Sobral v Burke
2014 NY Slip Op 32432(U)
September 12, 2014
Supreme Court, New York County
Docket Number: 651849/14
Judge: Jeffrey K. Oing

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL PART 48
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CARLOS SOBRAL,

Petitioner,

-against-

EDMUND BURKE, SUZANNE D. BURKE, and PRNUSA, LLC,

Respondents.

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Index No.: 651849/14
Mtn. Seq. Nos. 001, 002 & 003

JEFFREY K. OING, J.:

Petitioner, Carlos Sobral, moves, pursuant to CPLR 7503[a], to compel arbitration of certain claims asserted against respondents, Edmund Burke, Suzanne Burke, and PRNUSA, LLC (Mtn Seq. No. 002).

Respondents, by way of cross-petition, move, pursuant to CPLR 7503[b], to stay the underlying arbitration before the American Arbitration Association ("AAA"), and, pursuant to CPLR 3211[a][5], to dismiss the petition as barred by the doctrines of arbitration and award, res judicata, and collateral estoppel (Mtn Seq. No. 001). Respondents also seek, pursuant to 22 NYCRR § 130-1.1, the imposition of sanctions upon petitioner by arguing that the instant petition is frivolous. Justice Scarpulla granted respondents' application in their Order to Show Cause for a temporary stay of the underlying arbitration.

Petitioner moves for an order striking respondents' reply papers in support of their motion to stay arbitration on the ground that such papers were not permitted (Mtn Seq. No. 003).

For the reasons that follow, the petition is granted and the cross-petition is denied. The stay is hereby vacated, and the parties are hereby directed to proceed forthwith to arbitration, which shall include the preclusive effect, if any, of the Partial Final Award and Final Award made in the prior arbitration. Further, that branch of respondents' cross-petition for the imposition of sanctions and costs is denied. Petitioner's motion to strike respondents' reply papers is denied.

Background

In July 2009, the parties entered into an operating agreement for PRNUSA, LLC (Operating Agreement, Cross-Petition, Ex. A). The Burkes owned 50% of the company, and Sobral owned 50% (Id. at § 1.1[G]). Sobral agreed to design, manufacture, and ship jewelry to the company store in New York, which the Burkes operated (Id. at § 3.2). The Burkes managed the company's day-to-day operations, and Edmund Burke was the managing member (Id.). The parties also limited each other's liability. The agreement provides that the members must discharge their duties in good faith, and may not be liable to the company or each other except for "gross negligence or willful misconduct," unentitled financial benefits, distributions in violation of the agreement, and knowing violations of the law (Id. at § 6.4). With respect to acts or omissions on the company's behalf, the members may only be liable for "bad faith or ... wanton and willful

misconduct" (Id. at §6.5[C]). Any act in good faith based on a lawyer's advice or opinion is deemed not gross negligence or willful misconduct (Id. at § 6.4). The agreement also limits the members' remedies in case of disputes. The members must first proceed to non-binding mediation before JAMS Arbitration, Mediation, and ADR Services, Inc. ("JAMS," f/k/a Judicial Arbitration and Mediation Services) in New York County (Id. at § 11.4[A]). If the mediation fails, the members must then proceed to present their disputes to a single arbitrator of the American Arbitration Association ("AAA"), under AAA rules, for a binding arbitration (Id. at § 11.4[B]). The members irrevocably waived objections to the arbitrator's jurisdiction (Id.).

The company sold jewelry in retail stores in the New York metropolitan area, and wholesale all over the United States (Partial Final Award, Cross-Petition, Ex. B, pg. 2). The business was very successful from 2009 to 2011, and demand for Sobral's jewelry was high. Beginning in the summer of 2011, however, Sobral stopped responding to the Burkes' orders for inventory, preventing the Burkes from filling sales orders with customers (Id. at pp. 2-3). The Burkes tried to communicate with Sobral, but he ignored them. In order to mitigate the company's damages, the Burkes subleased the company's space.

Sobral alleged at the arbitration hearing that he thought the Burkes were mismanaging the company. During the summer of

2011, he hired Rene Duvekot as a consultant to evaluate the Burkes' management. The Burkes did not sign Duvekot's contract, but they gave him extensive access to evaluate them and their methods. On August 18, 2011, Duvekot advised Sobral that the Burkes were trustworthy. Sobral, however, continued avoiding the Burkes. He made no good faith attempt to rehabilitate either his relationship with the Burkes or the company's business (Id. at pp. 3-4). Indeed, the emails between the parties demonstrated that Sobral wanted to end his relationship with the Burkes (Id.).

Procedural Posture

In September 2011, the Burkes filed a Request for Mediation with JAMS (Cross-Petition, ¶ 12). The Burkes allege that Sobral ignored all attempts to get him to participate (Id. at ¶ 13). The Burkes then filed a Demand for Arbitration with JAMS. Sobral responded by commencing a lawsuit against the Burkes in federal court in Florida to dissolve the company. On March 12, 2012, the District Court granted the Burke's motion to compel arbitration, and transferred the matter to the federal court in the Southern District of New York (Id. at ¶ 15). Two months later, Sobral voluntarily discontinued the Florida action (Id. at ¶ 17).

The Burkes in March 2012 commenced a AAA arbitration, which was assigned to Hon. George D. Marlow (Id. at ¶¶ 18-19). After motion practice and seven days of testimony, Judge Marlow issued a Partial Final Award on August 6, 2013. In that award, Judge

Marlow found in favor of the Burkes and awarded them $1,794,500 plus 3% interest per year from the filing date (Partial Final Award, Petition, Ex. B). In that regard, Judge Marlow found that Sobral acted in bad faith by, inter alia, refusing to communicate with the Burkes and refusing to fill product orders, as well as refusing to mediate and attempting to avoid arbitration (Id. at pg. 5-7). Sobral moved to reopen the arbitration proceeding, but Judge Marlow denied his motion (Arbitration Decision, Cross-Petition, Ex. C). On December 31, 2013, Judge Marlow issued a final award ordering Sobral to pay most of the legal fees for the federal action, the fees incurred as a result of the motion to reopen, and half of the arbitration costs for a total of $75,501.15 (Final Award, Cross-Petition, Ex. D).

The Burkes petitioned this Court to confirm Judge Marlow's Partial Final Award and Final Award (Index No. 650147/2014). Sobral opposed the petition on the grounds that Judge Marlow exceeded his power. After oral argument on June 26, 2014, this Court granted the petition and confirmed the Partial Final Award and Final Award (Transcript of 6/26/14 Proceedings, Cross-Petition, Ex. E, pp. 40-44).

While that proceeding was pending, Sobral made a demand for arbitration on the Burkes and PRNUSA (Demand for Arbitration, Petition, Ex. A). Sobral asserted six claims: breach of contract for failing to indemnify him pursuant to section 6.5 of the

agreement; breach of contract for selling jewelry outside of New York and leasing property without his consent; breach of contract against Edmund Burke for allegedly co-mingling his assets, mismanaging inventory, and failing to account to the members; breach of contract against Edmund Burke for operating as managing member without holding an annual meeting; breach of fiduciary duty against Edmund Burke for the same reasons; as well as confirming the prior awards on his own behalf rather than PRNUSA's; and common law trademark infringement (Id. at pp. 4-5). He sought damages, and declaratory and injunctive relief (Id. at pp. 5-6).

Discussion

Initially, Sobral argues that the claims against PRNUSA must proceed to arbitration regardless of the Court's decision with regard to the Burkes because the award was confirmed in their name only. As this Court has previously held, Judge Marlow's decisions made a clear distinction between the Burkes and PRNUSA, all of whom were parties to the arbitration (Transcript of 6/26/14 Proceedings, Cross-Petition, Ex. E, pp. 14-16). Sobral's argument that PRNUSA is not bound by the Prior Award is therefore unsupported in the record, and he cites no authority in support of his argument that the final award cannot be preclusive of his current claims against PRNUSA. Accordingly, any preclusive

effect of the prior arbitration Awards is equally applicable to all respondents.

I. Preclusion

Collateral estoppel forbids relitigating issues where "the identical issue [was] decided in the prior action and [is] decisive of the present action, and ... the party to be precluded from relitigating the issue must have had a full and fair opportunity to contest the prior determination" (Sepulveda v Dayal, 70 AD3d 420, 421 [1st Dept 2010]). Similarly, the doctrine of "arbitration and award" applies to bar future adjudication of issues or claims "actually litigated, squarely addressed[,] and specifically decided" in a prior arbitration (Genger v Genger, 87 AD3d 871, 873 [1st Dept 2011]).

Res judicata applies to bar new claims "based upon the 'same transaction or series of connected transactions' ... if: (i) there is a judgment on the merits rendered by a court of competent jurisdiction, and (ii) the party against whom the doctrine is invoked was a party to the previous action, or in privity with a party who was" (People ex rel. Spitzer v Applied Card Sys., Inc., 11 NY3d 105, 122 [2008]). With respect to arbitration awards, however, res judicata only bars claims "actually contested and therefore determined by the award, including all matters reasonably comprehended in the dispute

submitted to the arbitrators" (Cine-Source, Inc. v Burrows, 180 AD2d 592, 594 [1st Dept 1992]).

The parties vigorously and sharply dispute what was and was not covered by Judge Marlow's decisions. A review of the Partial Final Award and the Final Award demonstrates that several of the issues raised in Sobral's demand for arbitration were clearly raised, discussed, and decided against him in the prior arbitration proceeding. Specifically, the record reflects that the issues of Sobral's good faith (Partial Final Award, Cross-Petition, Ex. B, pg. 3-5; Transcript of 6/26/14 Proceedings, Cross-Petition, Ex. E, pp. 40-44) and reliance on advice of counsel (Transcript of 6/26/14 Proceedings, Cross-Petition, Ex. E, pg. 27) were flatly rejected both by Judge Marlow and by this Court in confirming the prior Award. Sobral's claims that the Burkes breached the operating agreement through Edmund Burke's alleged mismanagement, by leasing the New York retail space to mitigate their damages, by failing to order new jewelry, and by violating certain unidentified laws (Demand for Arbitration, Petition, Ex. A, pp. 4-5), were already raised and decided against Sobral by Judge Marlow (Partial Final Award, Cross-Petition, Ex. B, pp. 3, 5-7). Nonetheless, whether the prior Award collaterally estops Sobral from asserting his present claims is an issue for the arbitrator.

New York law reserves for the arbitrator the issue of an arbitration award's preclusive effect on a subsequent arbitration arising out of the same arbitration agreement (see In re Falzone (New York Cent. Mut. Fire Ins. Co.), 15 NY3d 530, 534 [2010]["The effect, if any, to be given to an earlier arbitration award in subsequent arbitration proceedings is a matter for determination in that forum"]; Warner Bros. Records, Inc. v PPX Enterprises, Inc., 7 AD3d 330 [1st Dept 2004]["Arbitrators retain exclusive authority to preclude re-arbitration of issues previously decided"]; Port Auth. of New York and New Jersey v Port Auth. Police Sergeants Benev. Ass'n, 225 AD2d 503 [1st Dept 1996]["the res judicata effect, if any, of an earlier administrative proceeding on the arbitration respondent now seeks is a matter for determination by the arbitrator"]).

Mew Equity LLC v. Sutton Land Servs., L.L.C., cited by the Burkes for the opposite position, is distinguishable. That case dealt with the res judicata effect of a prior arbitration on a subsequent plenary action, not an arbitration (Mew Equity LLC v. Sutton Land Servs., L.L.C., 37 Misc 3d 1225(A) [Sup Ct, NY Cty 2012]; see also Port Auth. of New York and New Jersey, 225 AD2d 503 [1st Dept 1996] ["To the extent that prior cases of this Court [hold] that disputes otherwise arbitrable are not to be sent to arbitration unless the court first finds that a prior arbitration or administrative proceeding has no res judicata

effect, we decline to follow them"]). Thus, whether and to what extent the prior arbitration precludes any or all of Sobral's present claims sought to be arbitrated is to be determined by the arbitrator.

Accordingly, that branch of the Burkes' cross-petition to dismiss Sobral's petition on preclusion grounds is denied.

II. Permanent Stay or Compel Arbitration

On a petition to compel arbitration, a Court may only determine "whether a valid agreement was made or complied with, and [whether] the claim sought to be arbitrated is not barred by limitation" (CPLR 7503[a]). To stay an otherwise arbitrable dispute, a party must show "sufficient facts to establish justification for the stay" (AIU Ins. Co. v Cabreja, 301 AD2d 448, 449 [1st Dept 2003]). In other words, a party must show "that there is a genuine preliminary issue, which requires a trial" (Natl. Grange Mut. Ins. Co. v Diaz, 111 AD2d 700 [1st Dept 1985]).

Here, the record demonstrates that there is a valid agreement to arbitrate between the parties, that Sobral complied with the agreement, and that none of the claims -- breach of contract, breach of fiduciary duty seeking equitable relief, and common law trademark infringement -- subject to the six year statute of limitations (CPLR 213) -- are time-barred. Sobral commenced mediation pursuant to section 11.4 of the operating

agreement, which the Burkes and PRNUSA refused to participate in (Petition, ¶ 26). He then commenced an arbitration proceeding in accordance with the same section (Id.; Demand for Arbitration, Petition, Ex. A).

Accordingly, the petition to compel arbitration is granted, and that branch of the Burkes' cross-petition for a permanent stay of the underlying arbitration is denied.

III. Sanctions

22 NYCRR § 130-1.1 provides that a Court may award sanctions and costs in response to frivolous conduct by a party. The Burkes' complain that Sobral's demand for arbitration and petition to compel arbitration are frivolous because they are "completely without merit in law and cannot be supported by a reasonable argument for an extension, modification or reversal of existing law" (22 NYCRR § 130-1.1[c][1]). As the discussion, supra, shows, Sobral's application is not completely without merit. Accordingly, that branch of the Burkes' cross-petition for the imposition of sanctions is denied.

Accordingly, it is hereby

ORDERED that the petition to compel arbitration is granted, and the parties are hereby directed to proceed to arbitration; and it is further

ORDERED that the temporary stay of the underlying arbitration is hereby vacated; and it is further

ORDERED that branch of the cross-petition to dismiss the petition pursuant to CPLR 3211[a][5] is denied; and it is further

ORDERED that branch of the cross-petition for a permanent stay of the underlying arbitration is denied; and it is further,

ORDERED that branch of the cross-petition for the imposition of sanctions and costs, pursuant to 22 NYCRR 130-1.1, is denied; and it is further

ORDERED that petitioner's motion to strike respondents' reply papers is denied.

This memorandum opinion constitutes the decision and order of the Court.

Dated: 9/12/14

HON. JEFFREY K. OING, J.S.C.