



IN THE SUPREME COURT OF THE STATE OF DELAWARE

FIRST STATE DEPOSITORY)
COMPANY, LLC and CERTIFIED)
ASSETS MANAGEMENT, INC.,)
)
Defendants-Below,)
Appellants,)
)
v.)
)
ISRAEL DISCOUNT BANK OF)
NEW YORK,)
)
Plaintiff-Below,)
Appellee.)

Appeal No. 482, 2013
Court Below: Court of Chancery
of the State of Delaware
C.A. No. 7237-VCP

APPELLEE'S ANSWERING BRIEF

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NATURE OF PROCEEDINGS

This appeal is the culmination of Defendants’ consistent and purposeful litigation strategy of creating delay and confusion to distract from the fact that Defendant-below, Appellant, Certified Assets Management, Inc. (“CAMI”), by its owner Robert Higgins, absconded with more than \$18 million of Plaintiff’s collateral, and used Defendant-below, Appellant, First State Depository Company, LLC (“FSD”), also owned by Higgins, to allow it to do so. Over the course of this litigation, Defendants wasted Plaintiff’s and the Court of Chancery’s time and resources (while failing to obey court orders) by advancing a vast multitude of defenses, regardless of their stark legal infirmity. The Court below, aware that it was dealing with an “unscrupulous businessman,”¹ indulged these arguments in a “belt and suspenders approach,” thus creating a fulsome record and giving Defendants every conceivable benefit of the doubt. The issue presented to this Court – like those presented to the Court below – is far simpler than Defendants would have this Court believe.

Plaintiff-Below, Appellee, Israel Discount Bank of New York (“IDB”) commenced the action below to prevent Higgins, through his entities, from absconding with highly valuable numismatic coins and gold bullion entrusted to those entities as collateral for various loans. IDB’s ultimate claims were that (i)

¹ See Memorandum Opinion, dated May 29, 2013 (“Mem. Op. II”) at 3 n.2. A copy is attached as Exhibit B to Appellant’s Opening Brief (“AOB”).

FSD breached a bailment agreement that requires FSD, as a bailee, to obey IDB's sole instructions regarding its collateral and (ii) CAMI converted the collateral, which was subject to IDB's security interest. The bailment agreement IDB sued on does not contain an arbitration clause at all.

Finding that IDB would be irreparably harmed if it did not restrain Defendants' unlawful conduct, the Court of Chancery awarded IDB interim injunctive relief against Defendants, enjoining them from removing the collateral from FSD's depository. Defendants did everything imaginable to avoid their legal obligations and judicial scrutiny, particularly once they were faced with their first motion for contempt for violating the preliminary injunction. In their desperation, Defendants misled the Court below, violated court orders multiple times, and after answering IDB's complaint, Defendants moved to dismiss it by asserting a plethora of legally infirm arguments. Defendants' primary argument was that an arbitration clause contained in other contracts not executed by IDB required the claims to be arbitrated.

The Court below denied Defendants' motion in all respects and held that the contract upon which IDB sought relief – the bailment agreement – does not contain an arbitration clause and therefore IDB's claims need not be arbitrated. The Court below properly found that the other contracts were not implicated because they set forth different (and even contradictory) rights and obligations upon which IDB did

not sue. The Court of Chancery secondarily held that even if it analyzed the request for arbitration under the other contracts, arbitration of IDB's claims, which emanated solely from the bailment agreement, was not required. Defendants sought interlocutory appellate review, which this Court refused.

Trial concluded on November 21, 2012. The Court of Chancery found that FSD breached the bailment agreement and CAMI was guilty of conversion. Judgment was entered against Defendants in the amount of \$8,950,877.40, which includes pre-trial interest and an award of attorneys' fees due to Defendants' bad faith litigation conduct. Defendants then filed this appeal.

SUMMARY OF ARGUMENT

1. **Denied.** The Court of Chancery correctly determined who should decide the issue of substantive arbitrability, because (i) the Bailment Agreement does not contain an arbitration clause, (ii) the arbitration clause contained in other contracts – the CCAAs – is inapplicable to the action below, and (iii) assuming *arguendo* that the CCAAs’ arbitration clause does apply, it does not refer generally all disputes arising out of the CCAAs to arbitration.

2. **Denied.** The Court of Chancery correctly decided that IDB’s claims are not subject to arbitration, because (i) the Bailment Agreement does not contain an arbitration clause, (ii) the carve out to the CCAAs’ arbitration clause is broad, (iii) IDB’s claims do not fall within the arbitration clause, and (iv) IDB’s conversion claim does not depend on the CCAAs, but on IDB’s security interest in the property provided by separate loan agreements.

3. **Denied.** The Court of Chancery correctly exercised subject matter jurisdiction over IDB’s claims, because IDB’s claims were not required to be arbitrated.

STATEMENT OF FACTS

Defendants do not challenge any portion of the Court of Chancery's comprehensive summary of the facts as found after a full trial on the merits. The significant facts are as follows.

A. IDB Advances Money to Republic, and, In Turn, Republic Makes Loans to CAMI

In 2004, IDB advanced money to Republic National Business Credit LLC ("Republic") and its principal, Ned Fenton, pursuant to a revolving credit agreement, which was amended numerous times to increase the amounts loaned and to add various protective provisions. Mem. Op. II at 3-5; A720 at ¶8. One such provision was the limiting of the borrowings of each of Republic's customers to \$5 million. Mem. Op. II at 4; A67-68 at §1.1(bb)(xi). Republic's obligations to IDB were secured by a first priority security interest in all of Republic's assets. Mem. Op. II at 4-5; A66 at §1.1(v), A79-80 at §§3.1-3.4. Among the collateral pledged to IDB was the collateral pledged to Republic as security by persons to whom Republic extended credit or made loans (the "Property"). Mem. Op. II at 4; A65 at §1.1(s), (r).

One of Republic's largest customers was CAMI, which entered into a revolving loan agreement with Republic in 2005. Mem. Op. II at 5; A165-72. CAMI granted to Republic a continuing first and prior security interest in and lien on all collateral pledged to Republic to secure its obligations. Mem. Op. II at 5;

A167 at §§ 3, 4. Republic's interest in collateral pledged by CAMI was pledged to IDB. Mem. Op. II at 5-6; A171 at §12.

B. The Bailment Agreement, Not FSD's Agreements with Others, Governs IDB's Rights to the Property While Stored at the Depository

Republic's loans to customers were collateralized primarily with numismatic coins that were deposited with IDB in its own safes or another Delaware depository unaffiliated with FSD or Robert Higgins – the sole owner of both FSD and CAMI. Mem. Op. II at 3, 6. In 2006, Republic persuaded IDB to transfer the Property to FSD due to better pricing. *Id.* at 6. IDB conditioned that transfer on the execution of the bailment agreement, which was executed by IDB, FSD and Republic on August 24, 2006 (the "Bailment Agreement"). B114-15; A119-23. The parties to the Bailment Agreement acknowledged that IDB already had a security interest in the Property. Mem. Op. II at 7; A119 at §1. The Bailment Agreement provides:

Upon written notice from an officer of [IDB], [FSD] agrees that it will hold all such Property subject only to [IDB]'s written instructions, and that [FSD] will release same to [IDB] on demand, provided that [IDB] tenders to [FSD] payment of any accrued charges on the Property being released. [FSD] agrees that [FSD] will not hinder or delay [IDB] in enforcing [IDB]'s right in and to said Property.

A120 at §6. The Bailment Agreement grants IDB other rights, including inspections of the Property. Mem. Op. II at 7; A119-20 at §2.

FSD, Republic and Republic's customers signed separate collateral custody

account agreements (“CCAAs”) governing their deposit of assets stored at FSD. Mem. Op. II at 6. On August 24, 2006, CAMI signed two CCAAs regarding assets deposited into two separate FSD accounts. A174-97. On December 21, 2006, Donald Ketterling (Higgins’ crony) signed a CCAA for CAMI regarding assets deposited into a third FSD account. A212-23; Mem. Op. II at 9. On April 30, 2008, a CCAA was filled out in the name of Vicki Lott (Higgins’ sister) regarding assets deposited into a fourth FSD account, but was not signed. A199-210; Mem. Op. II at 10. CAMI illicitly used Ketterling and Lott to avoid IDB’s \$5 million limit and obtain loans that it otherwise could not have. Mem. Op. II at 9.

The CCAAs are agreements between FSD, as the depository, CAMI, as the pledgor of collateral, and Republic, as the lender. The CCAAs each contain an arbitration clause. A179 at §20; A191 at §20; A204 at §20; A217 at §20; *see also* Memorandum Opinion, dated September 27, 2012 (“Mem. Op. I”)² at 12-13. IDB is not a signatory to the CCAAs and it maintained its own, separate rights to the Property pursuant to the Bailment Agreement.

C. IDB Becomes Concerned and, Pursuant to the Bailment Agreement, Instructs FSD Not to Release the Property Without IDB’s Consent

As a result of the 2009 seizure of NGE’s assets (consisting of a portion of the Property), a friend of Fenton assigned an entirely new pool of “side” collateral

² A copy of Mem. Op. I is attached as Exhibit A to Appellant’s Opening Brief.

directly to IDB. AOB at 9; Mem. Op. II at 11. The side collateral consisted of “missing edge error coins” (the “Error Coins”) to cover the more than \$4.8 million deficit in the value of the Property. *Id.* On August 12, 2009, IDB, Republic and FSD executed a collateral custody account agreement concerning the storage of the Error Coins for the benefit of IDB (the “Error Coins CCAA”). A125-34.

Defendants mistakenly equate the Error Coins CCAA with FSD’s form CCAA. B2-16. When IDB received the form CCAA from FSD, it required several revisions prior to agreeing to its terms. *See id.* Under the Error Coins CCAA, among other differences, (i) IDB had sole power to direct FSD regarding the Error Coins, (ii) language about conflicting instructions between IDB and Republic (as the pledgor of assets) was replaced with language providing that IDB had sole dominion and control of the Error Coins, and (iii) FSD would have no liability only if it honored IDB’s instructions. *Id.*; A125-34.

Another result of the seizure of NGE’s assets was that IDB tightened its controls and tried to reduce its exposure to Republic. On December 23, 2009, pursuant to the terms of the Bailment Agreement, IDB sent a letter instructing FSD not to release the Property without IDB’s consent. Mem. Op. II at 11-13; B1.

D. In Breach of the Bailment Agreement, FSD Releases the Property Without IDB’s Consent

On September 12, 2011, FSD released the Property without IDB’s consent so CAMI could display it at a coin collectibles show in Philadelphia, Pennsylvania.

Mem. Op. II at 14. The Property was valued by FSD at the time of the release at \$18,266,776.38. *Id.*; A720 at ¶11. It was not returned to FSD after the Philadelphia show, and was displayed for sale at a November 2011 show in Baltimore, Maryland. Mem. Op. II at 14. Higgins did not return the Property after its release on September 12, 2011; instead, he deposited it into CAMI's safes. *Id.*

IDB was becoming more concerned about Republic's ability to repay its loan and, on September 21, 2011, notified CAMI, Lott and Ketterling that IDB was exercising its right to have all amounts owed to Republic made payable directly to IDB. *Id.* at 15. In addition to its own payments, CAMI made payments for Lott's and Ketterling's accounts. *Id.* This immediately raised concerns at IDB that Lott and Ketterling were not separate borrowers, which would have put the aggregate loan to CAMI at \$11,550,000, in direct violation of the \$5 million cap on receivables from a single client. *Id.* IDB alerted Fenton, and Fenton sought to reduce Republic's loan portfolio to below \$10 million. *Id.*

At the end of October, 2011, Fenton informed Higgins that IDB was aware of the sham loans and IDB would be utilizing its lawyers to ensure no Property leaves the depository without IDB's authorization. Mem. Op. II at 15-17. Attempting to keep IDB at bay, Fenton informed IDB that CAMI was seeking to create a new asset management fund, with the hope that the money it raised could be used to repay the loans to IDB in full. *Id.* at 17. Fenton sent IDB a draft press

release announcing the formation of the fund. *Id.* It revealed that Higgins was the president of CAMI and that the assets of the fund would be stored at FSD. *Id.* As a result, IDB became concerned that there was a direct relationship between CAMI and FSD and the Property was not protected. *Id.*

E. FSD Refused to Permit IDB to Inspect the Property

On November 3, 2011, IDB attempted to gain access to the depository to inspect the Property, but FSD refused access. *Id.* The next day, IDB delivered a formal written notice to FSD pursuant to the Bailment Agreement requesting an inspection of the Property. *Id.* at 18; B17-34. IDB attempted to schedule inspections numerous times at the end of 2011 and the beginning of 2012, but FSD stalled the process and ultimately refused. Mem. Op. II at 18-22.

Higgins never intended to permit an inspection. *Id.* at 19; B35-36. In early February 2012, IDB attempted another inspection and notified FSD that it would be removing the Property from the depository. Mem. Op. II at 20-22. IDB again was turned away by FSD. *Id.* at 21-22; A722 at ¶¶22. IDB sent numerous notices to FSD and had attempted, in good faith, to obtain inspection dates from FSD for months. Mem. Op. II at 20-22; A721-22 at ¶¶14-23. Not only did FSD demand that IDB's attempted inspection be cancelled, FSD threatened IDB that it would call the police on IDB's "goon squad." Mem. Op. II at 22. IDB did not cancel its visit, but FSD again refused access. *Id.*

F. FSD Fails to Inform IDB that CAMI Removed and Sold Property

While IDB was attempting to inspect the Property, Higgins was hiding the fact that the Property had been removed from the depository in September and was not returned to prevent IDB from moving it to an independent depository. *See* B37-38; B39. Meanwhile, Higgins was selling Property. *See* B41 at ¶¶5-9.

On February 13, 2012, IDB commenced this action to stop Defendants and Higgins from further removing any Property and to obtain an inspection it had been attempting for months. One week later, the Court of Chancery entered a temporary restraining order (“TRO”) against FSD enjoining FSD from removing the Property from its depository. *Mem. Op. II* at 23. On the same day, CAMI sold at least \$368,095.30 in Property. *Id.* at 23. The next day, CAMI sold over \$5 million in Property. *Id.*

On February 29, the Court of Chancery entered a stipulated preliminary injunction against Defendants extending the TRO and requiring, *inter alia*, inspections to take place on specific dates. *Mem. Op. II* at 24; B44-48. On March 1, IDB was informed by Defendants that the inspection the following day (as ordered in the preliminary injunction) was moot because no Property was stored at the depository at that time. *See* B52, B63, B65. On March 5, Defendants moved for an order of contempt against Defendants for violating the injunction. *Mem. Op. II* at 24. During the pendency of the contempt motion, Defendants filed an

answer to IDB's complaint, which did not assert that the Court below lacked subject matter jurisdiction over IDB's claims. B70-85. At the contempt hearing two days later, Defendants misled the Court below about the identity of the person in possession of the Property and why it could not be returned in a timely fashion. Mem. Op. II at 80. The Court below found Defendants in contempt of the preliminary injunction. *Id.* at 25, 80-81; B86-96.

Following the order of contempt, Defendants' counsel moved to withdraw as counsel, and five days later, substitute counsel entered an appearance. A27-28 at Dkt. Nos. 54, 56. Shortly thereafter, IDB filed a second motion for contempt due to Defendants' failure to comply with the contempt order. A26 at Dkt. No. 62. Substitute counsel opposed the second contempt motion and moved to dismiss IDB's complaint for a host of reasons, including arguing that the Court below lacked subject matter jurisdiction to adjudicate IDB's claims due to arbitration clauses in the CCAAs. A140-62; A236-78.

**G. Higgins Absconds With the Property
and Refuses to Return it to FSD**

Following the unauthorized release of the Property in September 2011, the unsold portions of the Property were kept at CAMI's offices. B123. On March 22, 2012, in connection with a seizure warrant issued by the District Court for the Southern District of New York, FBI agents raided FSD as well as the CAMI booth at another coin and collectibles show in Baltimore taking place that day. Mem.

Op. II at 25; B124. Nothing was seized because Higgins already had taken the Property, despite both the preliminary injunction and contempt Orders requiring the return of the Property to FSD. CAMI continued to dissipate the Property by selling it. Mem. Op. II at 25.

H. CAMI Returns a Small Fraction of the Property to FSD

On March 27, 2012, only a small portion of the Property, made up of mostly low value coins, was returned to FSD. *Id.* at 25-26; B117-18, B120-21. On March 29, IDB representatives visited FSD to inspect any Property returned pursuant the contempt Order. Mem. Op. II at 26. Shortly after arriving, FBI agents raided FSD and asked the IDB representatives to leave. *Id.* The FBI seized some of the Property. *Id.* On April 5, IDB conducted an inventory of the substitute Property not seized by the FBI. *Id.* IDB moved for a second contempt order due to Defendants' failure to abide by the terms of the preliminary injunction and first contempt Orders. B97-112. On May 8, the FBI seized the remaining Property. Mem. Op. II at 26; A722 at ¶25. The Property returned under threat of further sanctions and seized by the FBI (valued at approximately \$3.8 million, Mem. Op. II at 68) presumably is still in the possession of the federal government. The location of over \$14 million in Property remains completely unknown to IDB.

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY RETAINED THE DETERMINATION OF SUBSTANTIVE ARBITRABILITY BECAUSE IDB DID NOT SEEK TO ENFORCE RIGHTS UNDER A CONTRACT CONTAINING AN ARBITRATION CLAUSE

A. Question Presented

Did the Court of Chancery correctly retain for itself the substantive arbitrability determination where IDB sought to enforce rights that emanated solely from a contract without an arbitration clause and therefore properly exercise jurisdiction over such determination?

B. Standard and Scope of Review

This Court's review of whether the Court below properly exercised subject matter jurisdiction is a question of law subject to *de novo* review. *See Candlewood Timber Grp., LLC v. Pan Am. Energy, LLC*, 859 A.2d 989, 997 (Del. 2004).

C. Merits of Argument

The claims pursued by IDB in this action – both its breach of contract claim and its conversion claim – were correctly within the province of the Court of Chancery because no arbitration clause covers such claims. “A party cannot be forced to arbitrate the merits of a dispute ... in the absence of a clear expression of such intent in a valid agreement.” *James & Jackson, LLC v. Willie Gary, LLC*, 906 A.2d 76, 79 (Del. 2006). As against FSD, IDB sought to enforce rights under the

Bailment Agreement, which does not contain any arbitration clause and therefore no clear expression of intent to arbitrate. Even considering the separate CCAs that IDB did not seek to enforce, IDB's claims are not subject to arbitration. As against CAMI, IDB sought relief for a conversion of the Property that occurred subsequent to and separate from FSD breaching the Bailment Agreement, and such claim stems solely from IDB's security interest in the Property.

1. A *Willie Gary* Analysis is Unnecessary Because IDB Sought to Enforce Rights Under a Contract Without an Arbitration Clause

When a party seeks to force a litigant to arbitrate, it must be determined (i) whether the claims should be arbitrated and (ii) whether that decision on arbitrability should be decided by a court or an arbitrator. *McLaughlin v. McCann*, 942 A.2d 616, 620-21 (Del. Ch. 2008). “Substantive arbitrability issues are gateway questions about the scope of an arbitration provision and its applicability to a given dispute[,]” which are presumptively decided by the court. *Willie Gary*, 906 A.2d at 79; *see also Viacom Int’l Inc. v. Winshall*, 72 A.3d 78, 82-83 (Del. 2013). A court is divested of this determination only where parties clearly and unmistakably intended to arbitrate substantive arbitrability. *See Willie Gary*, 906 A.2d at 79-81. *Willie Gary* is the seminal decision on what constitutes clear and unmistakable evidence of intent to arbitrate substantive arbitrability.

Consistent with *Willie Gary*, “[a] basic arbitration principle is that ‘arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.’” *Vituli v. Carrols Corp.*, 2013 WL 2423091, at *2 (Del. Super. Ct. Mar. 28, 2013) (quoting *Willie Gary*, 906 A.2d at 78). Because no arbitration clause exists in the Bailment Agreement, Defendants “put the rabbit in the hat” and assume that the CCAAs and their arbitration clauses apply to IDB’s claims. *Id.* They do not. The rights IDB sought to enforce are distinct and independent from any rights it may have had as a third party beneficiary, or otherwise, under the CCAAs:

The specific right IDB seeks to enforce is its ability to insist, upon written notice to FSD, that FSD follow only IDB’s instructions. As discussed in the succeeding paragraphs, that right emanates entirely from the Bailment Agreement and, to a certain extent, supersedes rights granted under the CCAAs.

* * *

In this case, the right pursued by IDB is the right to demand that FSD handle the collateral only in accordance with its instructions. The CCAAs themselves do not confer upon IDB a right to direct FSD in handling the collateral. Rather, the Bailment Agreement creates this right and explicitly gives IDB the authority to require FSD to ignore any contrary instructions. The Bailment Agreement, however, does not contain an arbitration clause.

Mem. Op. I at 16-17. Indeed, the rights that IDB sought to enforce under the Bailment Agreement are inconsistent with the CCAAs.³ Accordingly, the Court

³ Compare Bailment Agreement, A120 at § 6, (“Upon written notice from an officer of [IDB], [FSD] agrees that it will hold all such Property subject only to [IDB’s] written instructions....”) with CCAAs, A176, A188, A201, A214, at § 9.D, (providing that FSD is

below could have ended its inquiry when it decided that the Bailment Agreement does not contain an arbitration clause and therefore IDB's claims properly could be decided by the Court of Chancery. There can be no clearer or unmistakable evidence of IDB's intent not to arbitrate than the absence of an arbitration clause.

Unlike in *Willie Gary*, the Court below was confronted with an unusual threshold question of whether the party resisting arbitration should be bound by an arbitration clause *contained in a contract it did not sign*. It would be an expansion of Delaware law if this Court were to reverse the Court below and bind a non-signatory to an arbitration clause contained in a contract under which the non-signatory did not seek relief and where that contract contains terms contradictory to the contract sued on. *See Vituli*, 2013 WL 2423091, at *2 (“[T]he court cannot find[] a case where arbitration was compelled despite a contract’s complete lack of an arbitration clause or reference to arbitration. Even if such case exists, it stands against the host of ‘arbitrability’ cases that all turn on some mention of arbitration in the contract at issue”). That would be contrary to the recognized principle of contract construction that parties (particularly sophisticated ones represented by counsel) can bargain for their rights, and the absence of an arbitration clause in the Bailment Agreement signifies that the parties did not intend for one to apply. *See*

“protected in acting upon an Formal Notice, written notice, request, waiver, consent, certificate, receipt, authorization, power of attorney or other document executed by Authorized Signer(s)”). Republic’s principal, Fenton, was an Authorized Signer, but IDB was not. *See* Mem. Op. I at 17 n.50.

Allied Capital Corp. v. GC-Sun Hldgs., L.P., 910 A.2d 1020, 1035 (Del. Ch. 2006) (holding that “courts should be most chary about implying a contractual protection when the contract could easily have been drafted to expressly provide for it”); *Union Oil Co. of Cal. v. Mobil Pipeline Co.*, 2006 WL 3770834, at *12 (Del. Ch. Dec. 15, 2006) (same); *EBG Holdings LLC v. Vredzicht’s Gravenhage 109 B.V.*, 2008 WL 4057745, at *9 (Del. Ch. Sept. 2, 2008) (same); *Caldera Props.-Lewes/Rehoboth VII, LLC v. Ridings Dev., LLC*, 2008 WL 3323926, at *12 (Del. Super. Ct. June 19, 2008) (recognizing “[t]he presumption that the parties are bound by the language of the agreement they negotiated applies with even greater force when the parties are sophisticated entities that have engaged in arms-length negotiations.”). No such expansion of Delaware law is warranted. The Court below correctly determined that IDB did not agree to arbitrate any dispute emanating from the Bailment Agreement.

Simply stated, if the *Willie Gary* analysis is applied to the correct contract – the Bailment Agreement – the analysis ends there because the Bailment Agreement does not contain an arbitration clause. *See Hough Assocs., Inc. v. Hill*, 2007 WL 148751, at *12 (Del. Ch. Jan. 17, 2007) (“In the face of the [agreement]’s silence as to arbitration, it is impossible to infer an implicit contract between the parties to use arbitration to resolve disputes arising under that [a]greement simply because the parties agreed to arbitrate other disputes arising under [another agreement]”).

Accordingly, the judgment of the Court below should be affirmed.

2. The Court of Chancery’s *Willie Gary* Analysis Correctly Resulted in the Court Below Making the Substantive Arbitrability Determination

Although the Court below did not need to apply *Willie Gary* to the CCAAs because they have no bearing on IDB’s claims, the Court of Chancery did not err. The Court of Chancery correctly found that even the arbitration clause of the CCAAs did not require that substantive arbitrability be arbitrated in connection with IDB’s claims. Since *Willie Gary*, this Court has yet to revisit its formulation of the test therein and nothing decided by the Court below was inconsistent with this Court’s last word on the issue.

Defendants contend that the arbitration clause in the CCAAs rebuts the presumption that a court determines the substantive arbitrability of a dispute thereunder because it “generally provides for the arbitration of all disputes” and “incorporates a set of arbitration rules that empower arbitrators to decide arbitrability.” See AOB at 14 (citing *Willie Gary* at 78-79). The Court of Chancery, however, correctly determined that because the arbitration clause contained a carve out “for interpleader suits,” the first prong of *Willie Gary* was not satisfied (*i.e.*, the arbitration clause did not “generally” “provide for arbitration of all disputes”). Mem. Op. I at 12, 14. Defendants contend that the Court below ignored the modifier “generally” before the word “all” in its application of the first

prong of the *Willie Gary* and that the interpleader carve out is, in reality, narrow and does not overcome a presumption in favor of arbitrability. AOB at 14-15.

Defendants incorrectly assume that the Court of Chancery required a more stringent standard than required in *Willie Gary*. *Id.* at 18. The Court below correctly applied this Court's formulation of the *Willie Gary* test, including the modifier "generally," and IDB does not dispute that an arbitration clause need not refer all disputes to arbitration in order to satisfy the first prong of the test. *See* Mem. Op. I at 12. The Court of Chancery did not literally hold that every single conceivable dispute must be referred to arbitration in order to satisfy the first prong of *Willie Gary*. Rather, the Court below made a judgment about the relative breadth of the carve out, which led it to conclude that it should retain for itself the substantive arbitrability determination. *Id.* I at 14.

The Court below got it right. The interpleader carve out is at least as broad as the carve out in *Willie Gary*, and, contrary to Defendants' contention, broader than the carve outs in *BAYPO Limited Partnership v. Technology JV, LP*, 940 A.2d 20 (Del. Ch. 2007) and *Orix LF, LP v. Inscap Asset Management, LLC*, 2010 WL 1463404 (Del. Ch. Apr. 13, 2010). In *Willie Gary*, this Court found that a carve out limited to injunctive relief and specific performance was broad enough to warrant a finding that the parties did not refer generally all disputes to arbitration. 906 A.2d at 79-81. The interpleader carve out broadly encompasses disputes *on*

the merits concerning competing instructions by Republic and CAMI about the disposition of collateral, which is at least as broad as the *Willie Gary* carve out.

The carve out in *BAYPO* was limited to injunctive and other equitable relief necessary to protect the *status quo* pending alternative dispute resolution. The *BAYPO* Court held that even though the parties did not refer all disputes to arbitration, the carve out was sufficiently narrow and provided the parties only “with limited ancillary relief to protect their interests during the pendency of the arbitration process.” 940 A.2d at 26-27. Moreover, the arbitration clause in *BAYPO* contained additional language “specifically directing that an arbitrator decide all substantive and procedural issues” – language not present in this case. *Id.* at 27. By contrast, the Court below correctly noted that the interpleader carve out was broader because it did more than maintain the *status quo* pending an arbitration on the merits; it provided a mechanism for a court to decide the merits of a dispute regarding the disposition of the Property, which is at the core of the CCAAs. Mem. Op. I at 13-14 & n.41.

The carve out of the arbitration clause at issue in *Orix* is substantially narrower than the interpleader carve out analyzed by the Court below. The *Orix* carve out was limited to a “special arbitration” – *not a court proceeding* – solely to determine if the manager of an LLC committed at least one of six specific forms of misconduct, which finding would trigger a vote on the manager’s removal.

Finally, each case applying *Willie Gary* upon which Defendants rely to support their argument that the arbitrability of IDB's claims are required to be arbitrated involves *signatories* to arbitration clauses resisting arbitration. *See McLaughlin*, 942 A.2d at 620, 626-27 (sellers of business demanded arbitration pursuant to arbitration clause in purchase agreement, but purchasers, counter-parties to the agreement, sought to stay arbitration); *BAYPO*, 490 A.2d at 22, 26-28 (party resisting arbitration was signatory to contract containing arbitration clause); *Orix*, 2010 WL 1463404, at *7 (party resisting arbitration was signatory to an agreement containing arbitration clause; other signatories to that agreement made arbitration demands that clearly alleged that the resisting party breached that agreement); *Carder v. Carl M. Freeman Cmtys., LLC*, 2009 WL 106510, at *2 (Del. Ch. Jan. 5, 2009) (plaintiff signatory to a real estate purchase contract containing an arbitration clause was the party resisting arbitration); *Lefkowitz v. HFW Holdings, LLC*, 2009 WL 3806299, at *1-2 (Del. Ch. Nov. 13, 2009) (parties resisting arbitration were sellers under an equity purchase agreement containing arbitration clause under which the plaintiff purchasers commenced their arbitration proceedings); *Brown v. T-Ink, LLC*, 2007 WL 4302594, at *1, *8 (Del. Ch. Dec. 4, 2007) (party resisting arbitration was a signatory to an LLC agreement containing arbitration clause at issue).

In this action, however, a non-signatory (IDB) is the party resisting arbitration. Unlike those parties, neither IDB (nor any affiliate of IDB) signed the CCAAs containing the arbitration clauses. Rather, IDB sought to enforce rights that exist solely by virtue of the Bailment Agreement, which does not contain an arbitration clause.

3. The Court Below Properly Analogized IDB's Claims to an Interpleader Action Under the Carve Out

In support of its holding that an arbitrability decision was reserved for itself, the Court below properly analogized IDB's claims to those within the ambit of the interpleader carve out. Mem. Op. I at 16-17. Defendants misapprehend the import of the Court's comments. It was not necessary for the Court below to "construe the action so as to fit into the narrow interpleader carve out...." AOB at 20. Rather, what is significant is the similarity of the relief sought by IDB (which the Court below correctly described as an action to enforce its right under the Bailment Agreement to control the disposition of the Property), Mem. Op. I at 19-20, and an interpleader action of the type provided for in the CCAAs. *See* A176, A188, A201, A214 at §9.C. In both instances, the relief requested consists of a court resolving the question of who has authority to control disposition of the Property.

Defendants also wrongly contend that the Court of Chancery's finding allows the interpleader carve out to "swallow the rule." AOB at 20. Defendants posit that under such analysis, any claim under the CCAAs or the Bailment

Agreement could be the subject of an interpleader suit, thereby rendering the CCAAs' arbitration clause meaningless. *Id.* at 20-21. First, no matter how claims under the Bailment Agreement are characterized, there is no need to consider whether any are analogous to an interpleader suit, because IDB's rights thereunder are not subject to arbitration. *See* Section I.C.1, *supra*. The analysis should end there. Second, regarding the CCAAs, Defendants overstate the scope of the Court of Chancery's statements. The Court below did not state that the arbitration clause would be overridden by "any claim related to the collateral." AOB at 21. What the Court below noted was that IDB's claim to enforce its rights to direct the disposition of the Property was analogous to an interpleader action. That is a significantly narrower construction than suggested by Defendants. Indeed, the Court below astutely noted that if IDB "was suing to enforce a provision of the CCAA, such as, for example, a provision regarding fees or FSD's compliance with procedures outlined for shipments into and out of FSD's facilities, IDB would be bound to the terms of that agreement" based on its third party beneficiary status. Mem. Op. I at 28-29. The Court below has not offered a construction of the interpleader carve out that would "swallow the rule." To the contrary, it is Defendants who have proffered a construction of the CCAAs' arbitration clause so broad that it swallows the Bailment Agreement.

The arbitration clause continues to have force and effect as among the parties that actually signed the CCAAs: FSD, Republic and Republic's customers. It has not, as Defendants suggest, been eviscerated. Its application to IDB has been limited, however, because IDB, Republic and FSD executed the Bailment Agreement, which gives IDB "separate and distinct" rights.

In sum, this Court should affirm the Court of Chancery's decision retaining the substantive arbitrability determination in connection with IDB's claims.

II. THE COURT OF CHANCERY CORRECTLY HELD THAT IDB'S CLAIMS ARE NOT SUBJECT TO ARBITRATION BECAUSE IDB DID NOT SEEK TO ENFORCE RIGHTS UNDER THE CCAAS, AND EVEN UNDER THE CCAAS, IDB'S CLAIMS SHOULD BE DECIDED BY A COURT

A. Question Presented

Did the Court of Chancery correctly hold that IDB's claims are not subject to arbitration where IDB sought relief solely under a contract without an arbitration provision and therefore properly exercised jurisdiction over the claims?

B. Standard and Scope of Review

See Section I.B, *supra*. Regarding the Court of Chancery's factual determinations discussed below in Section C.3, *infra*, they "will not be disturbed unless the trial court's findings or inferences are not supported by the record or not the product of an orderly and logical deductive reasoning process. *See Waggoner v. Laster*, 581 A.2d 1127, 1133 (Del. 1990).

C. Merits of Argument

The Court of Chancery properly found that IDB's claims were not subject to arbitration because they emanated from sources wholly separate from the CCAAs that contain arbitration clauses: (i) its contract claim against FSD stems only from the Bailment Agreement; and (ii) its conversion claim against CAMI stems only from IDB's security interest in the Property pursuant to separate loan agreements. When the arbitrability of a claim is disputed and a decision about arbitrability is

correctly within the province of a court, that court must resolve two issues: (i) whether the arbitration clause is broad or narrow in scope; and (ii) application of the relevant scope of the provision to the asserted legal claim to determine whether the claim falls within the scope of the contractual provisions that require arbitration. *Parfi Holding AB v. Mirror Image Internet, Inc.*, 817 A.2d 149, 155 (Del. 2002). The Court below properly found that regardless of whether the CCAAs' arbitration clause was broad or narrow, IDB's claims did not fall within that scope because they arose solely from the Bailment Agreement.

1. The Court of Chancery Properly Decided Against Arbitration Regardless of the Scope of the Arbitration Clause

Under *Parfi*, the policy favoring arbitration does not trump basic principles of contract interpretation. 817 A.2d at 156. "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." *Id.*

With that as a backdrop, the Court of Chancery reasoned that the scope of the CCAAs' arbitration clause could be considered narrow because the carve out is broad. *See* Section I.C.2, *supra*. Assuming that the arbitration clause is narrow, the question is whether IDB's breach of contract claim "directly relates to a right in the contract." *Parfi*, 817 A.2d at 155. The answer is "no." The right IDB sought

to enforce “emanates entirely from the Bailment Agreement and, to a certain extent, supersedes rights granted under the CCAAs.” Mem. Op. I at 16. Accordingly, the Court below correctly concluded that the arbitration provision of the CCAAs did not require arbitration of IDB’s claims.

Even if the arbitration clause were broad, the Court below determined that it would reach the same conclusion. *Id.* at 16-17. When an arbitration provision is broad, a court must decide whether the claims in question fall within its scope by determining whether the “claims fit within the rubric of a claim ‘arising out of or in connection with’” the contract at issue. *Id.* at 17 (citing *Parfi*, 817 A.2d at 155). The right pursued by IDB is the right to demand that FSD handle the Property solely in accordance with its instructions, which right arises *only* under the Bailment Agreement. There is no arbitration clause in the Bailment Agreement and therefore arbitration of IDB’s contract claim is not required.

Defendants’ contention that the Court below erred by concluding that the arbitration clause was narrow (which it did not for the reasons summarized above) ignores the Court of Chancery’s secondary holding that it would reach the same result even if it found that the arbitration clause was broad. *Id.* at 16-17. The Court below noted that when considering whether a plaintiff’s claim fits within the rubric of a claim “arising out of or in connection with” with the parties’ contract, *Parfi* instructs the Court of Chancery to focus on the separate rights pursued by

plaintiff rather than the similarity of conduct that led to claims under the contract and under a duty that arose outside of the contract. *Id.* at 17. As noted above, IDB pursued its right to a disposition of the Property only in accordance with IDB's instructions and that right is outside the scope of the CCAAs, which confer no such right on IDB. *Supra* at p.17; *see also* Mem. Op. I at 18 ("Bailment Agreement gives IDB the right to control the [Property], which right is independent of the rights IDB enjoys as a third-party beneficiary to the CCAAs."). In short, Defendants' *Parfi* analysis betrays their fundamental error on appeal – starting from the faulty conclusion that the arbitration clause in the CCAAs is controlling.

2. IDB's Contract and Conversion Claims are Not Sufficiently Related to the CCAAs

Defendants argue that IDB's claims fall within the scope of the arbitration clause of the CCAAs, because IDB sued under both the Bailment Agreement and the CCAAs and therefore acknowledged the inter-relationship between those agreements. This argument confuses and conflates the facts. In addition to suing to protect the Property, IDB also sued under the Error Coins CCAA to protect the Error Coins, but such dispute was mooted during the TRO hearing (only one week after commencing the action and two months prior to Defendants' filing their motion to dismiss), because FSD assented to IDB's request to remove the Error Coins from the depository. Thereafter, the only relevant claims concerned FSD's breach of the Bailment Agreement and the conversion of the Property. IDB never

sued under the CCAAs. Defendants appear to confuse the Error Coins CCAA (which they call the 2009 CCAA) with the CCAAs executed by CAMI and under which the Court below conducted its arbitrability analysis. The Error Coins CCAA has no nexus to the Property. The collateral is completely different because the Error Coins CCAA covers only the additional side collateral consisting of the Error Coins pledged by Republic to IDB in 2009. The Bailment Agreement and the Error Coins CCAA were executed three years apart. As set forth in the Statement of Facts, in Section C, *supra*, the Error Coins CCAA is significantly different than the CCAAs.

Citing *Westendorf v. Gateway 2000, Inc.*, 2000 WL 307369 (Del. Ch. Mar. 16, 2000), Defendants argue that IDB “explicitly acknowledg[ed] the inter-relationship” of the “CCAA” and the Bailment Agreement. *See* AOB at 25. IDB did not make this acknowledgement, and *Westendorf* is a factually distinguishable third party donee beneficiary case. *See* Mem. Op. I at 22-24. *Westendorf* involved a plaintiff and a friend each purchasing computers for one another, and such computers were shipped with standard agreements containing arbitration clauses. *Westendorf*, 2000 WL 307369, at *1-2. They also received an optional services agreement, which the plaintiff accepted and sued on. *Id.* at *3. The *Westendorf* Court held that the plaintiff was bound by the arbitration clause in the standard agreement for several reasons, including the manner in which she came to own her

computer, *i.e.*, swapping computers with her friend, and because the arbitration clause covered the services agreement as a “related purchase.” *Id.* at *4-5. Here, the CCAAs’ arbitration clause does not contain “language indicating that IDB [or any other party] intended to apply it to the Bailment Agreement” and nothing in that clause “precludes IDB from entering a direct agreement with a party to the CCAAs on different terms.” *See* Mem. Op. I at 24.

Defendants also contend that IDB’s conversion claim against CAMI arises out of the CCAAs. This argument fails because it relies solely on the premise that the Property alleged to have been converted by Defendants (and ultimately proved to have been converted by CAMI) was collateral held by FSD pursuant to the CCAAs. Defendants make the illogical leap that because the Property was supposed to be stored at FSD, that IDB was obligated to arbitrate its independent tort claim against CAMI for converting IDB’s property. The Court below dispensed with this argument and nothing in the Defendants’ brief demonstrates any legal error.

When assessing whether *Parfi* requires arbitration of this independent tort claim, the precise question to ask is whether it “depend[s] on the existence” of the CCAAs. Mem. Op. I at 25 (citing *Parfi*, 817 A.2d at 155). Here, it does not. CAMI unlawfully exercised dominion and control over Property in which IDB held a security interest pursuant to loan agreements with Republic and because

CAMI pledged the Property as collateral for money it borrowed. The fact that the Property was supposed to be stored at FSD's depository pursuant to contract is irrelevant. The conversion claim against CAMI pursued at trial would have been actionable without the existence of either the CCAAs or the Bailment Agreement, because IDB's rights to the Property existed independently of those contracts. Likewise, CAMI's conversion of the Property did not implicate such contracts; rather, it implicated loan agreements not at issue in this action.

Defendants' contention that IDB sued under both the Bailment Agreement and the CCAAs, and therefore that IDB's conversion claim must be arbitrated, is incorrect. IDB did not sue under the CCAAs. IDB's complaint does not even discuss the CCAAs, which makes sense because IDB was not a party to them and was not suing on those agreements.

3. Third Party Beneficiary, Agency and Related Doctrines Do Not Bring IDB's Claims Within the Scope of the CCAAs' Arbitration Clause

Defendants' final argument under *Parfi* is that IDB's claims are arbitrable under the doctrines of third party beneficiary, agency, assumption and assignment. AOB at 27-28. They offer two reasons: (i) the Bailment Agreement designates IDB as a third party beneficiary of the CCAAs; and (ii) FSD was acting for the benefit of IDB (explicitly under the Bailment Agreement and impliedly under the CCAAs) and therefore IDB is bound to the arbitration clause in the same manner

as Republic.

First, Defendants' third party beneficiary argument is inapplicable where, as here, IDB is not seeking to enforce any rights as a third party beneficiary to the CCAAs. *See E.I. DuPont de Nemours & Co. v. Rhone Poulenc Fiber & Resin Interms., S.A.S.*, 269 F.3d 187, 195 (3d Cir. 2001) (“[B]ecause the claims asserted by [plaintiff] do not arise from any ‘third party beneficiary’ status under the Agreement, [plaintiff] was not bound to arbitrate its claims as a third party beneficiary”). Again, IDB sought to enforce its separate and direct rights under the Bailment Agreement, which therefore is the only contract at dispute in this action. Defendants note that IDB is a third party beneficiary of the CCAAs because the Bailment Agreement generally provides that IDB is a third party beneficiary of “separate agreements between [FSD], [Republic] and [Republic’s] clients.” AOB at 27. They claim that IDB should therefore be bound to the arbitration clause in the CCAAs to the same extent as Republic. *Id.* at 27-28. Defendants fail to recognize what the Court below properly focused on:

[A]lthough IDB is a third-party beneficiary to the CCAAs, nothing in the language of the arbitration clause in those agreements precludes IDB from entering a direct agreement with a party to the CCAAs on different terms. Indeed, in the situation Defendants highlighted, where IDB, FSD, and Republic entered into a CCAA and the Bailment Agreement on the same day, that is exactly what happened. As such, concluding that the parties did not intend IDB’s claim under the Bailment Agreement to be subject to arbitration does not effectively “undo” the CCAA arbitration clause....

Mem. Op. I at 24.

Second, Defendants' argument that agency principles dictate the application of the arbitration clause in the CCAAs is refuted by the Court of Chancery's post-trial findings made after carefully considering the evidence:

Because FSD is unable to show that the CCAAs were assigned to IDB, FSD seeks to rely on agency principles to create a presumption that anything Republic did after it made the loans to CAMI, Lott and Ketterling bound [IDB], including Republic's execution of the CCAAs. FSD, however, cites no cases nor does this Court know of any that have held that an assignment of a loan creates an agency relationship whereby the assignor's other actions and other agreements bind the assignee. Nor has FSD demonstrated that IDB was bound to the CCAAs as a result of Republic having been authorized or appearing to an unsuspecting third party to have been authorized, to bind IDB. To the contrary, Republic appears to have acted contrary to IDB's authority. Accordingly, I conclude that IDB is not subject to any duties or obligations under the CCAAs based on "agency principles."

Mem. Op. II at 46-47. Simply stated, the Court below found that the facts did not support that the CCAAs were assigned to IDB or that Republic bound IDB to the CCAAs as IDB's agent.

In sum, this Court should affirm the Court of Chancery's ruling that IDB's claims are not subject to arbitration.

CONCLUSION

For the foregoing reasons, IDB respectfully requests that this Honorable Court affirm the judgment of the Court of Chancery.

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