IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

ASAMI ISHIMARU, Plaintiff, v. WILLIAM FUNG, and IVY ASSET MANAGEMENT CORP., Defendants, and PARADIGM FINANCIAL PRODUCTS INTERNATIONAL LLC, Nominal Defendant.	)	C.A. No. 929

MEMORANDUM OPINION

Date Submitted: October 4, 2005
Date Decided: October 26, 2005

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STRINE, Vice Chancellor

In essence, this is a derivative suit brought by Asami Ishimaru, a member of nominal defendant Paradigm Financial Products International LLC ("Paradigm"), against defendant Ivy Asset Management Corp. ("Ivy Asset"). Ishimaru alleges that defendant William Fung, who controls a majority of the membership interests in Paradigm and is its managing member, has not and will not consider fairly whether to press Paradigm's claims against Ivy Asset.

Ishimaru seeks an order allowing her to prosecute a claim in Paradigm's name that Ivy Asset breached contractual promises it made to Paradigm regarding the basis on which Ivy Asset would market certain investment funds in Japan. Ishimaru wants this court to hear that claim. But Ivy Asset argues that the breach of contract claim Ishimaru seeks to assert on Paradigm's behalf must be arbitrated, consistent with an arbitration clause (the "Arbitration Clause") in an operating agreement (the "Joint Venture Agreement") between Paradigm and Ivy International, LLC ("Ivy International"), a subsidiary that Ivy Asset formed specifically for the purpose of pursuing a joint venture with Paradigm in Japan (the "Joint Venture"). Ivy Asset therefore seeks to dismiss this action in favor of arbitration.

In this opinion, I conclude that Ishimaru may press a derivative claim on Paradigm's behalf against Ivy Asset. Her complaint articulates particularized facts that, if true, demonstrate that Fung is incapable of disinterestedly determining whether to cause Paradigm to sue Ivy Asset. Those facts indicate that Fung attempted to use financial products developed for Paradigm for his own benefit and to sacrifice the interests of Paradigm in order to secure concessions from Ivy Asset that would benefit

him personally, rather than as a member of Paradigm. Therefore, an order permitting Ishimaru to proceed on Paradigm's behalf shall issue.

I rule against Ishimaru, however, on the issue of where she can press that claim. Ishimaru's attempt to escape the reach of the arbitration clause of the Joint Venture Agreement is unavailing. By her own description of Paradigm's supposed claim, both in the current amended complaint and in the original complaint which also named Ivy International as a defendant, Ishimaru plainly alleges that Ivy Asset breached later promises (the "New Bargain") that had the effect of amending the Joint Venture Agreement. Indeed, Ishimaru alleges that Ivy Asset's motive for the New Bargain was its desire to avoid a dispute with Paradigm about whether Ivy Asset, by undertaking certain marketing activity in Japan outside the Joint Venture, had breached contractual duties it owed to Paradigm under the Joint Venture Agreement.

Although Ivy Asset is not, by literal terms, bound by the Arbitration Clause, that mere fact does not excuse Ishimaru's refusal to arbitrate — Paradigm is bound. Moreover, Ishimaru alleges that Ivy Asset owed important contractual duties to Paradigm by virtue of the Joint Venture Agreement. Not only that, Ishimaru alleges that Ivy Asset breached a promise made in a business plan that became, per the provisions of the Joint Venture Agreement, part of that Agreement. The New Bargain Ishimaru claims that Ivy Asset made and then breached had an important negative effect on Ivy International's rights under the Joint Venture Agreement. As a signatory to the Arbitration Clause, Paradigm fairly is bound to arbitrate claims premised on the notion that a non-signatory, Ivy Asset, signed a contract, the New Bargain, fundamentally amending the terms of the

Joint Venture Agreement and then breached that amendment. In essence, Paradigm's claims are contingent upon the proposition that Ivy Asset was, by Paradigm's consent, admitted as a party to the Joint Venture Agreement, could and did, by agreement with Paradigm, alter the formal terms of that Agreement, and thereafter breached the altered Joint Venture Agreement. Under the teaching of a series of well-reasoned federal cases,[1] Paradigm is equitably estopped from denying Ivy Asset's demand to arbitrate.

I. Factual Background

The description of the facts is drawn primarily from Ishimaru's amended complaint. Ordinarily, I would not draw much attention to the occurrence of an amendment. Regrettably, one cannot avoid dealing with both pleadings here. For reasons that she denies are tactical, Ishimaru amended her complaint in several important ways, including dropping Ivy International as a defendant. Although she denies that the reason for the amendment was to escape the Arbitration Clause, the happy coincidence seems to be that the amendment makes it easier for her to argue that she is free from the Arbitration Clause's reach. Whatever her motives, Ishimaru is not entitled to blind this court to her prior pleading, and the court will highlight the ways in which she has altered the claim she seeks to assert on Paradigm's behalf.

[1] *E.g.*, *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524 (5th Cir. 2000); *Thomson-CSF, SA v. Am. Arbitration Ass'n*, 64 F.3d 773 (2d Cir. 1995); *Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.*, 10 F.3d 753 (11th Cir. 1993); *McBro Planning and Dev. Co. v. Triangle Elec. Constr. Co.*, 741 F.2d 342 (11th Cir. 1984).

A. The Formation Of Paradigm

Ishimaru, Fung, and two associates of Fung formed Paradigm in 1997 to exploit what they hoped would become a growing demand among Japanese investors for hedge fund investments. Through Paradigm, Ishimaru and Fung hoped to bring hedge fund products of their own to the Japanese markets, and to place the capital of Japanese investors with other providers of hedge funds.

The basic skill divide among the Paradigm founders was clear. For his part, Fung, a research professor, possessed expertise in risk management. He was therefore to be the founder most involved on the investment side of the business, structuring funds and managing investments. In exchange for this role, Fung got 50% of Paradigm's equity and was named the managing member; his associates received another 18% of the equity.

For her part, Ishimaru was experienced in marketing and had business relationships in Japan that she could exploit. Therefore, she was to secure Paradigm's entrée into the Japanese market. According to her, this was a critical function. As of the time of Paradigm's formation, Japanese investors had little experience with hedge funds and such funds had little market penetration. Ishimaru's task was to familiarize Japanese investors with the concept of hedge fund investing and encourage them to entrust their capital to this emerging form of investment fund. As part of the founders' agreement, Ishimaru received 32% of Paradigm's equity.

B. Paradigm Looks To Ivy Asset As A Partner

After forming Paradigm, Fung and Ishimaru realized that Paradigm had a problem. Although Fung had written about risk management as an academic, he had no track

record as the manager of an actual investment portfolio. Given Japanese investors' relative unfamiliarity with hedge fund investments, the absence of successful past performance by Paradigm made inducing Japanese capitalists to invest in hedge funds more than tenably challenging.

To address this, Paradigm, through Fung, approached Ivy Asset, a registered Investment Company known for its management of investment funds that invest in hedge funds. The concept was that Ivy Asset and Paradigm would form a joint venture to sell hedge fund products to Japanese investors. Ivy Asset would bring to the table its track record and components of its products. Paradigm would provide Fung's risk management skills and Ishimaru's marketing skills and Japanese contacts, attributes that Ivy Asset lacked because it was not licensed to sell funds in Japan and had no Japanese contacts of its own.

For the purposes of entering into the Joint Venture with Paradigm, Ivy Asset formed Ivy International, a Delaware limited liability company. At the time of the formation of the Joint Venture, Ivy Asset was the sole member of Ivy International.[2] The formal Joint Venture vehicle was PI Asset Management, L.L.C., which was created by an operating agreement on December 18, 1997, i.e., by the Joint Venture Agreement.

By its terms, the Joint Venture Agreement identified Paradigm and Ivy International as the Joint Venture's only members ("Members")[3] and provided that they

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[2] This apparently changed in October 2000. When Bank of New York acquired Ivy Asset and Ivy International, it became the sole member of both Ivy Asset and Ivy International. That fact is not of material significance.
[3] Joint Venture Agreement ("JVA") § 5.01.

would jointly serve as managing members. But the Joint Venture Agreement reflected the essential business reality that the two primary Joint Venture partners were actually Ivy Asset and Paradigm, with Ivy International simply functioning as the formal corporate vehicle through which Ivy Asset would participate. I do not advance that proposition lightly, recognizing the importance of the corporate form and contractual language. I advance it because the Joint Venture Agreement and the subsequent course of dealing by the parties under that Agreement alleged by Ishimaru make that reality plain.

C. The Relevant Provisions Of The Joint Venture Agreement

A few features of the Joint Venture Agreement highlight that reality. For starters, the purposes of the Joint Venture emphasized the parties' intention to create an offshore investment fund that would invest in another fund involving multiple managers through a master-feeder structure. The so-called Offshore Master Fund was to employ strategies "substantially similar to those currently employed by the managers of Ivy Asset Management Corp.'s multi-manager funds . . . ."[4]

In § 1.08, the parties restricted transfers of membership interests, but they made exceptions that permitted Ivy International and Paradigm to transfer all or portions of their interests to affiliates, including specifically to Ivy Asset. In § 1.08(c), Paradigm and Ivy International agreed to disclose and keep current a list of each of their members.

The Joint Venture Agreement also spelled out certain rights and responsibilities, not only of Paradigm and Ivy International themselves, but of their affiliates, including

[4] JVA § 1.03.

Ivy Asset. For example, § 2.05 addressed activities by the members and their affiliates as follows:

> Each of the Members (and their equity owners) and any members, officers, employees or other agents or advisers of the Members or the Company (collectively, "Affiliates") shall devote so much of their time to the affairs of the Company as the conduct of the business of the Company shall reasonably require. Nothing herein contained shall be deemed to preclude the Members or their Affiliates from engaging, directly or indirectly, in any other business, irrespective of whether any such business is similar to, or a competitor with, the business of the Company. No Member shall have the right to participate in any manner in any profits or income earned or derived by or accruing to the other Member or its Affiliates from the conduct of any such other business.

Relatedly, § 2.06 provided exculpation for Members and their affiliates, while § 2.07 enhanced that exculpatory protection by granting Members and their affiliates certain advancement and indemnification rights against the Joint Venture in the event of proceedings related to their actions on behalf of the Joint Venture.

Importantly, § 9.03 protected the Joint Venture by binding Members and a group that would ordinarily be termed, but was not in that section, "affiliates." Rather, § 9.03 purports to bind Members and their officers, employees, agents, and the Members' own members. In pertinent part, it provides as follows:

> All knowledge and information . . . relating to the Company, each Member, any Fund or the Offshore Master Fund not already within the public domain which each Member may acquire by virtue of the performance of services hereunder shall at all times and for all purposes, be regarded by each Member as strictly confidential and held by each Member in strict confidence, and shall not be directly or indirectly disclosed by a Member or its respective officers, employees, members or agents to any person whatsoever.

By the plain terms of § 9.01, the Joint Venture was only to be amended "by a written instrument executed by each Member." Presumably, this amendment feature also applied to the business plan incorporated in § 1.03(a) of the Joint Venture Agreement (the "Business Plan"). By virtue of § 1.03(a), the Joint Venture was to be operated in accordance with a Business Plan, the initial version of which was annexed to the Joint Venture Agreement. The Business Plan was to "be in place at all times."[5] The initial Business Plan uses the term Ivy to refer to Ivy Asset. All of the duties to be undertaken under the Business Plan on behalf of the Joint Venture by an entity with the name "Ivy" are, by plain reading of the text, to be accomplished by Ivy Asset. The only reference to Ivy International is as the "Delaware LLC[]" formed by Ivy Asset to "participate in the JV." There is a similar reference to an LLC being formed by Paradigm for that purpose. Both references are in a section entitled "Taxes," indicating the use of this form was for tax purposes.

The last operative provision of the Joint Venture Agreement, § 9.13(b), is the Arbitration Clause, which provides that "[u]nless otherwise agreed in writing, each Member agrees to submit all controversies arising between Members, or one or more Members and the Company, concerning this Agreement to arbitration in accordance with the provisions set forth below." The Arbitration Clause does not, by its own terms, refer to affiliates of Members.

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[5] *Id.*

D. The Course Of Dealing Of The Parties Under The Joint Venture Agreement

Consistent with the Business Plan, the Joint Venture's operations in all practical respects were carried out by Paradigm and Ivy Asset. Ivy Asset worked with Fung to put together the product offerings of the Joint Venture, while Ishimaru concentrated on obtaining Japanese investors for those products. The Business Plan spelled out the roles with some precision.

In September 1998, the Joint Venture launched its first fund product in Japan — the PI Market Neutral Fund (the "Neutral Fund"). The Neutral Fund was to be a combination of two existing Ivy Asset financial products. The Neutral Fund concept was met with apprehension by Japanese investors due to their unfamiliarity with hedge funds and the novelty of this particular fund. Furthermore, the Joint Venture was not licensed to sell funds directly in Japan.

The Joint Venture took steps to address these concerns. To address the Japanese investors' reluctance to invest in a hedge fund, the Joint Venture offered the Neutral Fund along with a bond providing principal protection at maturity that sharply limited downside risk (the "Neutral Fund Bonds"). To provide a path to market, Ishimaru convinced licensed intermediary NatWest Tokyo to sell the Neutral Fund and the Neutral Fund Bonds.[6] The Neutral Fund was launched with approximately $50 million in seed money from Japanese investors. Later, in September 2000, the Joint Venture secured an

[6] Consistent with its general nature, the amended complaint's description of the relationship between the Neutral Fund and the Neutral Fund Bonds is unclear. It is not clear whether investors in the Neutral Fund could buy the Neutral Fund Bonds as optional protection or whether the only thing sold in Japan was Neutral Fund Bonds, which had returns linked to the similar Ivy Asset products but with principal protection.

additional dealer, Sakura Securities, to market the Neutral Fund and the Neutral Fund Bonds. Sakura Securities subsequently was merged into Daiwa Securities SMBC Co. Ltd. ("Daiwa"), which Ishimaru convinced to continue to distribute Joint Venture products.

The Joint Venture's second financial product was launched in November 2001. The PI Long Short Hedge Equity Fund Ltd. ("PILS") was allegedly unique by the standards of investment funds comprised of underlying hedge funds. What supposedly made it special was that the Joint Venture, as the portfolio manager, maintained direct control over all portfolio investments, which allowed it to continually monitor and hedge away risk. As of the time of the amended complaint, the Neutral Fund Bonds and PILS were the only two products marketed by the Joint Venture.

E. Ivy Asset's And Paradigm's Interests Diverge

In October 2000, a transaction took place that created a divergence in interest between Ivy Asset and Paradigm. That month the Bank of New York ("BoNY") acquired Ivy Asset. Unlike Ivy Asset, BoNY had a presence in Japan that pre-dated the Joint Venture, but that presence was limited to banking.

After the BoNY transaction, Ivy Asset allegedly began approaching unlicensed intermediaries in Japan to sell its own products, such as its Rosewood Offshore Fund, to Japanese investors. Paradigm got wind of this in May 2001 when Daiwa cried foul after learning that Ivy Asset was selling Rosewood in Japan through BoNY and other unlicensed vendors, activity that undercut Daiwa's effort to sell the products of the Joint Venture. In the Joint Venture's Business Plan for 2000-2001, which amended the

original Business Plan, the following statement was made: "Both joint venture parties remain committed to the business plan and will not engage in substantially similar businesses targeted at the Japanese market which may damage the success of the JV."[7]

Ishimaru and Fung contacted an Ivy Asset managing director, Jeffrey Lindenbaum, about their beef.[8] At that point, Ivy Asset admitted contacting ten Japanese institutions about buying Rosewood, and Lindenbaum agreed to limit Ivy Asset's activities in Japan to these ten institutions (the "Carve Out List"). Ishimaru and Fung agreed to this compromise. But, according to Ishimaru, Lindenbaum was not good to his promise and Ivy Asset continued to spread in Japan to investors not on the Carve Out List.

In late 2001 or early 2002, Daiwa again notified Paradigm that an unlicensed subsidiary of a Japanese trading company, Mitsui and Co., Ltd., was selling a fund managed by Ivy Asset. When called on this, Lindenbaum denied that Ivy Asset had authorized the sale of that fund through Mitsui. In April 2002, a Mitsui subsidiary secured a license to sell hedge funds in Japan. In September 2002, NatWest alerted Paradigm that Mitsui had approached a Neutral Fund Bonds investor and attempted to sell them Ivy Asset investment products. Concurrently, Daiwa complained that Mitsui

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[7] Am. Compl. ¶ 14. Ishimaru cited this Business Plan for 2000-2001 in her amended complaint as the most recent Business Plan based on "belief and information" but did not provide the entire document. Additionally, it appears that a more recent Business Plan that does not contain this permissive language was in effect at the time of this dispute. Fung appended the Business Plan for 2001-2002 to his motion to dismiss the original complaint.

[8] Jeffrey Lindenbaum is clearly a Managing Director of Ivy Asset. Am. Compl. ¶ 22. As is typical, the amended complaint and complaint make deciphering whether and how Lindenbaum is involved with Ivy International difficult. The original complaint refers to Lindenbaum as a Managing Director of Ivy when Ivy was defined as both Ivy Asset and Ivy International, and the amended complaint states he is a Managing Director of Ivy defined as Ivy Asset. Compl. ¶ 23.

was undercutting their ability to sell the Neutral Fund Bonds because Ivy Asset was offering vendors of the Rosewood Fund preferential pricing to that received by vendors of the Joint Venture's products. Once again, Lindenbaum denied that Ivy Asset had authorized Mitsui to contact any institutions other than the Carve Out List.

In October 2002, Lindenbaum ended his campaign of denial. He informed Paradigm that Norinchukin, a large Japanese investor not on the Carve Out List, wanted to meet with Ivy Asset; he also confessed that Mitsui was indeed the matchmaker. Later in 2002, Ivy Asset directly contacted Daiwa — distributor of the Neutral Fund Bonds — about the possibility of marketing Rosewood in Japan. Daiwa again informed Paradigm of this occurrence. In addition, Lindenbaum entered into discussions with Mizuho Trust to distribute Rosewood to Japanese pension funds.

After learning of these Ivy Asset dealings with investors not on the Carve Out List, Ishimaru contacted Lindenbaum and Lawrence Simon, who served as CEO of Ivy Asset, President of Ivy International, and co-CEO of the Joint Venture. Lindenbaum and Simon took the position that the Neutral Fund Bonds and the PILS Fund — the Joint Venture's only two products — should simply become part of an array of Ivy Asset products to be offered in Japan. Paradigm did not receive this proposal warmly. With Fung's permission, Ishimaru informed Ivy Asset that its compromise proposal was rejected and that Paradigm would seek legal advice about its options.

F. <u>The Alleged "New Bargain" Between Ivy Asset And Paradigm</u>

By the spring of 2003, the Joint Venture partners had not worked out their differences. In March and April of that year, Fung, Ishimaru, Lindenbaum, and Simon

met twice to consider options for resolving their disagreements without filing claims. Fung assigned Ishimaru lead responsibility to work things out because he considered it to be a marketing dispute in her bailiwick. Ishimaru alleges that Fung authorized all of her activities on behalf of Paradigm.

Ishimaru claims that Ivy Asset and Paradigm reached an accord at the second meeting, what I have termed the New Bargain. She further argues that the accord was formalized in an e-mail exchange between herself and Lindenbaum. Ishimaru's e-mail states:

> Based on our meetings on March 27th and April 16th, my understanding of what you offered regarding Japan is the following…all Ivy business in Japan will be conducted by the joint venture. The joint venture will be the unified front offering all Ivy related products and services in Japan. The fee split will be 50/50 with the following exception. 1) When an existing product managed solely by Ivy (e.g. Rosewood) is sold to a Japanese Investor, Paradigm will receive 25% of the fees paid by the investor. 2) If the Japanese investor is introduced by the Bank of New York, the fee split will be negotiated on a case by case basis.[9]

Lindenbaum's reply states in pertinent part that:

> We concur with all that you have stated, and most importantly, the spirit of uniform cooperation and joint activities will make this very worthwhile. As to BONY and possible future business, the fee structure will potentially vary depending on size of AUM placement, BONY fee share, and what Ivy gets as its portion. I can assure you that it will be worthwhile should these opportunities come to completion, and await the first to see what can be codified as a percentage of fees. Please be patient to see what may and can be allocated, I need a little time as I am negotiating with BONY as to how Ivy/BONY split fees for future business.[10]

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[9] Ishimaru Ans. Br. Ex. A.
[10] *Id.*

Ishimaru contends that the e-mail exchange represents a formal contract between Ivy Asset and Paradigm that has the following primary terms:

- Ivy Asset, with limited exceptions, would conduct all of its business in Japan through the Joint Venture;
- any fees generated by the sale of Ivy Asset's products managed by the Joint Venture to Japanese investors would be split 50%/50% between Ivy Asset and Paradigm;
- any fees generated by the sale of existing Ivy Asset products managed by Ivy Asset to Japanese investors would be split 25% to Paradigm and 75% to Ivy Asset; and
- any fees generated by the sale of Ivy Asset products to Japanese investors that were introduced to Ivy Asset by BoNY would be split on a "case-by-case" negotiated basis.

G. Ivy Asset Breaches The New Bargain

Ishimaru insists that she acted with alacrity in response to the New Bargain. Having assented to the marketing of Ivy Asset products in Japan in exchange for a cut of the proceeds, Ishimaru focused on maximizing the size of the overall pie. Therefore, she helped introduce Ivy Asset's products and key managers to many of her contacts in the Japanese investment community. Ishimaru encouraged Daiwa and other Japanese contacts to market not only Joint Venture products but also existing Ivy Asset products. Consistent with those efforts, Daiwa soon placed over $200 million in investments in Rosewood, and Ivy Asset received other infusions in Rosewood from sources not on the Carve Out List.

Ishimaru claims Paradigm and Ivy Asset even worked out a fee split on Ivy Asset products to be sold through the Mizuho Trust, which Lindenbaum claimed had been

introduced to Ivy Asset by BoNY. Lindenbaum, on behalf of Ivy Asset, offered Paradigm 10% of the fees generated from Ivy Asset business placed through Mizuho Trust. Paradigm accepted this offer.

According to Ishimaru, Ivy Asset led her to believe that it thought things were going swimmingly under the New Bargain. She allegedly received e-mails from Lindenbaum and Simon expressing satisfaction with the new arrangements and encouraging her to continue her marketing efforts. But when Ishimaru contacted Ivy Asset in October 2003 and requested payment of Paradigm's share of the fees generated on Ivy Asset products sold in Japan, Ivy refused and disclaimed the New Bargain.

While the Joint Venture partners' relationship was deteriorating, so too was the relationship between Fung and Ishimaru. According to Ishimaru, Fung began planning in 2002 to strike out on his own in Europe by marketing an investment fund product essentially identical to PILS. His problem was that PILS was a Joint Venture product, and his desire to use it for himself and to tout PILS's track record of success was arguably at odds with the provisions of the Joint Venture Agreement. Among other things, the Joint Venture Agreement § 9.03 expressly states:

> All knowledge and information (referred to herein as "Information") . . . not already within the public domain . . . shall at all times and for all purposes, be regarded by each Member as strictly confidential. The Information referred to above shall include names of investment managers and their performance records, or other information relating to such managers obtained in connection with a Fund, and any details relating to the financial engineering, Fund structure and identity of the financial intermediaries associated with any Company product.

Moreover, while the Joint Venture Agreement gave Members and their affiliates the right to compete, Fung was not trying to compete using assets and skills unrelated to the Joint Venture; he was trying to parlay Joint Venture property — PILS and its strategies — into gains for himself — not for the Joint Venture or even Paradigm. Although Fung allegedly proceeded without worrying much about the rights of his fellow Paradigm investors, he was worried that Ivy Asset, which had worked with Paradigm to develop the PILS product, would not be pleased if he proceeded to market a new PILS-like product without involving Ivy Asset.

Fung allegedly dealt with this concern by suggesting that Paradigm soften its position towards Ivy Asset's violation of the New Bargain. Fung was willing to trade away claims relating to Ivy Asset's conduct in Japan in exchange for concessions from Ivy Asset that would permit him to establish a personally-controlled entity to market a PILS-like product in Europe under the Ivy Asset banner. He engaged in these discussions with Ivy Asset behind Ishimaru's back. Fung believed that the Market Neutral Bonds product had little upside and that he could make out better by ignoring the Joint Venture's rights in Japan and focusing on securing a relationship for himself with Ivy Asset centered on PILS. Thus, Fung refused to back up Ishimaru in her desire to have Paradigm assert its rights against Ivy Asset. He then went even further and terminated Ishimaru's operational role on behalf of Paradigm and ceased paying her profit distributions.

In the meantime, Ivy Asset has reaped the benefits of Paradigm's paralysis. It has raised over $1 billion in capital in Japan since 2003 through its Rosewood product.

During the same period, the Joint Venture's Market Neutral product has not attracted a single new investor despite having outperformed Rosewood during the same period.

H. Ishimaru's Initial Complaint

In December 2004, Ishimaru filed the original complaint in this action. The first count sought relief against Fung for not filing suit on Paradigm's behalf against Ivy Asset and Ivy International. The second count named both Ivy Asset and Ivy International as defendants and sought relief against them for breaching the New Bargain (the "New Bargain Claim"). Not only that, the original complaint, consistent with the obvious business reality, defined Ivy Asset and Ivy International collectively as "Ivy."

The original complaint is consistent with the facts rendered previously in the opinion. But it did not seek to distinguish between Ivy Asset and Ivy International in any material way, except to note that Ivy International was formed as the subsidiary of Ivy Asset that was a direct party to the Joint Venture Agreement. By its clear terms, the original complaint makes plain the reality that Paradigm dealt with Ivy Asset and Ivy International indistinguishably and treated Ivy Asset as capable of making decisions as if it was the Member under the Joint Venture Agreement.

In that respect, the original complaint alleged that Ivy, as a collective comprising both Ivy Asset and Ivy International, was a party to the New Bargain. The original complaint specifically alleged:

> *Ivy and Paradigm entered into a contract by which the parties reaffirmed their agreement that the parties' business dealings in Japan, including the marketing and funding of investment products, would be conducted by PI, the joint venture the parties had previously formed for that purpose*. The parties additionally reaffirmed that all fees generated

> from Japanese business would be shared 50% by Paradigm and 50% by Ivy Int'l. For all existing products sold in Japan which Ivy Asset Management managed independently of [the Joint Venture], however, Paradigm would receive 25% of the fees. The split would, however, be negotiated on a case-by-case basis if the Japanese investor was introduced by BoNY.[11]

The original complaint sought damages from Ivy Asset and Ivy International for breach of the New Bargain.

I. Ishimaru Amends Her Complaint When The Ivy Defendants Argue That The Claims Against Them Are Subject To The Arbitration Clause

The Ivy defendants responded to the original complaint by moving to stay or dismiss this case on the grounds that Ishimaru's breach of contract claims were governed by the Arbitration Clause of the Joint Venture Agreement. Ishimaru countered by amending her complaint in a manner that to a cynic would appear purposely designed to retract pled facts that, if true, made it more difficult for her to escape the Arbitration Clause. A non-exhaustive parade of some of the highlights include:

- Removing Ivy International as a defendant altogether;
- Changing the definition of "Ivy" to include only Ivy Asset;
- Changing an allegation that Ivy Asset and Ivy International both breached an agreement not to compete with the Joint Venture in Japan to contend that Ivy Asset alone violated an agreement by Ivy International alone not to compete with the Joint Venture, by marketing products in Japan bypassing the Joint Venture. In other words, the amended complaint is internally inconsistent as it alleges that Ivy Asset is responsible singularly for breaching an agreement made by Ivy International singularly, and by trying to keep entities distinct that Ishimaru clearly treated as indistinct in the original complaint and her business dealings;
- Changing allegations related to the behavior of the Ivy entities under the Joint Venture Agreement to contend that Ivy Asset acted wrongfully by

[11] Compl. ¶ 51 (emphasis added).

using information gleaned from Ivy International through the Joint Venture to market Ivy Asset products in Japan outside the Joint Venture;

- Changing the allegation that Ivy International was a party to the New Bargain and alleging that Ivy Asset and Paradigm were the only parties;
- Changing the allegation that, after the New Bargain, Ishimaru invested time marketing Ivy Asset products on behalf of the Joint Venture, to allege that she invested that time only on behalf of Paradigm; and
- Changing the allegation that the New Bargain "reaffirmed" key aspects of the Joint Venture Agreement with certain "exceptions" to an allegation that Ivy Asset and Paradigm entered into the New Bargain as a "contract to settle a dispute between the members of [the Joint Venture]." That is, Ishimaru alleged that Ivy Asset settled a dispute among the Members of the Joint Venture, through a contract to which one of the alleged disputing members, Ivy International, was not even a party.

As can be seen, Ishimaru took an original complaint that told a plausible, unstrained story that rightly made little distinction between Ivy Asset — an operating company that both provided all the real work and made all the real decisions on the Ivy side related to the Joint Venture — and Ivy International — an LLC formed as the specific vehicle that for tax and liability-limiting purposes that was the direct Member of the Joint Venture — and converted it into a stilted, awkward, and implausible tale. Yet, Ishimaru claims that the amended complaint was filed to ensure the operative complaint more accurately reflected the facts, rather than to avoid the Arbitration Clause.

II. Legal Analysis

There are two critical issues before me now. The first is whether Ishimaru may assert derivative claims on behalf of Paradigm against Ivy Asset. The second issue is whether Ishimaru can proceed derivatively on Paradigm's behalf in this court, rather than

in arbitration. The second issue need only be addressed if the answer to the first issue in contention is affirmative. I therefore address them in logical order.

A. Does The Amended Complaint Plead Facts Justifying The Procession Of A Derivative Action By Ishimaru On Paradigm's Behalf?

The procedural posture in which this issue arises has been unnecessarily complicated, by both Ishimaru and Fung. The complications started with the odd nature of the complaint. Instead of simply alleging facts demonstrating why Ishimaru should be permitted to proceed as a derivative plaintiff on Paradigm's behalf, Ishimaru concocted a fiduciary duty claim against Fung premised on his failure to take any action against Ivy Asset for breaching the New Bargain.

For his part, Fung confused things by his responses to the complaint and amended complaint. Fung did not move to dismiss on the grounds that Ishimaru had not shown a basis to proceed with a derivative claim — in other words, by arguing that he as managing member of Paradigm could disinterestedly determine that matter. Instead, Fung simply moved to stay the fiduciary duty claim, arguing that it was premature to litigate that count against him until the claim Ishimaru asserted on Paradigm's behalf against Ivy Asset was adjudicated, in whatever forum.[12] Fung's theory was that if Paradigm's claim failed, he could not have harmed Paradigm by failing to assert it. Because of this approach, Ishimaru rightly claims that Fung led her and the court to

[12] In two letters to the court, Fung plainly said that the New Bargain Claim should be arbitrated. *See* Fung Letter at 3-4, April 18, 2005; Fung Letter at 2-3, June 10, 2005. Fung even argued that he would like to bring claims against Ishimaru if the New Bargain Claim was remitted to arbitration and that this was a further reason to stay the claim against him. Fung Letter at 2, June 10, 2005.

believe that he would not assert that she could not proceed derivatively on Paradigm's behalf.

As motion practice on Ivy Asset's motion to dismiss this case in favor of arbitration evolved, however, Fung gummed up the works by attempting to back-track on that position. He began raising objections to Ishimaru's right to proceed.

In order to clarify matters, I instructed Ishimaru to seek judgment on the pleadings as to her right to proceed derivatively, and gave Fung an opportunity to answer the amended complaint. That opportunity was without prejudice to Ishimaru's right to argue that Fung had waived the arguments he recently came to embrace. Briefing on the question of the procession of the derivative action was recently completed. After considering the arguments of the parties, I conclude that Ishimaru is entitled to proceed derivatively on Paradigm's behalf for two reasons.

The first is that Fung, by his conduct in this litigation, waived any argument that Ishimaru cannot proceed derivatively for Paradigm. By necessity, it is important that the question of whether a complaint pleads sufficient grounds to justify the procession of a derivative suit be addressed early in litigation. On not one but two occasions, Fung responded to complaints by urging this court to defer action on the fiduciary duty count against him until Ishimaru, on behalf of Paradigm, duked it out with Ivy Asset on the merits. Therefore, Fung waived the right to withdraw that position, for tactical reasons, and now claim that he, as managing member of Paradigm, should determine whether Paradigm sues Ivy Asset.

Delaware law rightly takes seriously the task of evaluating when a suit by an entity should proceed at the instance of a derivative plaintiff, rather than the entity's governing authority. That is why our corporate law imposes a specific burden to plead demand futility,[13] and why that has been replicated in our statute addressing LLCs.[14] But it is also the obligation of a defendant resisting the procession of a derivative suit to make a demand excusal argument promptly and not waste the resources of the plaintiff and court.[15] Here, Fung not once, but twice, expressed the view that the New Bargain claim should be decided on its merits. He is now rightly stuck with that position.

Second, even if Fung had properly preserved an objection to Ishimaru's attempt to proceed derivatively for Paradigm, the amended complaint pleads particularized facts demonstrating that Fung, as managing member, cannot disinterestedly determine whether Paradigm should sue Ivy Asset.[16]

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[13] *E.g., Aronson v Lewis,* 473 A.2d 805 (Del. 1984).
[14] 6 *Del. C.* § 18-1003.
[15] Ironically, Fung's earlier argument that arbitration of the New Bargain Claim should be the first order of business was justified as the best way to avoid "a highly inefficient use of judicial and the parties' resources . . . ." Fung Letter at 3, June 10, 2005.
[16] It is possible to conceive of this as a case where demand was made and refused because Ishimaru raised the issue of Ivy Asset's purported breaches with Fung and attempted to discuss a strategy for dealing with Ivy Asset. The test for determining whether a communication constitutes a demand was articulated by then Vice Chancellor, now Justice Jacobs in *Yaw v. Talley*, 1994 WL 89019, at *7 (Del. Ch. Mar. 2, 1994): "to constitute a demand, a communication must specifically state: (i) the identity of the alleged wrongdoers, (ii) the wrongdoing they allegedly perpetrated and the resultant injury to the corporation, and (iii) the legal action the shareholder wants the board to take on the corporation's behalf." Neither party has argued that the demand refusal standard applies, both have instead argued this as a demand excusal motion and I accept their rubic. Specifically, Fung does not allege that Ishimaru's communications to him satisfied the *Yaw* criteria. Additionally, even if Fung had raised the demand refusal standard, Ishimaru has articulated particularized facts in her amended complaint that create a reasonable doubt as to the good faith and reasonableness of Fung's investigation. *See Levine v. Smith*, 591 A.2d 194, 212 (Del. 1991).

The Delaware Limited Liability Company Act provides that "a member . . . of a limited liability company . . . may bring an action in the Court of Chancery . . . to recover a judgment in its favor if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers or members to bring the action is not likely to succeed."[17] A derivative complaint filed by an LLC member must also set forth with particularity "the effort, if any, of the plaintiff to secure initiation of the action by a manager or member or the reasons for not making the effort."[18] The standard governing demand by an LLC member, whether such demand is "likely to succeed," is the same standard governing demand in limited partnerships.[19] This court has recognized, despite the statutory basis for demand in the limited partnership context, that "the issues in determining demand futility for partnership law appear identical to those in corporation law"[20] and, therefore, has applied the familiar test for corporate demand futility. Similarly, we have applied the *Aronson* test to demand futility in the LLC context.[21] I will, therefore, look to precedent on corporate demand futility in determining whether Ishimaru was excused from making demand on Fung as the managing member of Paradigm.

Under the substantive law of Delaware, a court will find demand futility where "the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could

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[17] 6 *Del. C.* §18-1001.
[18] 6 *Del. C.* §18-1003.
[19] 6 *Del. C.* §17-1001.
[20] *Litman v. Prudential-Bache Properties, Inc.*, 1993 WL 5922 (Del. Ch. Jan. 4, 1993).
[21] *VGS, Inc. v. Castiel*, 2003 WL 723285 (Del. Ch. Feb. 28, 2003).

have properly exercised its independent and disinterested business judgment in responding to a demand."[22] Ishimaru easily satisfies the statutory requirement to plead demand excusal with particularity. She sets forth with particularity that Fung sought to strike a deal for himself personally with Ivy Asset in Europe that would have permitted him, to the exclusion of the Joint Venture and Paradigm, to exploit the benefits of PILS in Europe. Part of Fung's strategy was to compromise away the Joint Venture's and Paradigm's rights in Japan so as to further his own personal ends.

Fung's contention that the Paradigm LLC Agreement made him managing member with the initial authority to decide whether to sue does not aid him in opposing Ishimaru's wish to proceed as a derivative plaintiff, nor do the provisions of the LLC Agreement that permit Fung to consider his own interests in making certain decisions for Paradigm. As is common in LLC Agreements these days, the provisions dealing with the managing member's duties and rights in the Paradigm LLC Agreement can be read as contradictory and confusing. But the Paradigm LLC Agreement denies exculpation to the managing member for conduct that constitutes fraud, gross negligence, willful misconduct, or an intentional breach of the LLC Agreement.

The behavior that Ishimaru alleges is, if true, obviously the kind of willful misconduct that cannot be exculpated. In other words, although Fung might have been free to pursue opportunities in Europe outside of Paradigm and the Joint Venture using solely his own wiles, he could not usurp, without breaching § 9.03 of the Joint Venture Agreement, proprietary information and other assets (such as claims Paradigm and the

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[22] *Rales v. Blasband*, 634 A.2d 927, 934 (Del. 1993).

Joint Venture had against Ivy Asset and Ivy International) for himself, thereby purposely transferring wealth from them to himself.

In view of that reality, I have little difficulty in concluding that Ishimaru may press the New Bargain Claim derivatively on behalf of Paradigm.[23]

B. Must Paradigm Arbitrate Its Claim Against Ivy Asset?

Ivy Asset has moved under Rule 12(b)(1) to dismiss for lack of subject matter jurisdiction, alleging that Paradigm is bound to arbitrate its claims and may not press them in this court. In analyzing a motion to compel arbitration, "the question of whether the parties agreed to arbitrate . . . is generally one for the courts and not for the arbitrators."[24] In determining arbitrability, I must ascertain whether the dispute is one that, on its face, falls within the arbitration clause of the contract.[25]

In interpreting the Arbitration Clause, Delaware public policy comes into play and requires that doubts should be resolved in favor of arbitrability when a reasonable interpretation in that direction exists.[26] The strong federal policy to the same effect also applies in this case because the parties chose to submit their disputes to arbitration in a

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[23] Without dilating on the point, I want to make clear my own recognition that the claim Ishimaru seeks to press may be better conceived of as a double derivative claim. That is, in actuality, the party that was directly injured by any breach of the New Bargain was the "unified front," the Joint Venture, which was bypassed by Ivy Asset. The harm to Paradigm is indirect, resulting from the failure of Ivy Asset to conduct its business in Japan through the Joint Venture and to share the agreed-upon fees with the Members of the Joint Venture. Even more clearly, the claims against Ivy Asset that supposedly led it to agree to the New Bargain were ones possessed by the Joint Venture in the first instance. Neither party has picked up on the double derivative aspect of the New Bargain Claim, perhaps because it is obvious that Ivy International could block the Joint Venture from pressing claims and that Ivy International cannot impartially decide whether the Joint Venture should sue Ivy Asset.
[24] *SBC Interactive, Inc. v. Corporate Media Partners*, 714 A.2d 758, 761 (Del. 1998).
[25] *Id.*
[26] *Id.*

manner implicating the Federal Arbitration Act. In applying state-law principles of contract interpretation to an arbitration agreement "within the scope of the [FAA]," "due regard must be given to the federal policy favoring arbitration, and ambiguities as to the scope of the arbitration clause" must be resolved in favor of arbitration.[27] But, when there is no reasonable contractual or other legal or equitable basis for subjecting a resisting party to arbitration, the court cannot mandate resort to that process.[28]

Here, the ultimate question of arbitrability hinges on two subordinate inquiries. One inquiry is whether the New Bargain Claim has a sufficient relationship to the Joint Venture Agreement to fall within the scope of the Arbitration Clause. If the answer is yes, then it must be determined whether Ivy Asset, which is neither formally a "Member" of the Joint Venture nor mentioned in the Arbitration Clause, may nonetheless require Paradigm, which is a Member mentioned in the Arbitration Clause, to arbitrate, rather than litigate, the New Bargain Claim. As I will make clear, the factual allegations of Ishimaru's complaints that make clear that the New Bargain Claim falls within the scope of the Arbitration Clause also bear on the question of whether Ivy Asset may require Paradigm to arbitrate.

1. The New Bargain Claim Is A Dispute "Concerning" The Joint Venture Agreement

Although she denies her purpose was tactical, Ishimaru recast her complaint in a manner that helps her argue that the New Bargain was a stand-alone contract existing

[27] *Dresser Indus., Inc. v. Global Indus. Tech., Inc.*, 1999 WL 413401, at *4 (Del. Ch. June 9, 1999) (quoting *Volt Info. Sci., Inc. v. Bd. of Tr. of Leland Stanford Junior Univ.*, 489 U.S. 468, 475-76 (1989)).
[28] *SBC Interactive*, 714 A.2d at 761.

wholly apart from, and not as an evolutionary amendment of, the Joint Venture Agreement. She contends that the Arbitration Clause is narrow because it only addresses disputes "concerning" the Joint Venture Agreement, and not disputes "relating in any way" to that Agreement, as some arbitration clauses state. In an athlete, sheer force can sometimes render excusable or irrelevant a lack of subtlety and grace. But the logical force of Ishimaru's argument is underwhelming and provides no cover for her ham-handed pleading amendments.

For starters, Ishimaru makes an unpersuasive argument that the Arbitration Clause in the Joint Venture Agreement is narrow. In so contending, Ishimaru relies on the Supreme Court's decision in *Parfi Holding AB v. Mirror Image Internet, Inc.*,[29] holding that when a party brings an action to compel arbitration, a court must determine whether the arbitration clause in question is broad or narrow in scope.[30] If the clause is broad, then the court must "defer to arbitration on any issues that touch on contract rights or contract performance."[31] If the clause is narrow, the court "will ask if the cause of action pursued in court directly relates to a right in the contract."[32] Here, the Arbitration Clause provides:

> each Member agrees to submit all controversies arising between Members, or one or more Members and the Company, concerning this Agreement to arbitration in accordance with the provisions set forth below . . . [a]ll controversies that may arise among Members and one or more Members and the Company concerning this Agreement shall be determined by arbitration in New York City . . . to the fullest extent permitted by law.

[29] *Parfi Holding AB v. Mirror Image Internet, Inc.*, 817 A.2d 149 (Del. 2002).
[30] *Id*. at 155.
[31] *Id*.
[32] *Id*.

In *Parfi*, the Supreme Court held that a clause containing the words "any dispute, controversy, or claim arising out of or in connection with" a contract was broad.[33] Ishimaru argues that, in contrast, the language in the Arbitration Clause in the Joint Venture Agreement is much narrower.[34] I, however, do not find the distinctions in language to be of material importance in addressing the current dispute. The difference between using the words "concerning this Agreement," rather than the words "arising out of this Agreement," is slight, if extant. A primary definition of "concerning" is "relating to, regarding."[35] The expressed desire to arbitrate any claims that relate to the parties' agreement encapsulates a broad array of claims. Therefore, as the arbitration clause is broad, I consider "any issues that touch on contract rights or contract performance" to be within the scope of the Arbitration Clause.[36]

Ishimaru's allegation that Ivy Asset breached the New Bargain clearly touches on contract rights and performance under the Joint Venture Agreement. To begin with, the origins of the New Bargain are rooted entirely in the Joint Venture Agreement. Ishimaru contends that Ivy Asset had been violating obligations it owed to the Joint Venture under the Joint Venture Agreement by marketing competing products in Japan. Although Ishimaru's amended complaint attempts to root that alleged violation in Ivy Asset's use

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[33] *Id.*
[34] *Id.* (subjecting all claims "arising out of or in connection with" the agreement to arbitration).
[35] *Merriam-Webster OnLine Dictionary* (2005). *See also The Concise Oxford Dictionary of Current English* (9th ed. 1995) (defining "concerning" as "about, regarding"); *Webster's Desk Dictionary* (1996) (defining "concerning" as "relating to; regarding; about"); *Webster's Ninth New Collegiate Dictionary* (1990) (defining "concerning" as "relating to: regarding").
[36] *Parfi Holding*, 817 A.2d at 155.

of information it learned from Ivy International through the Joint Venture, even that explanation connects Ivy Asset's allegedly wrongful behavior to the Joint Venture Agreement. In essence, Ishimaru argues that Ivy Asset was breaching obligations it owed to the Joint Venture under § 9.03 not to misuse confidential information of the Joint Venture.

More fundamentally, the amended complaint continues to accuse Ivy Asset of breaching obligations it owed to the Joint Venture simply by marketing its own products in Japan other than through the Joint Venture. The basis for this argument is block quoted in the amended complaint and is a portion of the Business Plan for 2000-2001, adopted pursuant to § 1.03(a) of the Joint Venture Agreement. That portion states that "The JV recognizes the importance of gaining investors quickly as competitors can easily establish similar offerings. Both joint venture partners remain committed to the business plan and will not engage in substantially similar businesses targeted at the Japanese market which may damage the success of the JV."[37] By Ivy, that Business Plan is clearly referring not only to Ivy International, but to Ivy Asset. Indeed, to read it otherwise would be to conclude, contrary to Ishimaru's argument, that this promise did not bind Ivy Asset at all.

As we know, eventually Paradigm and Ivy Asset conducted negotiations to resolve their disagreement about whether Ivy Asset's activities in Japan breached obligations it owed to the Joint Venture. It bears pausing a moment to emphasize that point. To the extent Ivy Asset was marketing products in Japan directly, it was bypassing the Joint

[37] Am. Compl. ¶¶ 14-15.

Venture. Any harm to Paradigm from Ivy Asset's competitive activities in Japan was indirect and arose from the direct injury to the Joint Venture's rights.

When Paradigm and Ivy Asset were haggling over their dispute, it thus is clear that they were acting in their capacities as Joint Venturers. In that process, Ivy Asset and Ivy International did not have separate negotiators. Ivy International had no operatives separate from Ivy Asset. The officers who acted for the Ivy entities, Simon and Lindenbaum, were top officers of both entities.[38] In all material respects, Ivy International was simply the liability- and tax-insulating vehicle used by Ivy Asset to conduct its Joint Venture with Paradigm. The Business Plans of the Joint Venture recognize this, by expressly treating Ivy Asset as if it were the Member and assigning it direct responsibilities.

As even the amended complaint states, the New Bargain was an agreement "to resolve the claims that Ivy International was harming PI's business by allowing its parent access to PI's Japanese contacts."[39] The problem that poses for Ishimaru's argument that her claims do not concern the Joint Venture Agreement is insurmountable.

By virtue of § 9.01 of the Joint Venture Agreement, an amendment could only be accomplished by a writing signed by both of the Members. But Ishimaru disclaims the notion that Ivy International was a party to the New Bargain, arguing that the only parties were Ivy Asset and Paradigm. That contention, which is contrary to the original

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[38] In fact, it is not clear from the complaints whether Lindenbaum even had a position with Ivy International.
[39] Am. Compl. ¶ 29.

complaint, seems entirely implausible, but, even if true, does not aid Ishimaru in escaping arbitration.

By its plain terms, the New Bargain had several profound implications for the Joint Venture. The New Bargain had the effect of compromising away claims of the Joint Venture against Ivy Asset, both for damages for past conduct and for injunctive relief against future competition. If the New Bargain was in place, then Ivy Asset was free to exploit the Japanese contacts it had made through the Joint Venture in order to sell its own existing products, so long as it paid the fees outlined in the New Bargain. The New Bargain also changed the fee split between the Joint Venture partners in an important, related manner. To the extent that the Joint Venture Agreement was not amended, Ivy Asset would arguably have been required to conduct the marketing of its own products in Japan (at least as to contacts first identified by the Joint Venture) through the Joint Venture and to split the fees equally between the Joint Venture partners, per §§ 3.04-3.05 of the Joint Venture Agreement. By contrast, the New Bargain permitted Ivy Asset to market its existing products in Japan on a much more favorable 75%-25% split.

To salvage this part of her argument, Ishimaru seeks to distance herself from the plain language of the New Bargain. She says the New Bargain is not a "reaffirmation" of the Joint Venture Agreement, as the original complaint expressly characterized it,[40] but instead largely a complete substitute. But the words of the New Bargain itself are at odds with that claim.

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[40] Compl. ¶ 51.

The first operative part of the New Bargain flatly states: "all Ivy business in Japan will be conducted by the joint venture. The joint venture will be the unified front offering all Ivy related products and services in Japan."[41] It then goes on to explain what the economic implications would be for the Joint Venture partners depending on what product was sold in Japan and how the buyer came to be identified. By its plain terms, the New Bargain implies the Joint Venture would become the marketing force — the "unified front" — for all of Ivy Asset's products to be sold in Japan. When the product sold through the unified front was one developed by Ivy Asset alone, its Joint Venture vehicle, Ivy International, would get a higher amount. This different split obviously altered provisions of the Joint Venture Agreement.[42]

Ishimaru resists this reading, however. She contends that, after the New Bargain, the Joint Venture only would be involved in selling products it developed itself. Ivy Asset would market its own products in Japan, and Paradigm would help in that regard. If an Ivy Asset product was sold in Japan, Ivy Asset would get 75% of the proceeds, Paradigm would get 25%, and none of the funds would flow through the Joint Venture.

That construction necessarily depends on the Joint Venture being not much of a "unified front" at all despite the plain words of the New Bargain, a construction at odds with the notion that the New Bargain is clear enough to be capable of enforcement as a contract. More importantly, if true, that construction requires acceptance of the fact that Ivy Asset, a non-party to the Joint Venture Agreement, could compromise away rights of

[41] Ishimaru Ans. Br. Ex. A.
[42] *See* JVA §§ 3.04-3.05.

the Joint Venture through a contract with Paradigm to which Ivy International was not a party.

Stated bluntly, if Ishimaru is correct, then viable claims of the Joint Venture against Ivy Asset were compromised away in a contract that did not involve Ivy International. The New Bargain resulted in Ivy Asset being able to market its products in Japan using information derived from the Joint Venture and to receive the proceeds directly so long as it later turned over to Paradigm 25% of the fees. That compromise cut the Joint Venture out entirely, and therefore meant that Ivy International, a supposedly separate entity with separate legal dignity, received nothing! Under the Joint Venture Agreement, the two Members were Paradigm and Ivy International and under § 2.01 neither was permitted to act unilaterally. Therefore, to the extent the Joint Venture was to compromise away its rights, Ivy International had to be a party to the New Bargain and, along with its fellow member Paradigm, had to assent to that compromise on the Joint Venture's behalf.

Under Delaware law, the New Bargain must be analyzed in "the context of the on-going relationship of the parties."[43] Ishimaru will surely argue that the New Bargain is an enforceable, sensible, and understandable contract, when viewed in light of the evolving course of dealing under the Joint Venture Agreement. Likewise, Paradigm will no doubt look to the Joint Venture Agreement as the gap-filler for any unspecified details or references in the terse e-mail exchange that comprises the New Bargain. As important, Paradigm's New Bargain claim necessarily depends on the premise that the New Bargain

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[43] *Seiler v. Levitz Furniture Co. of E. Region, Inc.*, 367 A.2d 999, 1005 (Del. 1976).

either validly amended the Joint Venture or compromised away claims and rights of the Joint Venture, or, most likely, both. In all scenarios, the New Bargain claim rests on the assertion that rights belonging to both the Joint Venture and Ivy International could be altered in a contract exclusively between Ivy Asset and Paradigm.

In defending itself against the New Bargain claim, Ivy Asset will wish to argue that, per the terms of the Joint Venture, the New Bargain is not formal or specific enough to serve as an amendment to the Joint Venture Agreement. It will also argue that no amendment to the Joint Venture Agreement (or compromise of the Joint Venture's rights) could be made without Ivy International's assent. Perhaps of most importance, Ivy Asset will seek to explain the New Bargain in view of the limited duties Ivy Asset owed the Joint Venture and to use provisions of the Joint Venture Agreement as a defense.

The inescapable reality therefore is that any adjudication of the New Bargain will center on the Joint Venture Agreement, the parties' course of dealing under it, and the extent to which the business plans adopted pursuant to § 1.03(a) and the New Bargain modified the Joint Venture and the rights and duties of Ivy International, Ivy Asset, Paradigm, and the Joint Venture itself. Thus, the New Bargain claim clearly "concern[s]" the Joint Venture Agreement in a manner governed by the Arbitration Clause.

2. May Ivy Asset Require Paradigm To Arbitrate Even Though Ivy Asset Was Not Formally A Member Of The Joint Venture?

The fact that Paradigm asserts a dispute concerning the Joint Venture Agreement does not suffice to determine the question of whether Ivy Asset can force Paradigm to arbitrate. By its terms, the Arbitration Clause only applies to disputes between Members,

or between a Member and the Joint Venture. Member is defined early in the Joint Venture Agreement in a manner that does not sweep in affiliates like Ivy Asset, even though such affiliates are expressly dealt with in other provisions of the Joint Venture Agreement and even impressed by the Agreement with contractual duties to the Joint Venture (e.g., a duty to not to misuse the Joint Venture's confidential information[44]), as well as contractual rights (e.g., indemnification).[45] Ishimaru argues that because the Joint Venture Agreement took care to distinguish Members from their affiliates and the Arbitration Clause addresses Members only, Ivy Asset, as a non-Member, may not compel Paradigm to arbitrate the New Bargain Claim.

But, in so arguing, Paradigm slights the well-established proposition that a signatory to an Arbitration Clause, such as itself, may be required to arbitrate with a non-signatory when, among other grounds, concepts of equitable estoppel dictate that result.[46] Although there is a debate in the law at times about the precise factual circumstances in which those principles might require a signatory to arbitrate with a non-signatory, there is no debate that there are circumstances in which those principles have that effect. Indeed, principles of equitable estoppel may even operate to bind a non-signatory to an arbitration clause to arbitrate with a signatory.[47]

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[44] JVA § 9.03.

[45] JVA § 2.07. Other rights are contained in § 2.05 (right to compete on certain terms), § 2.06 (exculpation), § 1.08 (transfers of interest) and described earlier in this decision.

[46] *E.g., First Options Of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944 (1995).

[47] The various legal and equitable principles (e.g., agency, veil piercing, equitable estoppel, assumption by conduct) that can be deployed to require a signatory to arbitrate with a non-signatory can also be used to require a non-signatory to arbitrate with a signatory. *Id. See also Thomson-CSF, S.A.,* 64 F.3d at 776 (reciting examples of theories that enable these results).

Here, the circumstances clearly warrant an order requiring Paradigm to arbitrate its New Bargain Claim against Ivy Asset. One of the primary justifications for estopping a signatory from denying a non-signatory a right to arbitrate is that it is unfair for the signatory to have it both ways by attributing to a non-signatory the duties of a contract signatory for purposes of pressing claims but denying the non-signatory the right to invoke the arbitration clause.[48] In this case, the justification for estoppel is compelling and rests on grounds that would support the applicability of another theory that, when applicable, can be used to require a signatory to arbitrate with a non-signatory: veil piercing. But equitable estoppel is more appropriate because it is Ishimaru who is simultaneously arguing that the separate corporate existence of Ivy International has no dignity (when that is critical to the vitality of the merits of her New Bargain Claim) and that the separate corporate existence of Ivy International must be recognized and respected (when that aids her in refusing to arbitrate with Ivy Asset).

In other words, the New Bargain Claim is premised on the notion that Ivy Asset, as matter of fact, was so dominant of, and so indistinct from, its mere tool Ivy International that it could act unilaterally as if it were a Member of the Joint Venture. As already explained, the New Bargain, if enforceable in the manner Ishimaru suggests,

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[48] *E.g., Hughes Masonry Co., Inc. v. Greater Clark County School Bldg. Corp.*, 659 F.2d 836, 838-39 (7th Cir. 1981) ("we believe it would be manifestly inequitable to permit Hughes to both claim that J.A. is liable to Hughes for its failure to perform the contractual duties described in the . . . agreement and at the same time deny that J.A. is a party to that agreement in order to avoid arbitration of claims clearly within the ambit of the arbitration clause"); *Grigson*, 210 F.3d at 528 (quoting *MS Dealer Serv. Corp. v. Franklin*, 177 F.3d 942, 947 (11th Cir. 1999)) ("a signatory . . . cannot 'have it both ways': it cannot, on the one hand, seek to hold the non-signatory liable pursuant to duties imposed by the agreement, which contains an arbitration provision, but, on the other hand, deny arbitration's applicability because the defendant is a non-signatory").

compromised away claims of the Joint Venture and altered the fee split contained in the Joint Venture Agreement. The New Bargain therefore affected both the rights of Ivy International and the Joint Venture, a result that could only be accomplished through an agreement between the Members of the Joint Venture. Because Ishimaru claims that Ivy International was not a party to the New Bargain, she is indisputably arguing that its separate existence need not be respected because Ivy Asset could compromise away the Joint Venture's and Ivy International's rights without any act by Ivy International itself. Ishimaru therefore plainly argues that Paradigm treated Ivy Asset as a Member of the Joint Venture and that Ivy Asset should be held responsible in that capacity.

Having taken this tack, Ishimaru must accept the consequences that accompany it. Under much less clear circumstances, courts have bound a signatory to arbitrate "at the nonsignatory's insistence because of the 'close relationship between the entities involved, as well as the relationship of the alleged wrong to the nonsignatory's obligations and duties in the contract . . . and [because] the claims were intimately founded in and intertwined with the underlying contract obligations.'"[49] In this case, Ishimaru has herself attributed to the non-signatory, Ivy Asset, the duties and powers of a signatory, and pled that Ivy International is a nullity. Therefore, I grant Ivy Asset's motion and dismiss this case because the New Bargain claim must be arbitrated.[50]

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[49] *Thomson-CSF, S.A.*, 64 F.3d at 778 (quoting *Sunkist Soft Drinks*, 10 F.3d at 757) (quoting *McBro Planning & Dev*, 741 F.2d at 344) (first set of internal quotations omitted).

[50] In so ruling, I reject Ishimaru's argument that she stands in the same position as the party, the DuPont Company, seeking to avoid arbitration in the case of *E.I. DuPont de Nemours & Co. v. Rhone Poulence Fiber and Resin Intermediates, S.A.S. et al*, 269 F.3d 187 (3d Cir. 2001). Admittedly, Ishimaru cites that case for good reason. Like herself, DuPont took a very tactical

approach to pleading in that case. In its original complaint, DuPont pled that it was a third-party beneficiary of a joint venture agreement to which one of its subsidiaries was a party. DuPont alleged that it, and the parent company on the other side of the joint venture, entered into a later agreement whereby the two parents promised to provide loan guarantees for the joint venture and for the parents to "abide by the obligations contemplated by the [joint venture agreement]." *Id.* at 193.

When faced with a motion to refer its claim to arbitration, DuPont amended its pleading to wriggle out of arbitration. Had it continued to allege that it was a third-party beneficiary of the original joint venture agreement, DuPont appeared to recognize that it would have had to arbitrate. Therefore, it amended its complaint and alleged that the later agreement was a separate, new contract from the joint venture agreement and that DuPont, as a non-signatory to the contract containing the arbitration clause, could not be compelled to arbitrate its claim.

The facts in the case were complicated but essentially DuPont was alleging that it, as parent of one joint venturer, had reached a completely separate, new agreement with the parent of the other joint venturer, whereby each parent agreed to support the joint venture and to cause their subsidiary joint venturers to do the same. DuPont, after amending its complaint, clung to the theory that its claims found their essence only in this new agreement and therefore were outside the arbitration clause of the original joint venture agreement. The U.S. Court of Appeals for the Third Circuit ultimately bought that argument, while admitting that it was making a "close call." *Id*. at 201.

The court's decision involved different facts than this case, and those differences are legally material. For one thing, unlike in this case, the supposedly new contract that DuPont entered into did not have the effect of negatively affecting the rights of the joint venture or one of the joint venturer subsidiaries in a contract to which neither the joint venture nor the subsidiaries were a party. Here, if the New Bargain is enforceable, it compromised rights of the Joint Venture and changed the Joint Venture Agreement, the type of contract only the two Members of the Joint Venture could execute. Unlike the new agreement in *E.I. DuPont*, which perpetuated the existing joint venture, but with additional promises by the parents to provide support, the New Bargain changed the rights of the Joint Venture and the economic returns to the Members of the Joint Venture. Therefore, Ishimaru is alleging that Ivy Asset could act as a Member but is also seeking to deny it the rights of a Member. That was not as plainly the case in *E.I. DuPont*.

Equally important, in *E.I. DuPont*, the parties seeking to require DuPont to arbitrate argued that it did not matter that DuPont was a non-signatory rather than a signatory of the joint venture agreement containing the arbitration clause. Therefore, they contended that the court should feel as comfortable requiring DuPont to arbitrate as if it would have been in compelling a signatory to arbitrate with a non-signatory. The court expressly rejected that argument, stating that there was an important distinction between the two contexts, and that "'the circuits have been [more] willing to estop a signatory from avoiding arbitration with a nonsignatory when the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed.'" *Id.* at 202 (quoting *Thomson-CSF, S.A.*, 64 F.3d at 779); *see also CD Partners, LLC v. Grizzle,* 424 F.3d 795, 799 (8th Cir. 2005) (recognizing that it is less

III. Conclusion

For the foregoing reasons, Ishimaru is entitled to an order permitting her to press Paradigm's New Bargain Claim against Ivy Asset as a derivative plaintiff. But she must press that Claim in arbitration, in accordance with the procedures in the Arbitration Clause. The parties shall confer and submit an implementing final judgment within five days.

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difficult to obtain an order requiring a signatory to arbitrate with a non-signatory than vice versa).