SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 54

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PETRIDES & CO. LLC,

Index No.: 655849/2018

Petitioner,

DECISION & ORDER

-against-

YORKTOWN PARTNERS LLC, YORKTOWN ENERGY PARTNERS IV, LP, YORKTOWN ENERGY PARTNERS V, LP, YORKTOWN ENERGY PARTNERS VI, LP, YORKTOWN ENERGY PARTNERS VII, LP, YORKTOWN ENERGY PARTNERS VIII, LP, YORKTOWN ENERGY PARTNERS IX, LP, YORKTOWN ENERGY PARTNERS X, LP, and YORKTOWN ENERGY PARTNERS XI, LP,

Respondents.

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JENNIFER G. SCHECTER, J.:

Petitioner Petrides & Co. LLC (Petrides) moves to compel respondents Yorktown Partners LLC (Partners), Yorktown Energy Partners IV, LP, Yorktown Energy Partners V, LP, Yorktown Energy Partners VI, LP, Yorktown Energy Partners VII, LP, Yorktown Energy Partners VIII, LP, Yorktown Energy Partners IX, LP, Yorktown Energy Partners X, LP, and Yorktown Energy Partners XI, LP (collectively, Yorktown) to arbitrate claims under a contract to which Yorktown is not a signatory, arguing that the direct benefits theory of estoppel subjects Yorktown to that contract's arbitration clause. Yorktown opposes, arguing that this doctrine does not apply. The petition is granted.

Partners, a private equity firm that specializes in energy investments, manages the other Yorktown respondents. Yorktown collectively owns at least 90% of non-party Riley

Exploration Group LLC (Riley). Yorktown has complete control of Riley because it controls the majority of Riley's board of directors.

Petrides and Riley are parties to a letter agreement dated February 1, 2015, pursuant to which Riley engaged Petrides to perform consulting services (Dkt. 4 at 2 [the Agreement]; *see id.* at 3 [Petrides' "services provided as a consultant pursuant to this [Agreement] will include, as requested by Riley from time to time, reviewing such information as is reasonably required to effectuate a Transaction in which Riley acquires and operates the business of one or more potential target entities"]). Yorktown is not a party to the Agreement, nor does the Agreement require Petrides to provide services to Yorktown. On the first page of the Agreement, it states that "[t]he Parties acknowledge that George Petrides and/or [Petrides] have performed and ***may in the future*** perform various consulting services on behalf of entities affiliated with Riley ***or with Yorktown Energy Partners***" (*see id.* at 2 [emphasis added]). Paragraph 9(D) of the Agreement, titled "Limitation of Engagement to Riley," provides that "Riley agrees that [Petrides] ***has been retained to act solely as advisor to Riley***, and not as an advisor to or agent of any other person, and that Riley's engagement of [Petrides] is not intended to confer rights upon any person not a party hereto (***including security holders***, employs or creditors of Riley) as against [Petrides] or its Affiliates, or their respective representatives" (*id.* at 10 [emphasis added]). "Affiliates" is defined in paragraph 9(J) to "mean any other entity directly or indirectly controlling, controlled by, or under common control with such entity" (*id.* at 11).

The Agreement is governed by New York law (*id.* at 10). In paragraph 9(I), Petrides and Riley agreed that all of their disputes related to the Agreement are subject to mandatory arbitration (*id.* at 11). Petrides and Riley are currently arbitrating disputes under the Agreement related to services provided by Petrides between January 2015 and May 2017 in connection with at least seven projects, which are discussed at length in the affidavit of George Petrides (Dkt. 3).[1] Petrides, however, also wishes to arbitrate its disputes with Yorktown related to the Agreement. In October 2018, Petrides served an arbitration demand on Yorktown, which Yorktown rejected because it was not a signatory to the Agreement. In November 2018, Petrides filed this petition to compel Yorktown to arbitrate.

The Federal Arbitration Act (FAA) applies because the parties' business dealings affect interstate commerce (*Cusimano v Schnurr*, 26 NY3d 391, 400 [2015], *see Mahn v Major, Lindsey, & Africa, LLC*, 159 AD3d 546 [1st Dept 2018]).[2] "The FAA reflects the fundamental principle that arbitration is a matter of contract" (*Rent-A-Ctr., W., Inc. v Jackson*, 561 US 63, 67 [2010]). Under both the FAA and New York law, ordinarily, only signatories to a contract containing an arbitration agreement can be compelled to arbitrate (*TBA Global, LLC v Fidus Partners, LLC*, 132 AD3d 195, 202 [1st Dept 2015];

[1] The facts alleged in Mr. Petrides' affidavit are not contested by Yorktown, which did not submit an affidavit in opposition; thus, his factual account is deemed admitted (*Funk v Seligson, Rothman & Rothman, Esqs.*, 165 AD3d 429, 430 [1st Dept 2018]; *see Ferluckaj v Goldman Sachs & Co.*, 12 NY3d 316, 325 [2009]).

[2] Petrides' affidavit describes services performed in connection with projects in multiple states, such as Texas.

see Monarch Consulting, Inc. v Nat'l Union Fire Ins. Co. of Pittsburgh, PA, 26 NY3d 659, 665 [2016]).[3] There are, however, various exceptions to this rule (*see TNS Holdings, Inc. v MKI Sec. Corp.*, 92 NY2d 335, 339 [1998]). Only one exception applies here: "the direct benefits theory of estoppel" (*Belzberg v Verus Investments Holdings Inc.*, 21 NY3d 626, 631 [2013] [adopting doctrine from federal law and citing federal cases]). Under this doctrine, "a nonsignatory may be compelled to arbitrate where the nonsignatory 'knowingly exploits' the benefits of an agreement containing an arbitration clause, and receives benefits flowing directly from the agreement" (*id.*). Where "the benefits are merely 'indirect,' a nonsignatory cannot be compelled to arbitrate a claim" (*id.*). "A benefit is indirect where the nonsignatory ***exploits the contractual relation of the parties, but not the agreement itself***" (*id.* [emphasis added], citing *MAG Portfolio Consultant, GMBH v Merlin Biomed Grp. LLC*, 268 F3d 58, 61 [2d Cir 2001]; *see Kramer Levin Naftalis & Frankel LLP v Cornell*, 148 AD3d 430 [1st Dept 2017]).

Petrides contends that it provided a direct benefit to Yorktown under the Agreement – the settlement of the "Dernick Dispute" (*see* Dkt. 5 at 18).[4] Mr. Petrides, whose affidavit is uncontroverted, explains this dispute:

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[3] Where "as here, the parties dispute not the scope of an arbitration clause but whether an obligation to arbitrate exists," the general presumption in favor of arbitration does not apply" (*Oxbow Calcining USA Inc. v Am. Indus. Partners*, 96 AD3d 646, 649 [1st Dept 2012]; *see Applied Energetics, Inc. v NewOak Capital Markets, LLC*, 645 F3d 522, 526 [2d Cir 2011] ["because the parties dispute not the scope of an arbitration clause but whether an obligation to arbitrate exists, the presumption in favor of arbitration does not apply"]).

[4] Yorktown's ownership and control of Riley, without more, would not warrant compelling arbitration (*see* Dkt. 13 at 9-10 [collecting cases]).

In or about 2002, ***Yorktown*** (via Yorktown Energy Partners V) invested approximately $40 million in Dernick Resources, Inc. ("DRI") for acquisition of oil and gas properties in the Arkoma basin in Texas. In 2007, Yorktown Energy Partners VIII invested another $18 million in DRI, together with another $2 million from outside minority investors. Cinco Resources, Inc. ("Cinco"), like Riley, was an oil and gas company formed by Yorktown in 2002 around oil and gas executive Jon Glass who became its Chief Executive Officer. …

In 2009, via an exchange of shares with Yorktown and the minority investors in DRI, Cinco acquired approximately 85% of DRI. In connection with the exchange of shares, Cinco invested another $50 million in DRI through a preferred stock offering, pursuant to which the "Dernick Group" … were given the right to participate to avoid dilution of their ordinary shares of DRI. Subsequently, between 2009 and 2010, at a time when Cinco required additional capital to invest in additional oil and gas properties at Yorktown's direction a new company called Cima Resources Inc. ("Cima") was formed and capitalized with a $40 million investment with which Cima purchased Cinco's oil and gas property in Eagle Ford, South Texas. In 2011, the Dernick Group asserted a claim that Cinco, ***via Yorktown***, had acted improperly by selling the Eagle Ford property to Cima, thereby diluting the value of the Dernick Group's shares in Cinco, while at the same time failing to offer the Dernick Group any participation in the Cima investment. In November 2011, Cima was merged into Cinco.

In January 2012, Cinco began the process of an IPO. During February and March of 2012, the Dernick Group had settlement communications ***with Yorktown and Cinco*** regarding their dilution claim and participated in an unsuccessful mediation in New York in March 2012. In April 2012, Yorktown suspended the Cinco initial public offering process. The dispute between the Dernick Group, Cinco and Yorktown continued, culminating in arbitration as well as a lawsuit initiated by Yorktown in Texas, I was told. Settlement discussion between Yorktown's Lawrence and the Dernick Group's Stephen Dernick were ongoing over some years but they were unable to achieve a resolution. Cinco executives were not involved in these discussions.

[In February 2015], Yorktown directed Riley to engage [Petrides] under the [Agreement]. ***Yorktown*** directed [Petrides] to manage settlement of the dispute with the Dernick Group ***and such work was performed by [Petrides] pursuant to the [Agreement]. Importantly, Riley – [Petrides] contractual counterparty under the [Agreement] – had no interest or***

stake in the Dernick Group litigation; this was solely a dispute between the Dernick Group, Cinco and Yorktown (and its executives). Settling this dispute was important to Yorktown, and its executives, because this multi-year dispute was taking up valuable executive time and causing Yorktown and Cinco to incur significant legal expenses. ***[Petrides] negotiated over a period of several months with the Dernick Group*** and presented terms to Yorktown executives Lawrence and Keenan, pursuant to which a settlement was eventually achieved in April, 2015. At all times during the settlement negotiations with the Dernick Group, ***[Petrides] was acting on behalf of Yorktown and its executives, notwithstanding that the work was being performed under the [Agreement]***.

Prior to [Petrides'] involvement, the Dernick Group, Cinco and Yorktown had been in discussions regarding the purchase of the Dernick Group's interests in the Champions oil and gas field, which was situated in Yoakum County, Texas. Yoakum County is part of the Permian Basin, the most prolific oil producing area in the United States. The acquisition of the Champions field was an integral part of the settlement agreement negotiated by [Petrides]. Although Cinco would have been the natural party to acquire the Champions interest - since the original dispute with the Dernicks was with Cinco - Yorktown decided that it would rather have Riley purchase the Champions interest. ***Thus, when [Petrides] was engaged under the [Agreement], the potential acquisition of the Champions field by Riley is mentioned at paragraphs 4(B)(1) as a project to be accomplished by [Petrides], pursuant to which it would be compensated according to the terms stated therein*** [*see* Dkt. 4 at 5].

Ultimately, as part of the settlement of the Dernick dispute, in March 2016 Riley purchased from the Dernick Group their interests in the Champions field at values per acre that may have been higher than transactions among other parties at the time. Notably, ***although Riley had no interest in the Dernick Group litigation, it was utilized by Yorktown as the funding mechanism for the settlement, which was structured around Riley purchasing the Dernick Group's interests in the Champions field at a potentially high valuation***. In addition to settling the multi-year dispute with the Dernick Group, ***this purchase proved to be beneficial for Yorktown***, as the Champions field was eventually made into the core asset of a company to be taken public, that is, the "Permian JV" … and thereby potentially offset the losses mentioned above. [Petrides] was compensated for its services by Riley pursuant to the [Agreement], although [Petrides] performed all work at the direction of, and for the benefit of, Yorktown and

> its executives .... (Dkt. 3 at 8-12 [citations omitted; emphasis added; paragraph numbering omitted; breaks added for clarity]).

Petrides argues that without its "services provided under the [Agreement] ... [Yorktown] would not have settled the Dernick Dispute nor would they have been able to structure Riley and their other failed portfolio investments into the Permian JV in order to directly recoup their losses," and that it "is this direct benefit that [Yorktown] derived from [Petrides'] work under the [Agreement] for which [Petrides] seeks recovery in the arbitration" (Dkt. 5 at 20).

Yorktown does not meaningfully respond to this argument. In fact, Yorktown mentions the Dernick Dispute only once (*see* Dkt. 13 at 10) and does not explain why the benefits it received in connection with it did not flow from the Agreement. To the extent Yorktown claims "none of these purported 'benefits' [related to the Dernick Dispute] is contemplated under the [Agreement]" (*see id.*), Yorktown ignores paragraph 4(B)(1) and Mr. Petrides' discussion of how that paragraph establishes that Yorktown was expected to (and indeed) did receive a benefit from the Agreement. Yorktown did not submit an affidavit from someone with personal knowledge refuting Mr. Petrides' account of the context of the Dernick Dispute. Likewise, Yorktown does not refute that "resolution of the Dernick Dispute, carried out by Petrides in its capacity as a Yorktown-directed consultant, solely benefited Yorktown as Riley was not involved in the dispute" and that Yorktown used "Riley as a funding mechanism for the settlement of the Dernick Dispute" (Dkt. 17 at 8).

On this record, Petrides demonstrated that Yorktown knowingly exploited the benefits of the Agreement, which contained the arbitration provision, and that it received the benefits of Petrides' work under the Agreement. Petrides showed that benefits intentionally inured to Yorktown directly from Petrides' performance under the Agreement and were not merely the byproduct of the relationship between Petrides and Yorktown. To be sure, while the Agreement indicates that Petrides and Yorktown had a broader business relationship, the undisputed facts show that the work performed by Petrides in connection with the Dernick Dispute specifically benefited Yorktown and was done, as contemplated by paragraph 4(B)(1), specifically under the auspices of the Agreement. The court, therefore, finds that Yorktown received a direct benefit from the Agreement and, consequently, is subject to its arbitration clause.

Accordingly, it is ORDERED and ADJUDGED that Petrides' petition to compel arbitration against Yorktown is granted and Yorktown must arbitrate disputes related to the Agreement. This is the decision and judgment of the court.

Dated: January 18, 2019

ENTER:

Jennifer G. Schecter, J.S.C.