



1 as to the remainder of the Defendants pending conclusion of the anticipated arbitration  
2 proceeding. The parties are also instructed to file a joint status report on the status of  
3 the arbitration proceeding by June 1, 2018.

#### 4 **BACKGROUND**

5 On July 20, 2017, Plaintiff, a citizen of California, commenced this diversity  
6 action by alleging two claims for fraud and unfair business practices in violation of Bus  
7 & Prof Code §17200 et seq. Plaintiff's claims relate to an exclusive distributorship  
8 agreement entered into between Everest and BSPG, an entity organized and with its  
9 principal place of business in Hong Kong. Defendant Trigal Pharma Ltd. is an entity  
10 allegedly organized and with its principal place of business in Vienna, Austria;  
11 Hankang Bio-tech Ltd. is an entity allegedly organized and with its principal place of  
12 business in The Peoples Republic of China; BSPG Laboratories Ltd. is an entity  
13 allegedly organized and with its principal place of business in the United Kingdom;  
14 and Michael Stephenson is an alleged resident of the United Kingdom and an officer  
15 and shareholder of the alleged defendant business entities. (Compl ¶¶2 - 10).  
16 Defendants Biosynthesis Pharma Limited, Jaytee Biosciences Ltd., Iefenbaacher API  
17 GmbH, and SPG Austria GmbH, all alleged foreign entities, have yet to appear in this  
18 action.

19 In April 2015, Plaintiff and BSPG entered into an Exclusive Distribution  
20 Agreement ("Agreement") for the distribution of cannabidol ("CBD") in the United  
21 States. CBD is an industrial hemp product used for homeopathic, holistic, and  
22 naturopathic purposes. CBD does not contain THC, an active ingredient in marijuana.  
23 Pursuant to the Agreement, Plaintiff paid \$2 million for the exclusive right to distribute  
24 CBD in the United States. Defendant Stephenson allegedly represented that "his  
25 companies would turn over their existing clients in the United States to Plaintiff."  
26 (Compl. ¶14). The Agreement had a set purchase price of \$30,000 per kilo of CBD,  
27 and a set sales price of not less than \$40,000 per kilo.

28 Shortly after executing the Agreement, Plaintiff learned that Defendants had

1 distributed CBD to other companies in the United States. When confronted about the  
2 sale, Stephenson informed Plaintiff that the single shipment of CBD corresponded to  
3 an order placed before executing the Agreement. After this meeting, Plaintiff  
4 continued to be informed, and then discovered, that Defendants, collectively, continued  
5 to sell CBD in the United States.

6 When confronted about BSPG product sales by third parties, Defendant  
7 Stephenson stated that “enforcing any rights under the Agreement was the  
8 responsibility of Plaintiff.” (Compl. ¶17). Plaintiff then began to send cease and desist  
9 letters to the several companies that were selling Defendants’ products. In response,  
10 Defendants sent an email to Plaintiff unilaterally terminating the Agreement “without  
11 a factual basis.” (Compl. ¶18).

12 Seeking to enforce its rights under the Agreement, Plaintiff commenced  
13 litigation in the Superior Court of San Diego County against Visage Pro USA, LLC to  
14 stop the unauthorized sale of CBD products produced by Defendants. In this litigation,  
15 Plaintiff allegedly learned the true facts “that Defendants never had any intent to  
16 provide an exclusive distributorship to Plaintiff.” (Compl. ¶19). Plaintiff learned that  
17 Defendants continued to sell CBD in the United States before and during the period of  
18 exclusivity. Defendants allegedly made direct and continuous sales to Visage Pro USA  
19 and other vendors throughout the period of exclusivity in alleged violation of the  
20 Agreement. For example, one email from Defendant Stephenson, dated July 2, 2015,  
21 allegedly revealed Defendants’ plan to continue to sell CBD to Visage Pro USA and  
22 to disguise the origins of the product to avoid detection by Plaintiff. (Compl. ¶24).

23 The Agreement provides for the arbitration of any and all disputes in Hong  
24 Kong. Defendants move to compel arbitration of the claims asserted against BSPG,  
25 and to stay the claims asserted against the remainder of the Defendants pending  
26 resolution of the arbitration proceedings. Plaintiff opposes the motion and claims the  
27 Agreement is void ab initio based upon a fraud in the execution theory.

28

## DISCUSSION

### The Arbitration Provision

The Federal Arbitration Act (“FAA”) provides that

a written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising . . . shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or equity for the revocation of any contract.

9 U.S.C. §2. The FAA establishes federal policy favoring arbitration of disputes. Federal courts are required to “rigorously” enforce the parties’ agreement to arbitrate. Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 226 (1987). Indeed, “any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language or an allegation of waiver, delay, or a like defense to arbitrability.” Moses H. Cone Memorial Hosp. v. Mercury Const. Corp., 460 U.S. 1, 24 (1983).

[W]here a contract contains an arbitration clause, there is a presumption of arbitrability in a sense that [a]n order to arbitrate the particular grievance should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute. Doubts should be resolved in favor of coverage.

A.T.&T. Tech. Inc. v. Communications Workers of America, 475 U.S. 643, 650 (1986) (citations omitted).

The FAA creates “a body of federal substantive law of arbitrability,” enforceable in both state and federal courts and preempting any state laws or policies to the contrary. Moses H. Cone, 460 U.S. at 24. “The availability and validity of defenses against arbitration are therefore to be governed by application of federal standards.” Cohen v. Wedbush, Noble, Cooke, Inc., 841 F.2d 282, 285 (9th Cir. 1988). This body of federal law also requires that federal courts apply state law, “whether of legislative or judicial origin [] if that law arose to govern issues concerning the validity, revocability and enforceability of contracts generally.” Perry v. Thomas, 482 U.S. 483, 493, fn. 9 (1987).

This court’s inquiry is a narrow one, limited to determining whether the

1 arbitration provision is enforceable. The court concludes that it is. The arbitration  
2 provision is clear and concise and evidences the parties' intent to arbitrate any and all  
3 disputes concerning the Agreement. Section 9.07 of the Agreement requires disputes  
4 "arising out of or in connection with" that contract to be resolved through arbitration.

5 The Agreement provides:

6 Any dispute arising out of or in connection with this Agreement,  
7 including any question regarding its existence, validity or termination,  
8 shall be referred to and finally resolved by arbitration under Hong Kong  
9 International Arbitration Centre (HKIAC) under the HKIAC  
Administered Arbitration Rules in force, when the Notice of Arbitration  
is submitted; which Rules are deemed to be incorporated by reference into  
this clause;

10 (a) The number of arbitrators shall be two;

11 (b) The seat, or legal place, of arbitration shall be Hong  
Kong SAR. The language to be used in the arbitral proceedings  
shall be English;

12 (c) The governing law of the contract shall be the substantive law of Hong  
Kong.

13 (Compl. Exh. 1 ¶ 9.2). Plaintiff's claims for fraud and violation of Bus & Prof Code  
14 §17200 arise directly from the Agreement. In broad brush, Plaintiff alleges that the  
15 Agreement was a sham because BSPG made material misrepresentations regarding the  
16 exclusivity of the CBD sales territory while BSPG allegedly sold product within  
17 Plaintiff's exclusive territory. As the claims arise or relate to the Agreement, the court  
18 compels arbitration of Plaintiff's claims against BSPG.

### 19 **Fraud in the Execution of the Agreement**

20 In opposing the motion to compel arbitration, Plaintiff contends that Defendants  
21 engaged in fraud in the execution, and therefore the entire contract is void, including  
22 the arbitration provision. See Duick v. Toyota Motorsales, U.S.A., Inc., 198  
23 Cal.App.4th 1316, 1320 (12011). Plaintiff's argument is not persuasive because  
24 Plaintiff's fraud claims are "fraud in the inducement" of a contract, and not fraud in the  
25 "execution" of a contract. As explained in Rosenthal v. Great Western Fin. Securities  
26 Corp., 14 Cal.4th 394, 415 (1996) (fraud in the execution voids the entire contract,  
27 including the arbitration provision), in the case of fraud in the execution,

28 the fraud goes to the inception or execution of the agreement, so that the

1 promisor is deceived as to the nature of his act, and actually does not  
2 know what he is signing, or does not intend to enter into a contract at all,  
3 mutual assent is lacking, and [the contract] is void. In such a case it may  
4 be disregarded without the necessity of rescission.

5 (quoting Ford v. Shearson Lehman American Express, Inc., 180 Cal.App.3d 1011  
6 (1986). Fraud in the inducement, by contrast, occurs when “ the promisor knows what  
7 he is signing but his consent is induced by fraud, mutual assent is present and a  
8 contract is formed, which, by reason of the fraud, is voidable. In order to escape from  
9 its obligations the aggrieved party must rescind.” Id.

10 Here, Plaintiff clearly and unequivocally alleges that it negotiated with  
11 Defendants for the express purpose and intent to obtain an exclusive distributorship  
12 agreement for CBD. Moreover, the Complaint alleges that the parties to the Agreement  
13 conducted extensive research and discussions before executing the Agreement.  
14 (Compl. ¶¶12-15). The Complaint’s allegations simply fail to give rise to an inference  
15 that Plaintiff, when it executed the Agreement, did not know that it entered into a  
16 contract at that time.

### 17 **Unconscionability**

18 The court also rejects Plaintiff’s argument that the arbitration provision is  
19 unconscionable because “the contract was written to make it difficult for Plaintiff to  
20 pursue Defendants in litigation.” (Oppo. at p.7:14-15).

21 Under California state law, the court may invalidate an unconscionable contract  
22 provision. Civil Code section 1670.5, subdivision (a) states: “If the court as a matter  
23 of law finds the contract or any clause of the contract to be unconscionable at the time  
24 it was made the court may refuse to enforce the contract, or it may enforce the  
25 remainder of the contract without the unconscionable clause, or it may so limit the  
26 application of any unconscionable clause as to avoid any unconscionable result.”

27 Unconscionability has both a procedural and a substantive element. Stirlen v.  
28 Supercuts, Inc., 51 Cal.App.4th 1519, 1531 (1997). Both elements must be present for  
a contract or a clause therein to be invalidated, but they need not be present in the same  
degree. Armendariz v. Found Health Psychare Servs., 24 Cal.4th 83, 114 (2000);

1 Stirlen, 51 Cal.App.4th at 1533. A sliding scale is utilized so that, for example, the  
2 more substantively oppressive a contract is, the lesser the showing of procedural  
3 unconscionability is required to conclude the contract is unconscionable. Armendariz,  
4 24 Cal.4th at 114.

5 Procedural Unconscionability

6 Procedural unconscionability is oppression or surprise arising out of unequal  
7 bargaining power, which results from a lack of real negotiations and the absence of  
8 meaningful choice. Stirlen, 51 Cal.App.4th at 1532. Procedural unconscionability  
9 often arises when the contract in question is one of adhesion. Id. at 1533. A contract  
10 of adhesion is a “a standardized contract, which, imposed and drafted by the party of  
11 superior bargaining strength, relegates to the subscribing party only the opportunity to  
12 adhere to the contract or reject it.” Id.

13 Here, the contract is not one of adhesion and was bargained for by the parties.  
14 Several factors weigh against a finding of procedural unconscionability: (1) the parties  
15 negotiated the Agreement over an extended period of time and Plaintiff cannot now  
16 claim that it was surprised by the existence of the arbitration provision; (2) the amount  
17 of the Agreement (\$2,000,000) is sufficient for the parties to have carefully considered  
18 the terms and conditions of the Agreement, including consultation with business and  
19 legal advisors; (3) Plaintiff intended to deal with BSPG, and not some other  
20 manufacturer of CBD; and (4) the amount of the contract and business plans of the  
21 parties reflect a level of sophistication and business planning indicative of  
22 sophisticated business entities. Finally, the court rejects Plaintiff’s argument that the  
23 arbitration provision is procedurally unconscionable because it is a corporation  
24 “formed by a few young men just starting out in the business world.” (Oppo. at p.7:23-  
25 24). Even assuming some of the shareholders of Plaintiff are young, Plaintiff fails to  
26 explain how this allegation is relevant, especially where there is no discussion as to  
27 Plaintiff’s business experience, financial wherewithal, and other pertinent  
28 considerations.

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Substantive Unconscionability

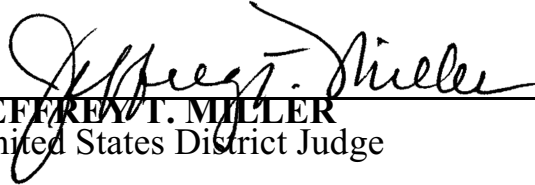
Substantive unconscionability arises when (1) the contract terms are so one-sided as to shock the conscience or (2) the contract terms imposed are harsh or oppressive. Stirlen, 51 Cal.App.4th at 1532. Plaintiff contends that the arbitration provision is substantively unconscionable because it calls for the arbitration to proceed in Hong Kong, and not the United States. Plaintiff sets forth no basis to conclude that arbitration in Hong Kong, a major global trading center, is so one-sided as to shock the conscience or is overly harsh or oppressive. The court concludes that the asserted grounds for substantive unconscionability are commonplace and insufficient to establish substantive unconscionability.

In sum, applying the Armendariz sliding scale, Plaintiff falls short of establishing the unconscionability of the arbitration provision.

In conclusion, the court grants the motion to compel arbitration of Plaintiff's claims against BSPG. The court also stays this action as to the remainder of the Defendants pending arbitration and instructs the parties to file a joint status report by June 1, 2018. The joint report should inform the court of the status of the arbitration proceeding.

**IT IS SO ORDERED.**

DATED: January 8, 2018

  
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**JEFFREY T. MILLER**  
United States District Judge

cc: All parties