

IN THE UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

VANEDE, LLC,)	
)	
Plaintiff,)	
)	
v.)	No. 17-cv-2865-SHM-cgc
)	
WILLIAM W. OXLEY, OXLEY I,)	
LLC, and OXLEY II, LLC,)	
)	
Defendants.)	
)	

ORDER

Before the Court is Defendants William W. Oxley, Oxley I, LLC, and Oxley II, LLC's (collectively, "Defendants") Motion to Compel Arbitration (the "Motion"), filed on December 22, 2017. (ECF No. 18.) Plaintiff Vanede, LLC ("Vanede") responded on January 5, 2018. (ECF No. 19.)

For the following reasons, the Motion to Compel Arbitration is GRANTED in part and DENIED in part.

I. Background

This action arises from an "Asset Purchase Agreement" between Vanede and Defendants in which Vanede agreed to purchase two cosmetology schools in Tennessee (the "Agreement"). Vanede alleges fraud in the inducement and breach of contract. (Compl., ECF No. 1.) The complaint seeks

rescission of the Agreement or compensatory damages, and attorneys' fees, interest, and costs. (Id.)

On December 22, 2017, Defendants filed the Motion, seeking to enforce the arbitration provision in the Agreement on all of Vanede's claims and remedies. (ECF No. 18.) Defendants seek costs and attorneys' fees incurred in bringing the Motion. (ECF No. 18-1 at 104.)

Vanede filed a response on January 5, 2018, arguing that its claims are exempt from arbitration. (ECF No. 19.)

II. Jurisdiction & Choice of Law

Vanede alleges that the Court has diversity jurisdiction. (Compl., ECF No. 1 ¶ 21.) Vanede is a Tennessee limited liability company that is wholly owned by GLC Solutions, a New York limited liability company. (Id.) GLC Solutions has two members, Kevin Koch, a citizen of New York, and Sherry Jones, a citizen of Utah. (Id. ¶¶ 6-12.) Vanede is a citizen of New York and Utah.

The complaint alleges that Defendant William W. Oxley is a citizen of Tennessee. (Id. ¶ 14.) It also alleges that Defendants Oxley I, LLC and Oxley II, LLC are limited liability companies that are wholly owned by Defendant William W. Oxley.

(Id. ¶¶ 15-19.) Oxley I, LLC and Oxley II, LLC are citizens of Tennessee. There is complete diversity.

The complaint alleges "the amount in controversy exceeds Seventy-Five Thousand Dollars (\$75,000.00), exclusive of interest and costs." (Id. ¶ 22.) The Court has subject matter jurisdiction over Vanede's claims based on diversity of citizenship. See 28 U.S.C § 1332(a)(1).

In a diversity action, state substantive law governs. Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938). A federal district court is required to apply the choice-of-law rules of the state in which it sits. Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487, 496 (1941).

Under the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 1, et seq., arbitration agreements may be invalid on the grounds that "exist at law" for the revocation of contracts. See 9 U.S.C. § 2. "In other words, whether an arbitration clause is enforceable is governed by state law." Stutler v. T.K. Constructors, Inc., 448 F.3d 343, 345 (6th Cir. 2006). State law determines the applicability of contract defenses such as fraud, duress, or unconscionability. Doctor's Assocs., Inc. v. Casarotto, 517 U.S. 681, 686-87 (1996); see Floss v. Ryan's Fam. Steak House, Inc., 211 F.3d 306, 314-15 (6th Cir. 2000).

Tennessee choice-of-law rules apply. See Klaxon Co., 313 U.S. at 496.

Tennessee follows the rule of *lex loci contractus*, which provides that a contract is presumed to be governed by the law of the jurisdiction in which it was executed absent a contrary intent. Vantage Tech., LLC v. Cross, 17 S.W.3d 637, 650 (Tenn. Ct. App. 1999) (citing Ohio Cas. Ins. v. Travelers Indem. Co., 493 S.W.2d 465, 467 (Tenn. 1973)). "If the parties manifest an intent to apply the laws of another jurisdiction, then that intent will be honored provided certain requirements are met": (1) the choice of law provision must be executed in good faith, (2) the "chosen jurisdiction must bear a material connection to the transaction," (3) the "basis for the choice of law must be reasonable," and (4) the choice of "another jurisdiction's law must not be 'contrary to a fundamental policy of a state having a materially greater interest and whose law would otherwise govern.'" Id. (citing Restatement (Second) of Conflict of Laws § 187(2) (1971)).

The Agreement includes a choice-of-law provision stating that "[a]ll issues and questions concerning the construction, validity, enforcement and interpretation of this Agreement shall be governed by, and construed in accordance with, the laws of the State of Tennessee without giving effect to any

choice of law or conflict of law rules or provisions." (ECF No. 1-2 at 61.) Neither party suggests that the choice-of-law provision was not entered into in good faith, and both parties assume that Tennessee law applies. (See, e.g., ECF No. 18-1 at 101-04; ECF No. 19 at 114-15.) The choice of Tennessee law is reasonable because the assets at issue in the Agreement are in Tennessee.

Tennessee contract law applies to Vanede's claims arising from the Agreement and in determining whether the arbitration clause in the Agreement is enforceable.

III. Legal Standard

To be enforceable, an arbitration agreement must be (1) in writing and (2) involve a transaction in interstate commerce. 9 U.S.C. § 2. Such an arbitration agreement "shall be valid, irrevocable, and enforceable." Id.

"Any doubts about whether an [arbitration] agreement is enforceable, including defenses to arbitrability, should be resolved in favor of arbitration." Johnson v. Long John Silver's Rests., Inc., 320 F.Supp.2d 656, 663 (M.D. Tenn. 2004) (internal citation omitted); see EEOC v. Waffle House, Inc., 534 U.S. 279, 289 (2002) (holding that the Federal Arbitration Act ("FAA") strongly favors arbitration). "In deciding whether to compel arbitration of a federal statutory claim, we first

consider whether the statutory claim is generally subject to compulsory arbitration. If the claim is not exempt from arbitration, we must then consider whether the arbitration agreement is valid." Morrison v. Circuit City Stores, Inc., 317 F.3d 646, 665 (6th Cir. 2003) (citing Floss, 211 F.3d at 311). "[A]bsent a showing of fraud, duress, mistake, or some other ground upon which a contract may be voided, a court must enforce a contractual agreement to arbitrate." Haskins v. Prudential Ins. Co. of Am., 230 F.3d 231, 239 (6th Cir. 2000).

On a motion to compel arbitration:

The court has four tasks: first, it must determine whether the parties agreed to arbitrate; second, it must determine the scope of that agreement; third, if federal statutory claims are asserted, it must consider whether Congress intended those claims to be nonarbitrable; and fourth, if the court concludes that some, but not all, of the claims in the action are subject to arbitration, it must determine whether to stay the remainder of the proceedings pending arbitration.

Stout v. J.D. Byrider, 228 F.3d 709, 714 (6th Cir. 2000)

(internal citation omitted). After the court hears the parties:

[U]pon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement If the making of the arbitration agreement . . . be

in issue, the court shall proceed summarily to the trial thereof.

Great Earth Cos., Inc. v. Simons, 288 F.3d 878, 889 (6th Cir. 2002) (quoting 9 U.S.C. § 4).

The showing necessary to compel arbitration absent trial is the same as the showing necessary for summary judgment in a civil suit. Id. The moving party must "clearly and convincingly establish[] the nonexistence of any genuine issue of material fact, and the evidence . . . must be read in a light most favorable to the party opposing the motion." Kochins v. Linden-Alimak, Inc., 799 F.2d 1128, 1133 (6th Cir. 1986). In particular, the moving party must show the existence of "a binding agreement to arbitrate." In re First Thermal Systems, Inc., 182 B.R. 510, 513 (Bankr. E.D. Tenn. 1995).

If that showing is made, the burden shifts to the non-moving party to prove "that the claims at issue are unsuitable for arbitration." Green Tree Fin. Corp.-Ala. v. Randolph, 531 U.S. 79, 91 (2000). That requires evidence beyond mere allegations and denials. See Simons, 288 F.3d at 889 (internal citation omitted) ("In order to show that the validity of the agreement is 'in issue,' the party opposing arbitration must show a genuine issue of material fact as to the validity of the agreement to arbitrate.").

IV. Analysis

A. Whether the Parties Agreed to Arbitration

The parties do not dispute that they agreed to arbitrate certain claims arising from the Agreement. The Agreement's arbitration provision states:

The Parties agree that any controversy or other matter in question arising out of an indemnification claim, whether relating to a third party claim or a first party claim pursuant to ARTICLE VII, or otherwise involving the Transaction, that is not resolved following negotiations by the Parties (an "Unresolved Indemnification Claim") will be resolved through an arbitration administered by the American Arbitration Association ("AAA") in accordance with the Commercial Arbitration Rules of the AAA in effect as of the Effective Date, provided, however, that the dispute resolution procedures under this Section 8.2 shall not apply to any claim or controversy for which the party seeks specific performance or other equitable relief relating to the Transaction or the obligations under this Agreement. . . .

Either Party may seek to enforce the arbitration provisions in this Agreement by bringing an action to compel arbitration in a court of competent jurisdiction.

(Agreement, ECF No. 1-2 at 60-61.) The parties' dispute hinges on the scope of the arbitration provision.

B. Scope of Agreement to Arbitrate

The parties dispute whether the claims in the complaint fall within the scope of the Agreement's arbitration provision. Defendants argue that, because the complaint seeks monetary damages, Vanede's claims are subject to arbitration. (ECF No.

18-1 at 102.) Vanede contends that it seeks equitable relief, which is exempt from arbitration under the Agreement, and monetary damages in the alternative. (ECF No. 19 at 112.) Because Vanede's primary relief is equitable, Vanede argues that its claims are outside the scope of the arbitration provision. (Id.) Vanede also argues that the arbitration clause does not apply to its fraud claim. (Id. at 116.)

The Agreement exempts claims for equitable relief from arbitration: "the dispute resolution procedures under this Section 8.2 shall not apply to any claim or controversy for which the party seeks specific performance or other equitable relief relating to the Transaction or the obligations under this Agreement." (Agreement, ECF No. 1-2 at 60-61.)

The arbitration provision is limited to indemnification claims arising from ARTICLE VII, the indemnification provision, or otherwise involving the Transaction. (Agreement, ECF No. 1-2 at 56, 60.) Indemnification claims are limited to non-fraud claims against a contracting party and to non-equitable remedies:

[T]he Parties acknowledge and agree that their sole and exclusive remedy with respect to any and all claims (*other than claims arising from fraud on the part of a Party hereto in connection with the transactions contemplated by this Agreement*) for any breach of any representation, warranty, covenant, agreement or obligation set forth herein or otherwise

relating to the subject matter of this Agreement, shall be pursuant to the indemnification provisions set forth in this ARTICLE VII. . . . Nothing in this ARTICLE VII shall limit any Person's right to seek and obtain any equitable relief to which any Person shall be entitled.

(Id. at 59 (emphasis added).) Based on the Agreement's clear language, claims for fraud against a contracting party and claims seeking equitable relief are outside the scope of the arbitration provision.

The complaint alleges two causes of action: breach of contract and fraud in the inducement. It seeks rescission of the Agreement, and, in the alternative, compensatory monetary damages:

[P]laintiff demands judgment:

(1) Rescinding and cancelling the Agreement, returning the Schools to defendants and ordering Defendants to cancel the Note and refund the entire Purchase Price together with such other restitution as may be required to return the parties to the status quo ante; or

(2) Awarding plaintiff damages against defendants in such an amount as will be determined at trial to compensate plaintiff for the injuries caused by Defendants with such amount set off against any amount otherwise owed under the Note with the excess recovered by Plaintiff from Defendants;

(Compl., ECF No. 1 at 23-24 (emphasis added).)

'Rescission' is a court-ordered abrogation, nullification, termination, or voiding of a contract or agreement. Rescission operates to extinguish a contract that is legally valid but must be set aside due to fraud, mistake, or for some other reason to avoid unjust enrichment. It is a court-directed

unwinding of a contract, with the court applying equitable principles in an attempt to restore the status quo or place the parties in their respective positions prior to the contract.

12A C.J.S. Cancellation of Inst. § 1 (2017). Typically, rescission is granted in cases of mutual mistake, see, e.g., Robinson v. Brooks, 577 S.W.2d 207 (Tenn. Ct. App. 1978); or fraud, see, e.g., Richards v. Taylor, 926 S.W.2d 569, 572 (Tenn. Ct. App. 1996) (citing Birdsong v. Birdsong, 39 Tenn. 289 (Tenn. 1859)). Rescission may be granted for a breach of contract, "but depends on the gravity of the breach; [T]he general rule is that rescission will not be permitted for a slight or casual breach of the contract, but only for such breaches as are so substantial and fundamental as to defeat the object of the parties in making the agreement." Loveday v. Cate, 854 S.W.2d 877, 879 (Tenn. Ct. App. 1992) (quoting 17A C.J.S. Contracts § 422(1), Right to Rescind in General, p. 516).

Because fraud claims against a contracting party are exempt from arbitration, Vanede's fraud-in-the-inducement claim is outside the scope of the arbitration agreement. Because claims for equitable relief are exempt from arbitration, Vanede's breach-of-contract claim seeking equitable relief is outside the scope of the arbitration agreement. Defendants' Motion to Compel Arbitration of those claims is DENIED.

Vanede's breach-of-contract claim seeking monetary relief, however, falls squarely within the scope of the arbitration provision. To the extent that Vanede brings a claim for breach of contract seeking monetary relief, that claim is subject to arbitration. Defendants' Motion to Compel Arbitration of that claim is GRANTED.

C. Whether Stay of Nonarbitratable Claims Is Appropriate

Vanede's breach-of-contract claim seeking monetary damages is subject to arbitration. Its claim for equitable relief remains before the Court. To avoid legally inconsistent outcomes arising from Vanede's breach-of-contract claim, the claim for equitable relief is stayed pending the arbitration decision. See 9 U.S.C. §3.

D. Attorneys' Fees and Costs

Defendants seek attorneys' fees and costs incurred in bringing the Motion. (ECF No. 18-1 at 103.) The Agreement provides that "[e]ither Party may seek to enforce the arbitration provisions in this Agreement by bringing an action to compel arbitration in a court of competent jurisdiction. The prevailing Party in any such action to enforce the arbitration provisions of this

Agreement shall be entitled to recover its attorneys' fees and costs for such action." (Agreement, ECF No. 1-2 at 60.) Defendants sought to compel arbitration of all Vanede's claims and possible remedies. Defendants have prevailed in enforcing arbitration of one of the claims: Vanede's breach-of-contract claim seeking monetary damages. Defendants' motion for attorneys' fees and costs incurred in bringing the Motion is GRANTED.

V. Conclusion

For the following reasons, the Motion is GRANTED in part and DENIED in part. Defendants' motion for attorneys' fees and costs is GRANTED.

So ordered this 26th day of June, 2018.

/s/ Samuel H. Mays, Jr.
SAMUEL H. MAYS, JR.
UNITED STATES DISTRICT JUDGE