

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

PRESENT: IRA GAMMERMAN, J.H.O.
Justice

PART 27

MARKSTONE CAPITAL PARTNERS, L.P.,

INDEX NO. 101085-2010

Petitioner,

MOTION DATE 00/

For a Judgment Pursuant to Article 75 of the CPLR
Staying Arbitration of a Certain Controversy

MOTION SEQ. NO. _____

-- against --

MOTION CAL. NO. _____

GIBSON, DUNN & CRUTCHER, L.L.P.,

Respondent.

The following papers, numbered 1 to _____ were read on this motion to/for _____

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

PAPERS NUMBERED

Answering Affidavits — Exhibits _____

Replying Affidavits _____

Cross-Motion: Yes No

*This motion + cross motion are
decided in accordance with the accompanying
memo decision.*

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IRA GAMMERMAN

Dated: 5/25/10

u
J. H. O.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

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MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

NYS SUPREME COURT E-FILED AS DOCUMENT # 274
6-11-2010

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 27

-----X
MARKSTONE CAPITAL PARTNERS, L.P.,

Petitioner,

Index No. 101085/2010
PC No. 23325

For a Judgment Pursuant to Article 75 of the CPLR

-against-

GIBSON, DUNN & CRUTCHER, L.L.P.,

Respondent.

-----X
HON. IRA GAMMERMANN, J.H.O.:

In this attorneys' fees dispute proceeding, petitioner moves, pursuant to CPLR 7503 (b), to stay arbitration. Respondent cross-moves, pursuant to CPLR 7503 (a), to dismiss the petition and to compel arbitration. For the reasons set forth below, the petition to stay arbitration is denied, and the cross motion to compel arbitration is granted.

Background

Petitioner Markstone Capital Partners, L.P. ("Markstone") is a Delaware limited partnership with its principal place of business in Los Angeles, California. Markstone operates a private equity investment fund that primarily does business in Israel. It is controlled by a general partner, non-party Markstone Capital Group, L.P., which, in turn, is controlled by its own general partner, non-party Markstone Capital, L.L.C.. The three managing members of Markstone Capital, L.L.C. are non-parties Elliott Broidy ("Broidy"), a resident of Los Angeles, California, and Amir Kess ("Kess") and Ron Lubash ("Lubash"), both residents of Israel. Respondent

Gibson, Dunn & Crutcher, L.L.P. (“Gibson Dunn”) is a an international law firm with headquarters in Los Angeles, California.

Pursuant to a retainer agreement, dated May 14, 2007 (the “first retainer”), Broidy retained Gibson Dunn to represent Broidy’s company, non-party Broidy Capital Management, and any subsidiaries thereof, in connection with a securities fraud investigation being conducted by the New York Attorney General (the “AG”). The retainer agreement provides that “all disputes, claims and controversies . . . arising out of this agreement” shall be submitted to arbitration by JAMS “in the principal city of the federal jurisdiction in which this agreement is entered into.”¹

On or about June 29, 2007, the AG’s office sent Markstone an informal request for information in connection with their fraud investigation. Gibson Dunn claims that as a result of this request, on July 17, 2007, it met with Broidy and Scott Gluck, Markstone’s Vice President and General Counsel, to discuss Markstone’s strategy in responding to the AG’s information request. Following that meeting, Gibson Dunn alleges that it was retained, along with another firm, Wachtell, Lipton, Rosen & Katz, to represent Markstone as co-counsel in the investigation.

In April 2008, in response to what it characterizes as a widening of the AG’s investigation, Gibson Dunn prepared a draft of a new retainer agreement for Broidy to sign, formalizing Gibson Dunn’s representation of Markstone. Broidy declined to sign the new agreement, on the grounds that Markstone Capital, L.L.C.’s operating agreement required all three managing members to agree on any decision concerning the company. Gibson Dunn then

¹ The first retainer also provides that, in the alternative, the parties may agree to submit a dispute to arbitration by the California State Bar Association.

prepared a second draft retainer agreement, dated August 18, 2009 (the “second retainer”), for Broidy, Kess, and Lubash to sign, which Broidy did sign, but Kess and Lubash did not. The second retainer agreement similarly provides that “all disputes, claims, or controversies . . . arising out of this agreement” shall be submitted to arbitration by JAMS “in the principal city of the federal district in which the agreement is entered into.” The agreement also specifically recites that it applies to Gibson Dunn’s representation of Markstone and any of its subsidiaries. Accompanying the second retainer is an engagement letter that begins, “ It has been our pleasure to have represented Markstone Capital Partners, L.P. [] as a client . . . since the inception of the investigation being conducted by the New York Attorney General’s office and other regulators in around May 2007.”

Although, as already noted, Kess and Lubash did not sign the second retainer agreement, they did, along with Broidy, sign an interim agreement prepared by Gibson Dunn, dated October 18 and 19, 2009 (the “interim agreement”). The one page agreement is not a retainer agreement with Gibson Dunn and does not contain an arbitration clause, but merely provides, in pertinent part, that:

1. [Markstone] retains Gibson, Dunn . . . to represent it in connection with investigations being conducted by the New York Attorney General, Securities and Exchange Commission, California Attorney General and any other state and federal regulators.
2. Markstone authorizes Gibson, Dunn . . . to continue to represent Elliott Broidy jointly with Markstone in the matters referred to above.

Gibson alleges that it represented Markstone until November 24, 2009. During the period from May 2008 to October 2009, Markstone Capital L.L.C. made \$976,510.35 in payments for

Gibson Dunn's legal services. Throughout this time, Gibson Dunn was in continuous contact with Markstone's Israeli counsel, Meir Linzen, who requested and received frequent status reports on the AG's investigation for the benefit of Markstone's Israeli-based managing members, Kess and Lubash.

In bringing the arbitration action, Gibson Dunn alleges that Markstone failed to pay it approximately \$1.3 million in attorneys' fees that accrued in the period ending November 24, 2009. Gibson Dunn served a demand for arbitration of its claim on JAMS in New York on or about December 24, 2009.² Although Markstone attempted to decline arbitration, JAMS commenced an arbitration proceeding on January 25, 2010. Markstone commenced the present proceeding to stay the JAMS arbitration by notice of petition and petition.

Discussion³

Markstone argues that there is no valid agreement to arbitrate between it and Gibson Dunn. As a general rule, a non-signatory to an arbitration agreement cannot be compelled to arbitrate a dispute, *Lerman v Russel*, 207 AD2d 746 (1st Dept 1994); *Matter of First Winthrop*

² Per the terms of the first retainer agreement, which Gibson Dunn claims governs this dispute, it appears that arbitration should have been commenced in Los Angeles, CA, rather than in New York, NY. However, the question of where the arbitration proceeding should be conducted is a question for the arbitrator to determine, not the court, *see Rockland County v Primiano Const. Co., Inc.*, 51 NY2d 1 (1980).

³ Although the first retainer agreement provides that it "shall be governed by the internal law . . . of the state of California," the parties have not raised the applicability of California law to this action, and have briefed the legal issues under New York state and federal law. Accordingly, the designation of California law is deemed waived, *see Cargill, Inc. v Charles Kowsky Resources, Inc.*, 949 F2d 51 (2d Cir 1991) ("even when the parties include a choice-of-law clause in their contract, their conduct during litigation may indicate assent to the application of another state's law.") citing *Walter E. Heller & Co. v Video Innovations, Inc.*, 730 F2d 50 (2d Cir 1984) (interpreting New York Law).

Props. (Carney), 177 AD2d 282 (1st Dept 1991). In the absence of an express agreement to arbitrate, the burden is on the party seeking to compel arbitration to establish a basis from which an intent to do so may be inferred, *see Marben Realty Co. v Sweeney*, 87 AD2d 561 (1st Dept 1982). That intent may be imputed to a non-signatory in five ways: incorporation by reference; assumption; agency; veil-piercing/alter ego; and estoppel, *Merrill Lynch Inv. Mgrs. v Optibase, Ltd.*, 337 F3d 125 (2d Cir 2003). A non-signatory may be estopped from denying an obligation to arbitrate if the non-signatory knowingly receives a direct benefit of an agreement containing an arbitration clause, *In re SSL Intern., PLC*, 44 AD3d 429 (1st Dept 2007); *HRH Const., LLC v Metropolitan Transp. Auth.*, 33 AD3d 568 (1st Dept 2006); *MAG Portfolio Consultant, GmbH v Merlin Biomed. Group*, 268 F3d 58 (2d Cir 2001). A benefit is considered direct if it “flow[s] directly from the agreement, while [a] benefit derived from an agreement is indirect where the nonsignatory exploits the contractual relation of parties to an agreement, but does not exploit (and thereby assume) the agreement itself [internal quotation marks and citation omitted],” *Republic of Ecuador v Chevron-Texaco Corp.*, 499 F Supp 2d 452 (SD NY 2007), *affd* 296 Fed Appx 124 (2d Cir 2008).

Here, Markstone willingly accepted Gibson Dunn’s legal services and Gibson Dunn rendered those services pursuant to its first retainer agreement with Broidy. Certainly, Gibson Dunn’s representation of Markstone before the New York Attorney General, and, later, the Securities and Exchange Commission, and other regulators and investigators, over the course of more than two years is a direct benefit of the first retainer agreement. The frequent status updates Gibson Dunn sent to Markstone’s Israeli counsel and managing partners are, similarly, direct benefits Markstone received as a result of the retainer agreement. Moreover,

correspondence between the parties throughout this period, and the payments Markstone remitted to Gibson Dunn for its services, demonstrate that Markstone not only took advantage of Gibson Dunn's representation but openly acknowledged the fact that it was doing so.⁴

Although not dispositive, I also note that New York regulations require that an attorney who undertakes to represent a client, and enters into any arrangement to collect fees thereby, "shall provide to the client a written letter of engagement before commencing the representation, or within a reasonable time thereafter . . . ," N.Y. Comp. Codes R.& Regs. tit. 22, §1215.1(a). Markstone's argument that Gibson Dunn, a large and experienced law firm, represented Markstone without any governing written terms for over two years is, therefore, unpersuasive, and the retainer agreement must be deemed to be the source of the governing terms of Markstone's representation.

As Markstone knowingly received legal services for over two years pursuant to Gibson Dunn's retainer agreement with Broidy, and derived direct benefits therefrom, it is estopped from now avoiding arbitration under that agreement, *see HRH Const., LLC v Metropolitan Transp. Auth., supra*, 33 AD3d 56; *Merrill Lynch Intern. Fin., Inc. v Donaldson*, 27 Misc 3d 391 (Sup Ct NY County 2010) ("a non-signatory who exploits a contract containing an arbitration clause is estopped from repudiating that clause"), citing *In Re SSL Intern., PLC*, 44 AD3d 429 (1st Dept 2007).

Based on the foregoing, it is not necessary to address Gibson Dunn's arguments that Markstone is bound by the terms of the retainer agreements based on agency and contract

⁴ I note, in passing, that, because the payments to Gibson Dunn were made by the L.L.C., all three managing members thereof would presumably had to have authorized those payments.

ratification principles.

Accordingly, it is

ORDERED and ADJUDGED that the petition to stay arbitration is denied, and the cross-motion to compel arbitration is granted.

The proceeding is dismissed.

This constitutes the decision and judgment of the Court.

Dated: 5/25/10, 2010

ENTER:



Hon. Ira Gammerman, J.H.O.

UNFILED JUDGMENT

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