SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

Liquid Holdings Group, Inc.,	:	
Petitioner,	:	Memorandum of Law in Support of Petition for Stay Pursuant to CPLR ¶¶ 7502 and 7503(b)
-against-	:	
Gibson Dunn & Crutcher, LLP,	:	
Respondent.	:	Index No.

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Preliminary Statement

Petitioner Liquid Holdings Group, Inc. ("Liquid Holdings"), pursuant to New York Civil Practice Law and Rules ("CPLR") §§ 7502 and 7503, submits this Memorandum of Law in Support of its Petition to stay the arbitration of a fee dispute commenced by Respondent Gibson, Dunn & Crutcher, LLP ("Gibson Dunn"). Gibson Dunn claims that Liquid Holdings is required to arbitrate the fee dispute under its engagement letter (the "Engagement Letter"), but as detailed herein, the Engagement Letter does not govern the dispute, and Liquid Holdings cannot be forced to participate in the arbitration.

The Engagement Letter provides that fee disputes arising out the Engagement Letter must be submitted to arbitration. However, the Engagement Letter governs ***only*** legal services performed on behalf of Liquid Holdings or Liquid Holdings' affiliates. And the legal services that are the basis for the fee dispute at issue were performed on behalf of Liquid Holdings' Audit Committee, an autonomous entity established by Liquid Holdings' board of directors to investigate and oversee, among other things, Liquid Holdings' financial reporting obligations.

As detailed herein, the Audit Committee is not Liquid Holdings and it is not an affiliate of Liquid Holdings. Thus, the arbitration provision in the Engagement Letter does not apply to disputes arising out of services performed on behalf of Audit Committee. Accordingly, Liquid Holdings cannot be required to arbitrate the fee dispute, and the arbitration must be stayed.

Factual Background

The Engagement Letter

On or around July 2, 2012, the Engagement Letter was executed by Eduardo Gallardo of Gibson Dunn and Brian Ferdinand of Liquid Holdings. Engagement Letter at p. 4. The

Engagement Letter governs Liquid Holdings' retention of Gibson Dunn to perform legal services in connection with Liquid Holdings' proposed initial public offering as well as additional legal services performed on behalf of "Liquid Holdings, and any affiliate of Liquid Holdings...as to which [Mr. Ferdinand] represent[s] that [he] ha[s] authority to bind such affiliates to the terms of th[e] letter." Id.

The Engagement Letter mandates that Liquid Holdings and its affiliates agree to "binding arbitration...of any dispute claim or controversy regarding [Gibson Dunn's] services, including as to the fees for [Gibson Dunn's] services." Engagement Letter, at p. 3.

The Audit Committee

In July 2013, Liquid Holdings' Board of Directors established an audit committee (the "Audit Committee"). The Audit Committee was formed as an autonomous entity to investigate and oversee, among other things, the accounting and financial reporting processes of Liquid Holdings. Id. at § 2. Moreover, the Audit Committee has, "the authority to retain such outside counsel ... as it determines appropriate to assist it in the performance of its functions." Id. at § 2

The Audit Committee's Retention of Gibson Dunn

In February 2015, the Audit Committee retained Gibson Dunn to perform an investigation into alleged wrongful conduct involving one of Liquid Holdings' shareholders. Gibson Dunn never attempted to confirm that the Audit Committee was a party to the Engagement Letter.

Gibson Dunn submitted three invoices for services performed on behalf of the Audit Committee totaling nearly $1 million.

The Arbitration

On June 24, 2015, a scant two weeks after submitting its final invoice, Gibson Dunn submitted a Demand for Arbitration to Liquid Holdings seeking payment for legal services rendered to the Audit Committee. A copy of the Demand for Arbitration is attached to the Petition as Exhibit C. The Demand for Arbitration included a notice of claims made by Gibson Dunn (the "Notice of Claims"), which is attached to the Petition as Exhibit D.

Throughout the Notice of Claims, Gibson Dunn referred to Liquid Holdings and the Audit Committee as different parties. See Generally Notice of Claims. Moreover, in the Notice of Claims, Gibson Dunn acknowledged that, the Audit Committee – not Liquid Holdings – retained Gibson Dunn to perform the investigation. Notice of Claims ¶ 1 ("The Audit Committee of Liquid decided to retain [Gibson Dunn] to handle the Investigation."); see also Notice of Claims ¶ 12 ("[Gibson Dunn] was retained by Liquid's Audit Committee beginning on or about February 16, 2015 in connection with the investigation").

Furthermore, throughout the Notice of Claims, Gibson Dunn repeatedly acknowledged that it received instructions from and reported to the Audit Committee with respect to its investigation. E.g., Notice of Claims ¶ 14 ("During this time, [Gibson Dunn] regularly discussed with Liquid's Audit Committee and the Outside Auditor the scope of the Investigation and the process by which the Investigation would be conducted....[T]he Audit Committee...in at least two instances...informed [Gibson Dunn] that certain investigative steps [Gibson Dunn] was interested in pursuing were unnecessary given the circumstances."); ¶ 18 ("[T]he Outside Auditor requested that Liquid's Audit Committee authorize [Gibson Dunn] to perform additional work in connection with the Investigation...Liquid's Audit Committee authorized this additional

work that same day."); ¶ 23 ("[Gibson Dunn], upon receiving instructions from the Audit Committee, provided high-level interview summaries as well as a binder of representative documents of interest for review by the Outside Auditor.")

Liquid Holdings has not participated in the arbitration proceedings.

ARGUMENT

The Arbitration Should Be Stayed

The Court should stay the arbitration because the Engagement Letter does not require Liquid Holdings to engage in arbitration over disputes to which it is not a party. It is well settled that, "a party cannot be required to arbitrate unless there is affirmative evidence that the party expressly agreed to arbitrate its dispute in writing." Katz v. Albert, 68 A.D.3d 640, 640-41, 891 N.Y.S.2d 386 (1st Dep't 2009) (citation omitted) (affirming stay of arbitration where petitioners were not party to an agreement requiring arbitration); see also Matter of Riverdale Fabrics Corp., 306 N.Y. 288, 389 (1954) ("A party is not to be compelled to surrender his right to resort to the courts, with all of their safeguards, unless he has agreed in writing to do so and by clear and convincing evidence.") (citations omitted).

CPLR § 7503(b) provides that a party that "has not participated in the arbitration and who has not made or been served with an application to compel arbitration, may apply to stay arbitration." See CPLR § 7503(b). On a motion to stay arbitration pursuant to CPLR § 7503(b), "there are three threshold questions to be resolved by the courts: whether the parties made a valid agreement to arbitrate, whether if such agreement was made it has been complied with, and whether the claim sought to be arbitrated would be barred by limitation of time had it been asserted in a court of the State." County of Rockland v. Primiano Constr. Co., 51 N.Y.2d 1, 5-6

(1980); see also Sisters of St. John Baptist, Providence Rest Convent v. Phillips R. Geraghty Constructor, Inc., 67 N.Y.2d 997, 998, 502 N.Y.S.2d 997 (1986) ("It is of course for the court in the first instance to determine whether the parties have agreed to submit their disputes to arbitration and, if so, whether the disputes generally come within the scope of their arbitration agreement.") Thus, even if the parties have "a valid agreement to arbitrate" arbitration will be stayed if "the particular claim sought to be arbitrated is outside that scope [of the agreement]." Id.

To be enforceable, the language in an arbitration provision must be "clear, explicit and unequivocal." Katz 68 A.D.3d at 640-41. Moreover, when determining the scope of an arbitration provision, any ambiguity must be resolved against the party that drafted the agreement. PaineWebber Inc. v. Bybyk, 81 F.3d 1193, 1119 (1996) (citing Graff v. Billet, 64 N.Y.2d 899, 902, 487 N.Y.S.2d 733, 734–35, 477 N.E.2d 212 (1984)).

The arbitration provision in Gibson Dunn's Engagement Letter does not cover fee disputes between the Audit Committee and Gibson Dunn. By its own terms, the Engagement Letter governs ***only*** Gibson Dunn's representation of Liquid Holdings in connection with Liquid Holdings' initial public offering and additional legal services performed by Gibson Dunn on behalf of either (i) Liquid Holdings or (ii) Liquid Holdings' affiliates. Work performed on behalf of the Audit Committee does not fall into either of these categories.

In particular, the Audit Committee is composed of independent members of Liquid Holdings' board of directors, and is, by definition, an autonomous body that acts on its own accord. See In re BCE W., L.P., 7, at *2 (S.D.N.Y. Aug. 31, 2000) ("Because the Special Committee is a separate and distinct group from the Board of Directors, with separate legal

representation, the privilege afforded it is not the privilege of the corporation, but rather, is the privilege of the Special Committee.") For example, the Audit Committee has its own charter, and it was formed primarily to investigate and oversee the accounting and financial reporting processes of Liquid Holdings. In addition, the Audit Committee has the authority to retain its own outside counsel without input from Liquid Holdings. All of these factors make clear that the Audit Committee is a separate, independent entity from Liquid Holdings.

Gibson Dunn clearly recognizes the distinction between Liquid Holdings and its Audit Committee. In its arbitration filing with JAMS, Gibson Dunn adopted separate defined terms for Liquid Holdings and the Audit Committee.

Critically, Gibson Dunn's arbitration filing acknowledged that the Audit Committee – not Liquid Holdings – retained Gibson Dunn to perform the investigation. See Notice of Claims ¶ 1 ("The Audit Committee of Liquid decided to retain [Gibson Dunn] to handle the Investigation.").

In addition, Gibson Dunn repeatedly acknowledged in its arbitration filing that it reported to, and took its instructions from, the Audit Committee, not Liquid Holdings. E.g., Notice of Claims ¶ 14 ("During this time, [Gibson Dunn] regularly discussed with Liquid's Audit Committee and the Outside Auditor the scope of the Investigation and the process by which the Investigation would be conducted....the Audit Committee...in at least two instances...informed [Gibson Dunn] that certain investigative steps [Gibson Dunn] was interested in pursuing were unnecessary given the circumstances.").

Given these facts, it is clear that the Engagement Letter was not intended to cover work performed on behalf of the Audit Committee. The Engagement Letter was intended to cover an

initial public offering by Liquid Holdings years earlier. Gibson Dunn cannot come close to establishing the required "clear explicit, and unequivocal" proof that the Audit Committee ever agreed to arbitrate disputes with Gibson Dunn. See Katz v. Alpert, 68 A.D.3d at 641 (party will not be compelled to arbitrate "absent evidence which affirmatively evidences that the parties expressly agreed to arbitrate their disputes," and such agreement must be "clear, explicit and unequivocal.")

Similarly, the Court should not infer that the Audit Committee is an "affiliate" of Liquid Holdings as that term is used in the Engagement Letter. Black's Law Dictionary defines "affiliate" as "[a] corporation that is related to another corporation by shareholdings or other means of control; a subsidiary, parent, or sibling corporation." Likewise, the Internal Revenue Code defines an affiliate to include any entity in which the parent has at least an eighty percent ownership stake. 26 U.S.C. § 1504. The Audit Committee is not a parent, subsidiary or sibling of Liquid Holdings, and it is not an affiliate of Liquid Holdings. See id.

Gibson Dunn may argue that the Audit Committee should be considered an affiliate of Liquid Holdings because the Audit Committee is composed of Liquid Holdings board members. But, because the Engagement Letter, which was drafted by Gibson Dunn, does not unequivocally adopt such a broad definition of affiliate, the Court cannot infer such an inference. See Katz v. Alpert, 68 A.D.3d at 641; PaineWebber Inc. v. Bybyk, 81 F.3d at 1119 (1996) (citing Graff v. Billet, 64 N.Y.2d at 902.

In addition, even if the court finds that the parties intended to adopt a very broad definition of affiliate beyond that specified in the Engagement Letter, the only affiliates covered by the Engagement Letter were those for which Mr. Ferdinand represented that he could bind at

the time he executed the Engagement Letter. The Audit Committee was established ***after*** the Engagement Letter was signed. Clearly, Mr. Ferdinand could not bind an entity that did not yet exist.

Furthermore, even if the Audit Committee was an affiliate of Liquid Holdings, Mr. Ferdinand did not have the authority to bind the Audit Committee when the Audit Committee retained Gibson Dunn in February 2015. In fact, Mr. Ferdinand has not been an officer or director of Liquid Holdings since April of 2014. Moreover, Mr. Ferdinand has never been an independent director and thus never was a member of, or had the authority to bind, the Audit Committee under the Audit Committee Charter (which Gibson Dunn drafted).

If Gibson Dunn wanted to ensure that the Audit Committee was covered by its Engagement Letter, it could have sought confirmation from the Audit Committee. But, it failed to do so. Gibson Dunn cannot now benefit from its lack of diligence and faulty assumptions.

Thus, the Court should find that the legal services that Gibson Dunn performed on behalf of the Audit Committee were not covered by the Engagement Letter and that Liquid Holdings cannot be required under the Engagement Letter to arbitrate Gibson Dunn's dispute with the Audit Committee. Accordingly, the arbitration should be stayed.

Conclusion

For the reasons set forth herein, Liquid Holdings respectfully requests that the Court stay the arbitration proceedings.

Dated: New York, New York

July 6, 2015

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