in the APA is restricted only slightly and, thus, does not negate the Court's conclusion that the arbitration clause generally refers all disputes to arbitration. *See supra* note 10.

[51] *Id.* at *5 (holding that the "language 'any dispute, controversy or claim arising out of or relating to this [Employment] Agreement' generally refers all disputes to arbitration" and satisfies the first prong of *Willie Gary*).

arbitration "[i]f a dispute arises under this agreement" satisfied the first prong of the *Willie Gary* test.[52] Notably absent was the phrase "relating to"—which extends the arbitration clause beyond the four corners of the agreement.[53]

With respect to the second prong of the *Willie Gary* test, the arbitration clauses in each of the parties' prior agreements reference the rules of the Judicial Arbitration and Mediation Services.[54] Because those clauses incorporate the JAMS rules, and because the JAMS rules empower arbitrators to decide issues of substantive arbitrability, prong two is also satisfied. Rule 11(c) of the JAMS Comprehensive Arbitration Rules and Procedures states:

> Jurisdictional and arbitrability disputes, including disputes over the formation, existence, validity, interpretation or scope of the agreement under which Arbitration is sought, and who are proper Parties to the Arbitration, shall be submitted to and ruled on by the Arbitrator. The Arbitrator has the authority to determine jurisdiction and arbitrability issues as a preliminary matter. [55]

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[52] *McLaughlin*, 942 A.2d at 619, 626 (internal quotation marks omitted); *see also Carder*, 2009 WL 106510, at *4-5 (holding that an arbitration clause that states "all disputes arising in any way under the Agreement" is subject to arbitration satisfies the first prong of the *Willie Gary* test). The Court in *Carder* noted that "although some of the examples the Supreme Court cited in *Willie Gary* of arbitration clauses that 'generally provide[] for arbitration of all disputes' included disputes not only 'arising out of,' but also 'relating to' or 'in connection with' an agreement, two others did not." *Id*.

[53] *Julian*, 2009 WL 2937121, at *5 (noting that the "related to" language "explicitly extends the scope of the arbitration provision 'beyond the four corners of' the LLC Agreement.")

[54] Schulman Aff. Ex. 1 § 11.13, Ex. 2 § 9.12, Ex. 3 § 10.

[55] Def. Standard Fiber, LLC's Opening Br. in Supp. of its Mot. to Dismiss or Stay Ex. 9.

Thus, together the broad arbitration clause and the reference to the JAMS Rules clearly show that the parties intended to arbitrate issues of substantive arbitrability with respect to disputes that relate to the prior agreements.

As mentioned, Li's primary argument with respect to the threshold issue is that the integration clause in the Indemnification Agreement bars the consideration of the prior agreements under *Willie Gary*. In other words, Li asserts that the Court should not look beyond the four corners of the Indemnification Agreement to find the "clear and unmistakable" evidence needed to rebut the presumption that a court should determine the second-order question of who decides substantive arbitrability. Admittedly, this narrower focus would undoubtedly result in the conclusion that the *Willie Gary* test is not satisfied, as the Indemnification Agreement contains neither an arbitration provision nor any reference to the American Arbitration Association Rules, JAMS Rules, or something analogous to them.

Key to Li's argument is the effect that the integration clause has on the prior agreements. On the one hand, the integration clause is evidence that the Indemnification Agreement is completely independent of the parties' other agreements. That view, if supported further, might lead to the conclusion that the arbitration provisions in the prior agreements are nullified with respect to the subject matter of the Indemnification Agreement (*i.e.*, advancement and

indemnification).[56] On the other hand, under Delaware law, an integration clause serves as a presumption of integration, triggering the applicability of the parol evidence rule, which "bars the admission of preliminary negotiations, conversations and verbal agreements . . . ."[57] In the context of the limited inquiry permitted under *Willie Gary* and its progeny, Li's integration argument falls short because the integration clause here does not conclusively establish that the valid arbitration clauses in the prior agreements were terminated. In fact, at least some of the cases examining this issue have concluded that a standard integration clause in a later agreement, with no arbitration clause, does not overcome an earlier agreement that contains a valid arbitration provision.[58] In keeping with *Willie Gary*, and absent a more searching inquiry, the Court can only conclude that Li has offered a colorable argument against arbitrability.

Li also relies on other portions of the Indemnification Agreement to argue against arbitrability. The later in time Indemnification Agreement not only lacks an arbitration provision, it explicitly grants the parties a right to litigate in the

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[56] *See Hough Assocs., Inc. v. Hill*, 2007 WL 148751, at *11-12 (Del. Ch. Jan. 17, 2007) (noting that an arbitration provision in a stock purchase agreement did not apply to an employment agreement because it contains both an integration clause and a remedial clause that directly conflicts with the stock purchase agreement).

[57] *MicroStrategy Inc. v. Acacia Research Corp.*, 2010 WL 5550455, at *13 & n. 98 (Del. Ch. Dec. 30, 2010) (internal quotation marks omitted) (noting that "the presence of an integration clause is not conclusive because the intent of the parties always controls.")

[58] *See Bank Julius Baer & Co., Ltd. v. Waxfield Ltd.*, 424 F.3d 278, 283 (2d Cir. 2005); *Primex Int'l Corp. v. Wal-Mart Stores, Inc.*, 679 N.E. 2d 624, 626-27 (N.Y. 1997); *but see Goss-Reid Assoc. Inc. v. Tekniko Licensing Corp*., 54 F. App'x 405 (5th Cir. 2002).

Delaware Court of Chancery under certain limited circumstances.[59] That runs counter, Li asserts, to Standard Fiber's argument that the parties agreed contractually for all disputes to be arbitrated and confirms, in Li's view, that the Indemnification Agreement was intended to stand alone and operate independently from the prior agreements.

By concentrating solely on the Indemnification Agreement, Li subtly asserts that the claims asserted in the complaint do not relate to the prior agreements. Although he ultimately may be right,[60] his reasoning essentially invites the Court to resolve the first-order issue of substantive arbitrability at the outset, contravening a central tenet of *Willie Gary*.

In *Legend*, the Court rejected similar arguments made by the partnership-plaintiffs, who asserted that their claims related only to a partnership agreement, which contained a jurisdiction and venue clause in favor of Delaware courts, as opposed to an employment agreement with a broad arbitration clause. The Court stated:

> The major problem with the [plaintiffs'] argument is that they essentially want this Court to assess definitively at the outset whether [defendant's] claims arise out of or relate to the Employment Agreement. Such an assessment would amount to deciding substantive arbitrability, thereby circumventing the very purpose of

[59] Those circumstances are limited: Li may bring an action against Standard Fiber in this Court only if he is "successful on the merits of the claims" in any underlying action and the Company fails to pay indemnification. Schulman Aff. Ex. 4 § 2(c).
[60] The Court expresses no definitive view on whether Li's claims are subject to arbitration.

> *Willie Gary*, which is to effectuate the clear intent of parties to arbitrate arbitrability, when such intent is shown.[61]

Similarly, in *Julian*, the Court rejected the argument that the *Willey Gary* test was not satisfied where the plaintiff had argued that his claims were based solely on a statute, and not the parties' LLC agreements, each of which contained a broad arbitration clause and a reference to the American Arbitration Association rules. The plaintiff relied on language from the *Parfi* case, that "[g]enerally, purportedly independent actions do not touch matters implicated in a contract if the independent cause of action could be brought had the parties not signed a contract."[62]

Just as it did in *Legend*, the Court in *Julian* declined to accept the invitation to "decide whether [the plaintiff's] claims arise out of or relate to the LLC agreements" because to do so "would turn *Willie Gary* on its head."[63] Instead, the Court held that "it is not clear that [the plaintiff's] purportedly independent action under the LLC Act seeking fair value of the interests of a member who resigned could be brought in the absence of an LLC Agreement."[64] In applying this low threshold, the Court also noted that there was a colorable argument that the

[61] *Legend*, 2012 WL 4481303, at *5.
[62] *Julian*, 2009 WL 2937121, at *6 (quoting *Parfi*, 817 A.2d at 156 n. 24). In *Parfi*, the court was deciding the first-order question of substantive arbitrability.
[63] *Id*. at *6.
[64] *Id*. at *7.

plaintiff's fair value claim "implicates issues that can only be resolved by interpreting the LLC agreements . . . ."[65]

Finally, in *Majkowski*,[66] a case upon which Li heavily relies, the Court opined that the *Willie Gary* test would have been satisfied had that argument been timely made where there was a broad arbitration clause in a consulting agreement that was entered into eight months after the plaintiff became an officer and where the claims were based solely on pre-existing LLC agreements.[67] Even though the Court concluded ultimately that the dispute was "not subject to the mandatory arbitration provision" in the consulting agreement, it appeared to assume that the arguments to the contrary were at least colorable.[68]

Thus, who decides the question of substantive arbitrability turns on whether Li can clearly show that Standard Fiber has made no non-frivolous argument that the dispute relates to the prior agreements. That, he has not done. Just as in *Julian*, where the Court reasoned that the "plaintiff's claims for fair value of his membership interests . . . at least colorably relate to the agreements that arguably made him a member in the first instance[,]"[69] Li's claims, though based solely on the Indemnification Agreement, could arguably not have been brought absent the parties' prior agreements that made him a member and officer of Standard Fiber.

[65] *Id.* at *8.
[66] *Majkowski*, 913 A.2d at 581 n.13.
[67] *Id*. at 582-83.
[68] *Id*. at 586.
[69] *Julian*, 2009 WL 2937121, at *7.

In that broad sense, there is at least a colorable argument that Li's claims touch upon the prior agreements.

Legend also seems to mandate the conclusion that Standard Fiber has presented a non-frivolous argument in favor of arbitrability. In that case, the plaintiffs sought various declarations relating to Section 7.7 of a partnership agreement, which set forth an intricate process for the valuation of interests. Notwithstanding the fact that Section 7.7 was "arguably outside . . . the scope of the Employment Agreement," the Court held that there was a colorable argument that the valuation claims related to the employment agreement.[70] The Court seemed to rely on the fact that the defendant's financial interest was derived from his employment agreement.[71]

As in *Legend*, Standard Fiber's advancement and indemnification obligations arguably would not have arisen absent the parties' execution of the prior agreements. Indeed, the Indemnification Agreement could be viewed as

[70] *Legend*, 2012 WL 4481303, at *8.

[71] *Id.* at *9. Li argues that in *Legend* the plaintiffs' repurchase claims, arising under a separate section of the partnership agreement, "expressly depended on whether the former officer had been terminated for 'Cause' under a separate employment agreement." Pl.'s Br. 24. It also points out that the partnership agreement explicitly referenced the employment agreement. Thus, in seeking to distinguish *Legend*, Li contends that the "Indemnification Agreement does not rely upon or otherwise incorporate the terms of the [prior agreements] in any respect." *Id.* at 25. Nor, Li argues, does it "require the Court to refer to the terms of the [prior agreements] to resolve [Li's] claims . . . under the Indemnification Agreement." *Id.* And, finally, Li contends that this case is distinguishable because of the integration and non-exclusivity clauses, which were apparently not present in *Legend*. *Id.* Although Li's contentions are mostly correct, they do not necessarily show that Standard Fiber's arguments are not colorable. They also do not distinguish the Court's reasoning as to Section 7.7 of the partnership agreement, which found a colorable argument where there was no incorporation of, or reference to, the employment agreement.

supplementing various provisions in the LLC and Employment Agreements. Moreover, Li's claims under the Indemnification Agreement relate, at least colorably, to the LLC Agreement in that Li seeks adjudication of substantively the same advancement and indemnification rights that are provided for in the LLC Agreement. These arguments may not be particularly persuasive, but given the low threshold the Court is obligated to apply, the Court cannot conclude that Standard Fiber has made no non-frivolous arguments in favor of arbitrability. Thus, the Court must defer to the arbitration forum to resolve the question of whether his effort to obtain advancement is properly resolved through arbitration.

C. *Is the Dispute Ripe for Adjudication?*

The parties disagree over whether Li has properly made a demand for advancement under the Indemnification Agreement, and if not, whether the dispute is ripe for adjudication. That basic controversy has wandered into a hodgepodge of side-issues. The parties have offered competing versions of events; estoppel arguments have been raised; and one party has accused the other party of inordinate delay. None of these issues, however, needs to be addressed given that the arbitrator must determine whether Li's claims are subject to the mandatory arbitration clauses. This course of action is also prudent because the question of ripeness may be settled in just a few days. Indeed, it appears that Li has recently provided to Standard Fiber the specific invoices for which he is seeking

advancement. If the invoices were sufficient, then any question of ripeness would be resolved by no later than early April. If this issue is not resolved, the arbitrator can address that issue.

III. CONCLUSION

Standard Fiber seeks either dismissal or a stay of this action. The Court may issue a stay pending the resolution of arbitration, based on "comity, efficiency, or common sense."[72] Having concluded, first, that the parties intended to arbitrate the question of who decides arbitrability, and second, that Standard Fiber's arguments in favor of arbitrability are not frivolous, the Court will issue a stay pending the arbitrator's determination of whether the parties contractually agreed for Li's claims to be arbitrated.

[72] *Legend*, 2012 WL 4481303, at *4.